

DERBYSHIRE COUNTY COUNCIL

CABINET

3 April 2012

Report of the Director of Finance

**LOCAL GOVERNMENT RESOURCES REVIEW PHASE ONE
- GOVERNMENT RESPONSE
(FINANCE AND MANAGEMENT)**

1 Purpose of the Report

To provide Members with details of the Government's response to the first consultation on the Local Government Resources Review (LGGR) - Phase One.

2 Information and Analysis

The Government published a consultation on the future funding of local authorities on 18 July 2011. Proposed changes primarily focussed on the ability of local authorities to retain either all or a proportion of the business rates income in their area. The Council responded to this consultation and details of the response were reported to Cabinet Member – Finance and Management on 5 December 2012. The Council's main concerns included:

- The size and purpose of the set aside.
- Funding baseline ie the use of the damped formula grant allocations
- Lack of correlation between business rates growth and service needs.

On 19 December the Government confirmed its intention to push ahead with reforms to the way in which local authorities are funded.

The Government have confirmed that there will be no changes to the way in which business rate bills are calculated, properties are valued or the method by which bills are set. National discounts and rates relief will also continue.

The Local Government Finance Bill will be introduced to parliament and will provide the legislative changes required for the Business Rates Retention Scheme to come into effect from April 2013.

As expected the exact design of the rates retention system will continue to be developed and published in secondary legislation. However, the Government have confirmed the following:

The Central Share (formerly the Set-Aside)

The Government's response to the LGRR announced a change in the way that the set-aside will be calculated.

In order for the Government to manage the scheme within the Spending Review (SR) totals and meet the deficit reduction programme the original consultation said that the set-aside would be worked out as the difference between the SR totals and the forecast national business rates – set at the largest figure (in the early years, using the latest year of the spending review). This would enable the top-up and tariff to remain fixed whilst any excess in the set aside amount would be returned to local government as a general grant.

In replying to the consultation many local authorities, raised concerns that this meant that local authorities would only be able to benefit from growth above the national forecast.

Whilst the Government are keen to remain within the control totals set out in the Spending Review, there will be a moderate change to the calculation of the set -side. They will now set a proportion of shares rather than a cash amount. For example, billing authorities may have to pay 25% of their collected rates to Government (the Central Share) and then the remaining 75% (the Local Share) will be divided amongst tiers and/or fire authorities before being subject to tariffs, top-ups, levies and safety nets.

The result of this, is that Government shares the risk of businesses growing below forecast levels. But it will also share in the benefits of growth above the forecast levels.

As before, all the business rates which gets paid to Central Government will be returned in full to local government.

The Business Rates Baseline

The Business Rates Baseline for an individual authority will be established on the basis of an average of its rates income over a number of years. The number of years and the data to be used will be consulted on further later this year.

The Baseline Funding Level will be ascertained using the 2012/13 formula grant process and applying it to the 2013/14 and 2014/15 Spending Review control totals. The Government's response to the consultation acknowledges the problems and concerns with the current

method of formula grant distribution. However the Government remain committed to their plans as the most stable route.

In setting the Baseline Funding the Government will also update current datasets (including the possibility of using population figures from the 2011 Census), in addition to making “limited technical adjustments” for the cost of rural services and concessionary fares. The Government may also wish to re-examine the Resource Equalisation.

The Baseline Funding will also include the 2011/12 Council Tax Freeze Grant but exclude both the 2012/13 Freeze Grant and the Transition Grant (introduced to take account of reductions to spending power) as these are both one-off payments.

The consultation paper sought views on whether this baseline should use damped or raw formula grant figures. The responses were mixed but the Government has decided to use damped formula grant figures for stability reasons. The paper also confirms that the Government will not be phasing out damping as it will add significant complexities to the system and distort the incentive effect.

There will be no changes to the tailored grants distribution.

Tariffs and Top-ups

Authorities who collect more rates than they currently receive in formula grant will pay the difference to central government as a *tariff*, and those who collect fewer rates than their formula grant funding will receive the shortfall in the form of a *top-up* from central government. The tariff and top-up should be self-funding. The tariff and top-ups are intended to be fixed until a reset, although they will be linked to inflation.

The Paper states that the result will be that top-up authorities (for example; all county councils in two-tier areas) will not have their business rates income eroded in real terms and the tariff authorities will face a very strong incentive for growth.

It is through the use of tariffs and top-ups that the Government are using, to support their statement that no authority will be disadvantaged by their starting rates position – despite the acknowledged difference in the incentive effect between tariff and top-up authorities.

Growth

Councils will be able to keep x% of their rates – this will be known as the *local share*. The Government will retain discretion over the varying of this figure, in order to “*protect the interests of taxpayers and the wider economy*”.

The Levy

Under the Rates Retention Scheme, some authorities could gain significantly more than others from the basic tariff and top up arrangements. The Government therefore proposes to recover 'disproportionate' benefit through a levy.

The Government has chosen to use the proportionate levy. This sets a ratio between increase in rates and increase in spending power.

