

Business rates retention

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The Coalition:
our programme
for government

 UK Government

“We will promote the radical devolution of power and greater financial autonomy to local government and community groups. This will include a review of local government finance.”

“We will provide incentives for local authorities to deliver sustainable development, including for new homes and businesses.”

Local growth: realising
every place's potential

 UK Government

“Local business rate retention will be considered within this review, which we intend to launch in January after a period of consultation on the proposals in this document. This is a significant opportunity to consider a range of options to provide genuine incentives for local economic growth through the business rates regime, and to equip local authorities with the tools to support that role.”

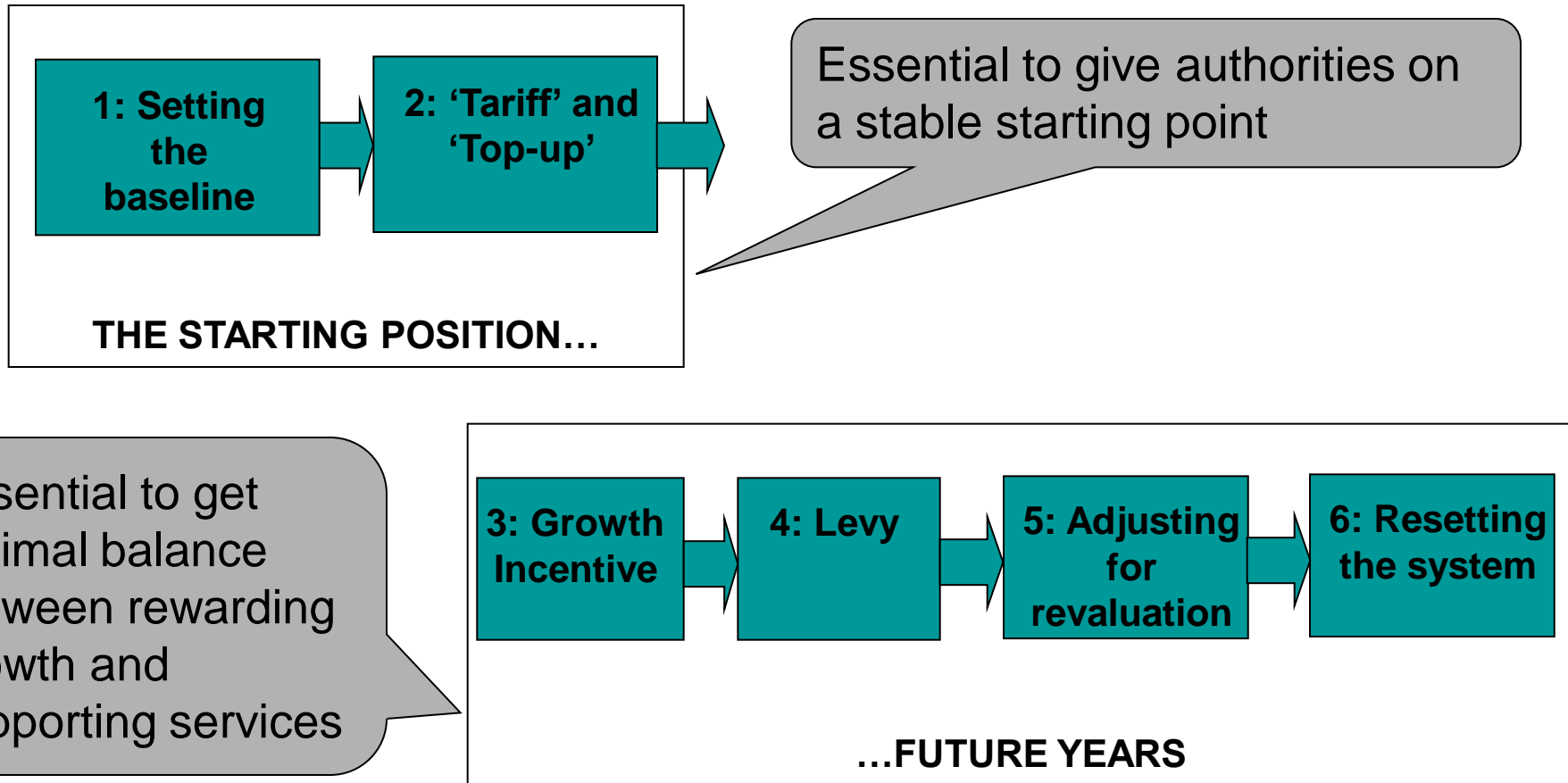
To build into the local government finance system an **incentive for local authorities** to promote local growth over the long term