A proportional levy that seeks to ensure that there is a fixed relationship between increases in business rates and retained income - for example, an x% increase in collected rates would mean no more than an x% increase in income.

The Safety Net

The Safety Net will ensure that no authority sees their income fall below a set percentage below their baseline. For the purpose of the operation of the safety net the baseline will be increased annually by the Retail Price Index. The percentage level which would trigger the use of the safety net will be consulted on in 2012.

The paper states that it is intended that the safety net should be funded by the levy but that in the early years of the scheme Government will ensure that there are "*sufficient funds available to provide support to all authorities who meet the safety net criteria, regardless of the level of levy income*". In future years, it may be the case that Government scales back any safety net payments in order to keep it affordable. The paper says that this would be a last resort.

Any excess monies built up through the proceeds of the levy would be redistributed back to local government. Central Government will consult on the basis for redistribution.

Resets

If it is felt that resources no longer sufficiently meet service pressures within individual local authority areas (eg due to population changes), the Government could reset the system by balancing resources.

Resets will occur every ten years but in exceptional circumstances a reset could be called earlier.

Two-Tier Areas

In two-tier areas, Government considers that the lower tier has the greatest control over business growth and as such want to place the greatest reward/risk with them. Districts will therefore keep 80% of the growth in their areas.

The result is that county councils will all become top-up authorities – enabling services to vulnerable people (adult social care and children’s social services) to be protected. Districts will now all be tariff authorities of varying degrees.

This means that if the levy option of 1:1 was adopted (i.e. 1% growth in business rates means a limit of 1% growth in spending) then a two-tier county would not ever be subject to the levy, however if the ratio were smaller, 1:0.5 for example (where 1% growth limits growth in spending power to 0.5%) then it is possible that the county could be a top-up authority and also attract a levy payment.

Tax Incremental Financing (TIF)

The long reset period will allow authorities to undertake Tax Incremental Financing (TIF) within the existing prudential borrowing rules. Government will also allow a limited number of TIF projects, in a similar way to Enterprise Zones, to be exempt from the levy and reset for 25 years. More details are to be announced later this year.

Pooling

Pooling will be voluntary and the Government will wish to see assurances around governance and workability with sign-off from all relevant Chief Executives and Section 151 officers.

There will be a published framework for those authorities who wish to pool and authorities will be expected to publish their pooling arrangements. There will be no further incentives offered to pooling authorities “at the start of the scheme” and districts will be able to pool outside of their county boundaries.

Applications from authorities who wish to form pools will be sought next year before the publication of the draft Local Government Finance Report.

Police

Police Authorities – or Local Policing Bodies, as the report refers to them as (due to the introduction of Police Reform and Social Responsibility Act 2011) – will be treated separately from the Rates Retention scheme and their funding will be protected from fluctuations to business growth/decline. This acknowledges their limited levers for driving business growth.

As stated in the July consultation, the funding of police will be fully reviewed in time for the changes to be made at the end of the current SR period (2015).

Fire & Rescue Authorities

The Government has taken into account responders' concerns about funding for fire services – particularly those related to the two different types of fire authority – namely single purpose and county councils with fire responsibility, and they have decided to treat them both in the same way.

As such there will a proportion removed from the baseline rates of each billing authority (pre tier split) to fund the fire service, subject to any tariff or top-up required to bring them to their baseline funding level.

Revaluation

At revaluation the Government ensure that the national take of business rates does not exceed RPI. This is done by resetting the multiplier. This, combined with the effect of the property revaluation, means that the business rate yield could potentially be redistributed throughout the country.

In other words, the rateable value in one authority could vary significantly due to the authority's growth in comparison to the national average. Allowing these changes to simply feed through into the rates retention scheme could result in changes to the incentive effect. Government propose to adjust the tariff and top-ups so that income from business rates retention is unaffected by revaluation.

Subsequent appeals will not be adjusted for and local authorities will be expected to manage the impact of them alongside normal turbulence. However the continuation of the rates relief system will be recognised. In cases where the income excluding-relief is greater than including-reliefs, authorities will receive the difference from central government. Authorities will be required to repay the difference where the rates total including-relief is greater than rates excluding-reliefs.

Any deficit in the transitional relief pot will be met by Central Government.

The Government anticipate that the Local Government Finance Bill will receive Royal Assent later this year enabling rates retention to be introduced in April 2013.

The Government will be establishing a Working Group comprised of a range of individuals from the local government sector, who will contribute to the policy and technical debate and act as a critical friend to central government in designing and underpinning the scheme.

3 Considerations

In preparing this report the relevance of the following factors has been considered: financial, legal, prevention of crime and disorder, equality and diversity, human resources, environmental, health, property and transport considerations.

4 Key Decision

No

5 Call-in

Is it required that call-in be waived in respect of the decisions proposed in the report? No

6 Background Papers

Local Government Resource Review – Proposals for Business Rate Retention – consultation. Government response
Local Government Resource Review – Proposals for Business Rate Retention – consultation. Summary of responses.

7 OFFICER'S RECOMMENDATION

To note the Government's response to the Local Government Resource Review - Proposals for Business Rates Retention.

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