To **reduce local authorities' dependency** upon central government, by producing as many self-sufficient authorities as possible

To maintain a degree of redistribution of resources to ensure authorities with lower taxbases are **able to deliver services** in their areas

Protection for businesses and, specifically, no increases in locally-imposed taxation without the agreement of local businesses

Components of scheme design

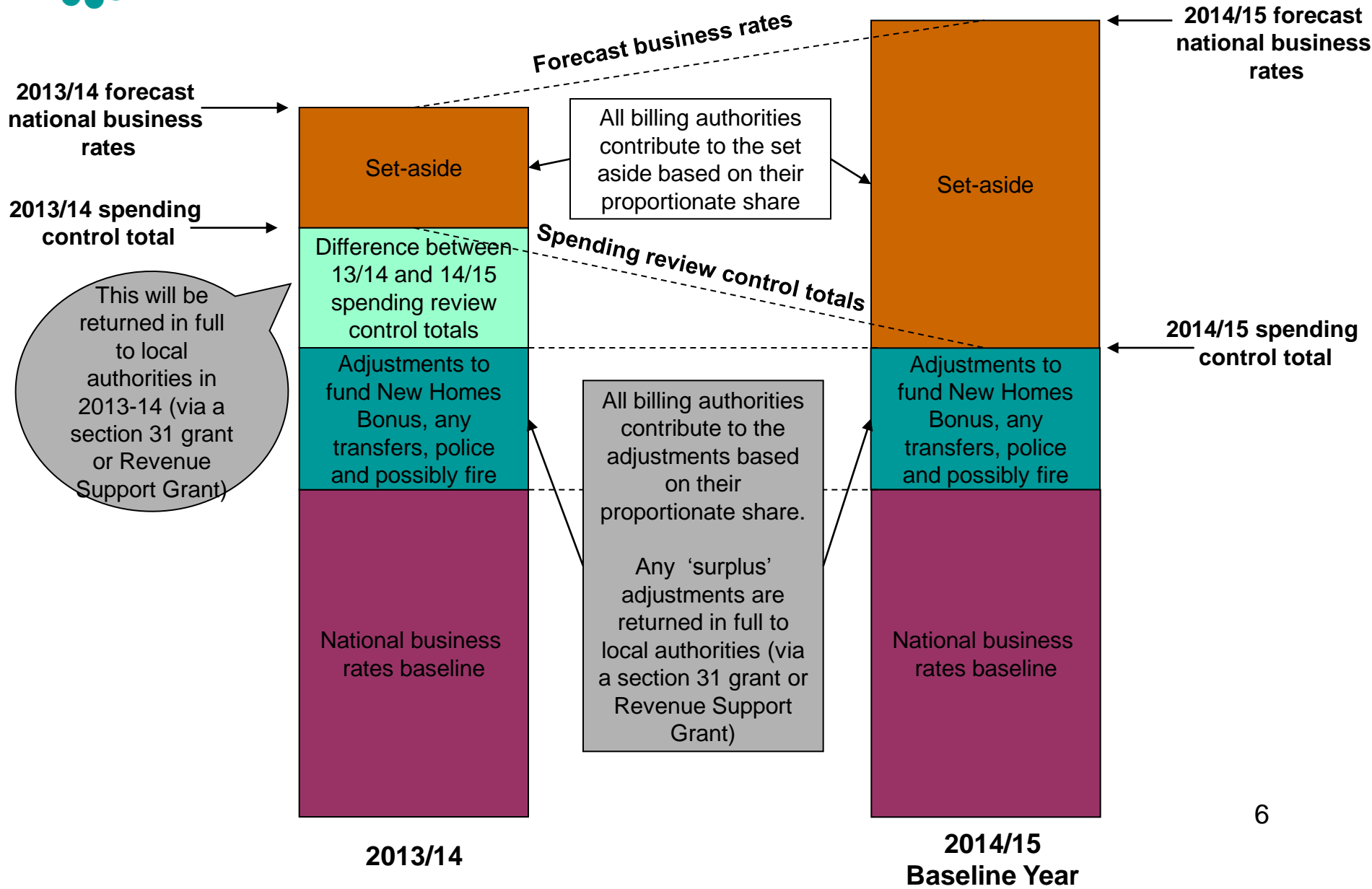


Setting aside a share of forecast national business rates

- Need to avoid putting at risk the deficit reduction programme. Business rates retention scheme will operate within the expenditure control totals for 2013-14 and 2014-15.
- Business rates in 2013-14 and 2014-15 are forecast to be greater than expenditure control totals - need to set aside share of the *forecast national business rates*.
- In determining the National Business Rates Baseline, need to remove two elements:
 - a “set aside” amount equivalent to the difference between forecast rates and Spending Review control totals
 - adjustments to fund New Homes Bonus, any transfers, police & possibly fire authorities
- The set aside will be based on 2014-15 spending figures, but will be adjusted in 2013-14 to ensure that the difference in 2013-14 and 2014-15 Spending Review control totals is returned in full to local government
- From the National Business Rates Baseline, a calculation is made for each billing authority as to the proportion of business rates it will retain – the “individual business rates baseline”

Local authorities will keep growth above forecast levels⁵

Component 1: Setting the National Business Rates baseline



A stable starting point

- Need to establish a stable starting point for all authorities and ensure no authority loses out at the outset of the scheme, as a result of their business rates base.
- Proposing to use the **2012-13 formula grant allocations as the basis** of constructing the funding baseline in the **first year** of the new system, taking account of Spending Review totals for 2013-14.

Two options:

- 1) Adjust actual 2012-13 formula grant allocations
 - Reduce actual 2012-13 formula grant allocations in proportion to reduced spending control totals i.e. freezing the 2012-13 distribution
- 2) Apply the 2012-13 formula grant process
 - Apply existing formula grant process to the sum of the *national business rates baseline*, the police adjustment and any fire adjustment. Would produce greater changes to current distribution than option one.

Component 2: Setting tariffs and top ups

- In the base year, we compare the individual business rates baseline for each authority against its baseline funding level
- Authorities whose individual authority business rates baseline is higher than their baseline funding would pay the difference to central government in the form of a **'tariff'**
- Authorities whose individual authority business rates baseline is lower than their baseline funding would receive the balance from central government in the form of a **'top up'** grant
- This will ensure protections for those authorities who have a low business rates base.
- The system will balance overall, so that:

Total tariffs = Total top-ups

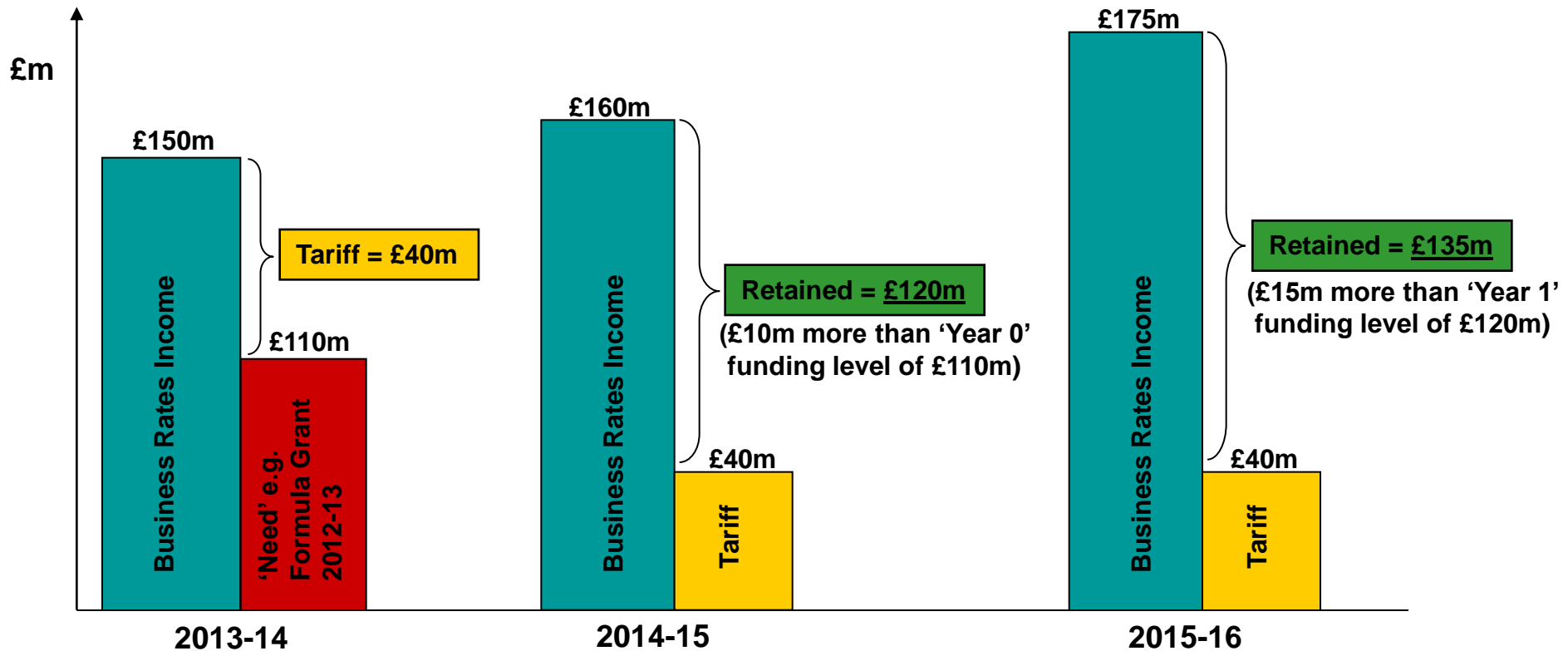
Two-tier county councils

- Government proposes county councils should benefit from growth in local business rates – district councils would share a fixed percentage of the business rates they collect with county council, and enable their tariffs and top-ups to be set.
- Two options consulted on:
 - 1) Fixed national shares** – Each tier of authority would be allocated a standard proportion of business rates based on average national spending
 - 2) Individually tailored shares** – Tier splits relating to local rates bases. County and district shares would vary from one to area to another.

Component 3: The incentive effect

To create a strong incentive and reward authorities promoting growth, in future years the tariff and top up amounts would remain fixed so that a significant proportion of business rate growth in future years would be retained.

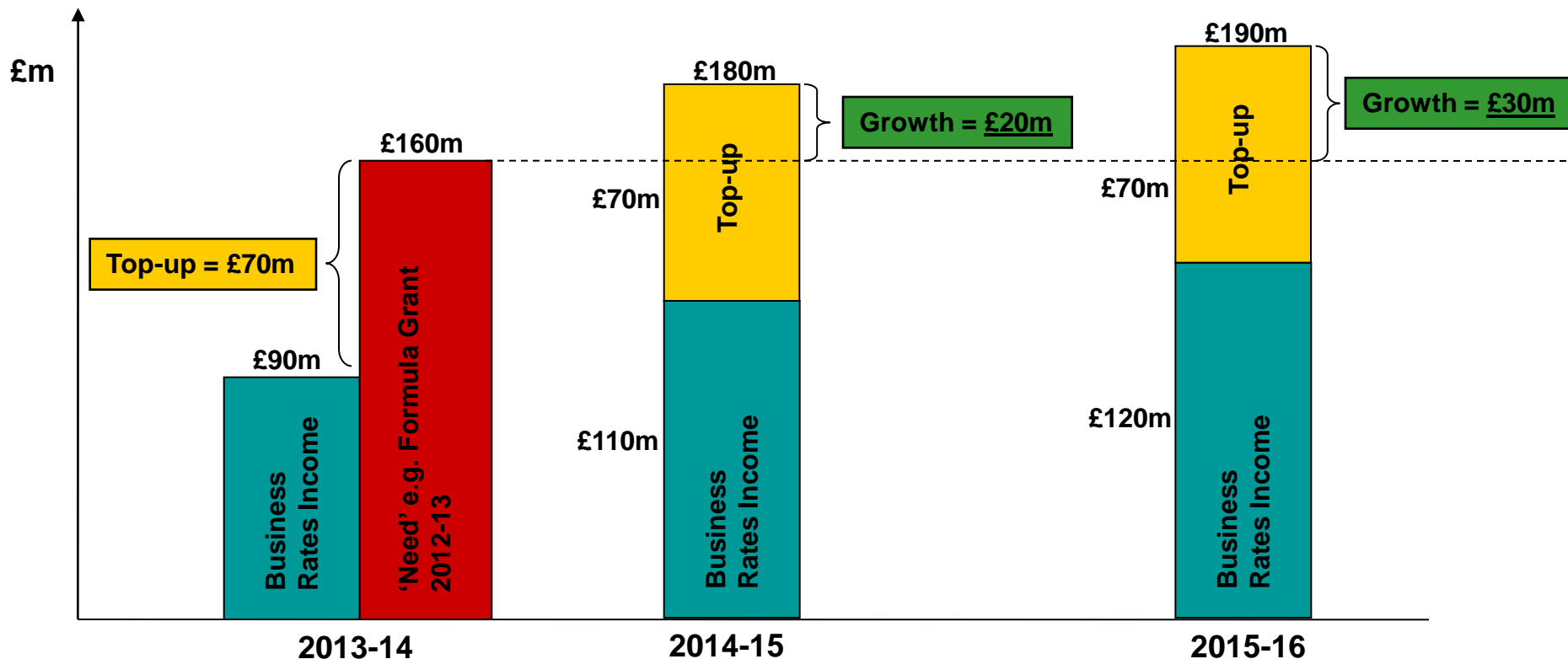
e.g. Local Authority A ('Tariff' authority)



Component 3: The incentive effect

To create a strong incentive and reward authorities promoting growth, in future years the tariff and top up amounts would remain fixed so that a significant proportion of business rate growth in future years would be retained.

e.g. Local Authority B ('Top-up' authority)



Options for rolling forward tariffs and top-up in future years

- The tariff and top-up amount would be fixed until the system was next re-set. However, we have sought views on whether those amounts should be index-linked to RPI.
- An authority which saw no physical growth or decline in its individual business rates base could expect to see their business rates income increase by RPI each year.

Indexing tariffs and top-ups to movements in the RPI

- Provides greater security to top-up authorities; tariff authorities' budgets would be exposed to volatility in their business rates

Fixing tariffs and top-ups as a cash amount that does not change

- Creates a strong incentive for growth; risk that growth in pre-levy income is more limited in higher top-up authorities.

Component 4: A levy recouping a share of disproportionate benefit

- In addition to the system of tariffs and top-ups, we are proposing further protections
- Some local authorities with high business rate taxbases could see disproportionate financial gains due to gearing (i.e. the relationship between an *individual authority's business rate baseline* and its *baseline funding*),
- To limit divergence and make the system **more sustainable** in the long-term, we are proposing a **levy to recoup a share of disproportionate benefit** in those cases where there would otherwise be disproportionate financial gain.
- Proceeds of the levy could be used to:
 - Protect authorities who are less able to respond to the incentive
 - Manage the effects of large, unforeseen, negative volatility in individual authorities' budgets.

Levy Options

Option 1) Flat rate levy

- An authority contributes x pence of every pound of growth to levy pot
- Simplest way to levy
- Would not fully address all consequences of gearing

Option 2) Banded levy

- Authorities are grouped together in a number of bands, with different levy rates applied to each band
- Would recognise the differential impact of gearing
- Further choices to be made on band parameters, number of bands & levy rate.

Option 3) Proportional levy

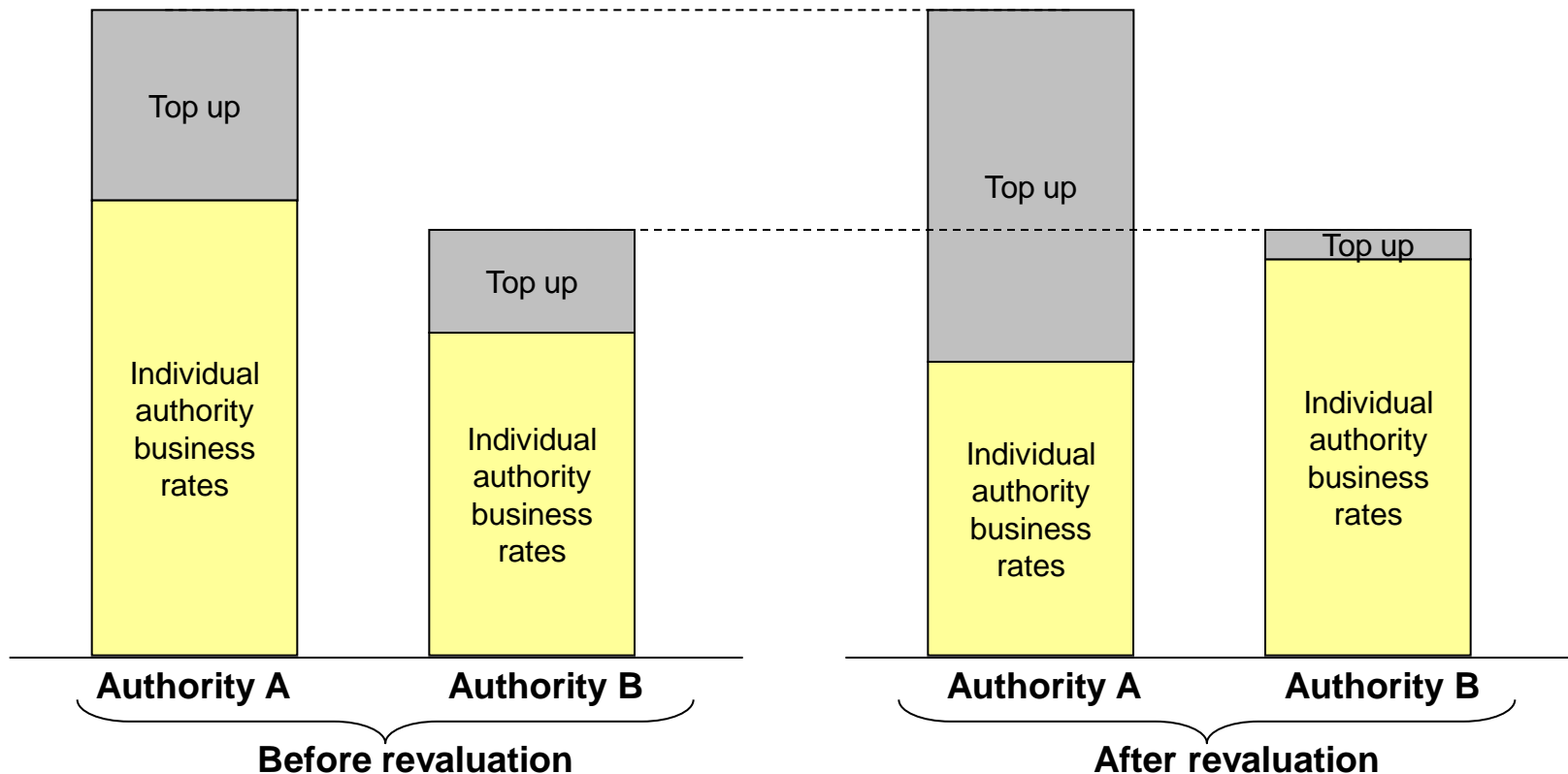
- An authority's levy rate is individually tailored so that growth in business rates results in a proportionate level of growth in retained income
- Tackles both the extent and variation of disproportionate growth in authorities
- Further choices to be made on using 1:1 basis or varying the ratio

- A proportion of the levy pot could be used to provide a *safety net* – to offer protection for authorities against volatility or changes in local economic circumstances
- We are proposing to use *post-levy income* as the basis for deciding whether an authority is entitled to protection
- The Government proposes to introduce:
 - an **annual safety net** – if an authority’s post-levy income declines by more than a set percentage when compared to their previous year’s retained income
 - a **baseline safety net** – if an authority’s post-levy income declines by more than a set percentage below its baseline funding level.
- The consultation documents provide further information on setting safety net percentages, nature of the guarantee, timing of payments, and the treatment of pools

- Relationship between an authority's *individual authority business rates base*, its *baseline funding* and its *tariffs* and *top-ups* – creates gearing effect where impact of growth has very different effects on *pre-levy income*
- The way in which *tariffs* and *top-ups* are set (e.g. whether they are linked to RPI) has implications on the operation of the *levy*, and the likely call upon the *safety net*.
- **Interactive calculator** – enables users to explore these interactions by entering their own inputs and varying components

Component 5: Adjusting for revaluation

- Every 5 years at a revaluation, all business properties are re-assessed and given new rateable values to calculate the business rates payable.
- As different properties' rateable values will change by different proportions, the tax charge is redistributed across England. This means business rates yield in each authority could go up or down, resulting in significant volatility in their budgets.
- To avoid this, tariff and top ups will be recalculated to ensure, as far as possible, that retained income for each authority is the same immediately after revaluation as it was before.



- Local authorities **needs will change by different amounts over time.**
- Re-setting the tariff / top-up of each authority periodically to take account of changing relative need could make the system **more sustainable** in the long-term.
- However, this could also **damage the incentive effect** by re-distributing growth that authorities had achieved over time.

Options

1) Full Reset – Re-run either Formula Grant or a new assessment of need to establish how all business rates should be shared between authorities to set new levels of baseline funding, and new tariffs and top-ups.

2) Partial Reset - Would still involve a new assessment of need, but would not redistribute growth – instead would focus on the original individual authority business rates baseline.

- A group of local authorities could come together voluntarily to form a 'pool'.
- There would be a single tariff or top up for the pool which would be the sum of all tariffs or top ups of the individual authorities.
- There would be a single levy for the pool which would be calculated on the aggregate income and growth across authorities in the pool rather than levying each authority individually.
- Pools would be able to decide for themselves how they distribute aggregate revenues, including any levy proceeds, amongst their members.
- Pooling could enable groups of local authorities to make additional increases in growth through collaborative effort
- Pooling could also help local authorities to manage volatility by sharing fluctuations in their budgets across a wider economic area.

Tax Increment Financing (TIF) and Enterprise Zones



TIF proposals

Option 1: Authorities would be free to borrow against retained business rates revenue, including future growth. Authorities would need to take account of levy arrangements but would be able to plan borrowing, and any TIF projects.

Option 2: Additional business rates arising from a TIF project would be retained for a defined period, and during that period, would not be subject to levy payments, and would be disregarded in any re-assessment of top ups and tariffs. This second option would require government approval to maintain resources available for rebalancing at any reset.



Enterprise zones

All business rates growth within the zone to be retained for 25 years to support the LEP priorities. To deliver this, the business rates uplift from within an EZ will be disregarded from any levy calculations, and will not be taken into account in any reassessment of top ups and tariffs. This will ensure that all growth is retained locally for the benefit of the LEP.

Any questions? Please get in touch:

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Consultation paper, technical papers and the interactive calculator are available at:

<http://www.communities.gov.uk/localgovernment/localgovernmentfinance/lgresourcereview/>