

# POLICY DEVELOPMENT: NOT A STATEMENT OF GOVERNMENT POLICY

## 100% Business Rates Retention

Steering Group 14 May 2018

## Technical paper 2: The Safety Net, Levy & Tier Splits – Risk and Gearing

### Introduction

- 1.1 On 5 July 2016, the Department for Communities and Local Government (DCLG), published a consultation paper, **Self Sufficient Local Government: 100% business Rates Retention**. Following this, on the 15 February 2017, DCLG, published a further consultation paper, 100% Business Rates Retention: **Further Consultation on the Design of the Reformed System**.
- 1.2 These set out proposals for a rates retention scheme to replace the current local government finance system, under which local authorities pay a central share of 50% of their business rates income to be redistributed as grants.
- 1.3 The consultation papers outlined the principal features of the proposed greater rates retention scheme. A summary of responses received to the Further Consultation was published alongside the 2018/19 Provisional Settlement on 19 December 2017.
- 1.4 Following the fall of the Local Government Finance Bill, MHCLG (formerly DCLG) will be developing a package of reforms, in close collaboration with the sector, that furthers the manifesto commitment to continue to allow local government greater control over the money it raises. Reforms to the design of the system will seek to make improvements to the functionality and stability of Local Government Finance.
- 1.5 A commitment was made to the Steering Group and Technical Working Group that a series of technical papers would be shared with the Technical Working Group for discussion and published on the Local Government Association (LGA) website. A suggested forward look of these was shared with the Working and Steering Groups in November 2017.
- 1.6 Taken together these technical papers will raise a number of questions about the proposed rates retention scheme, on which the Government is seeking views.

1.7 This is one of seven core technical papers. The full list is:

- Paper 1: The Central and Local Rating Lists
- Paper 2: The Safety Net, Levy & Tier Splits - Risk and Gearing**
- Paper 3: Appeals and Loss Payments
- Paper 4: Resets, Measuring Growth and Revaluation
- Paper 5: Transitional Arrangements
- Paper 6: Pooling
- Paper 7: Proposed Overall Short Term Package and Future Reform Using Primary Legislation

1.8 We expect that these will be supplemented by other papers in response to Technical Working Group discussions. Additional papers will be announced as need for them arises.

## Background

- 2.1 At present, the local share of business rates income is divided between tiers of local government in two tier areas according to a **tier split** of 80% to lower tiers and 20% to upper<sup>1</sup>. Although tariffs and top-ups redistribute the baselined income, any growth or reduction in business rates rests with authorities according to the original tier split. This produces a gearing effect reflecting the amount of local business rates that a council is able to raise, compared to the amount it is assessed to 'need' as its baseline funding level.
- 2.2 The level of this gearing produces a varying level of risk. Where a council (at present, typically a district council) receives a tier split that gives them a much higher amount in business rates than they "need", a small percentage growth or reduction in business rates produces a disproportionately high effect on their final income, meaning they enjoy large benefits but suffer higher risk. Conversely, where a council (typically a county) receives a much lower amount in business rates than they need they have low risks, but low rewards.
- 2.3 Councils with high gearing are therefore much more likely to trigger the **safety net** mechanism, as this protects local authority income when it falls below a certain level. It does this by guaranteeing that no local authority will see its retained rates income fall beyond a threshold – currently set 7.5% below an authority's index linked baseline funding level. In practice, this means that every local authority is guaranteed to receive at least 92.5% of its baseline funding level.
- 2.4 At present, the safety net is funded through a **levy** paid on growth in business rates income and through a top-slice on Revenue Support Grant. The levy is set as a proportion of the growth, on a sliding scale based on the gearing of the authority in question, but with a maximum of 50%.

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<sup>1</sup> In cases where upper tier authorities do not have responsibility for fire services the position of the fire authority is also reflected in the tier split

## Overview of this paper

- 3.1 This paper sets out options for how to ensure that the retained business rates system continues to incentivise growth while providing appropriate protection from reduction in business rates income when 75% business rates retention is introduced, aimed to be in 2020/21.
- 3.2 In particular, it discusses the options for reform of the safety net and tier split mechanisms, and the future of the levy, including:
- How revised tier splits could adjust gearing and thereby the balance of risk and reward, avoiding the need for highly geared local authorities to trigger the safety net, and what different options might mean;
  - Whether local authorities should have a role in developing their own tier splits;
  - At what level (or levels) the safety net should operate;
  - How the safety net should be funded; and
  - Whether (when legislation permits) Government should still seek to abolish the levy, or whether it should be retained to address concerns about disproportionate growth benefits.
- 3.2 The working group are asked to consider the implication of combinations of options as well as the merits of individual options.

### Legislative considerations

- 3.3 The previous Local Government Finance Bill, which fell upon dissolution of Parliament ahead of the 2017 General Election, would have: provided the framework to deliver 100% business rate retention; provided new flexibilities to reduce rates and add a new infrastructure levy; and provided the framework to deliver reform to how the local government finance system works. There is unlikely to be a further opportunity to legislate for reform with primary legislation during this Parliamentary session.
- 3.4 Therefore the options presented are suggested reforms that could be implemented via secondary legislation when 75% business rates retention is introduced. However the Working Group are also asked to consider any recommendations for future reform that could be enacted if primary legislation was brought forward at a later date.

## Previous Discussion

- 4.1 The System Design Working Group has considered several previous papers on tier splits, gearing, the safety net, and the levy. Views were also sought from the local government sector through the consultation held in 2017 on the implementation of 100% business rates retention.
- 4.2 On the **tier split**, discussion has focussed on the potential for authorities to be able to determine their own tier split. The group considered that there would need to be a default position where agreement could not be reached. Two

possibilities were considered: firstly that if authorities could not agree, then they would retain no growth or, alternatively, if areas could not agree, then a fall back position would be activated. In addition, at a meeting of the Working Group on 15 November 2017, concerns were raised about the possibility of reforms creating 'big winners', especially if the levy were to be scrapped.

- 4.3 On **gearing**, some lowly geared authorities highlighted the difficulty in making significant increases to their budgets via business rates growth. Highly geared authorities stressed the higher levels of risk they face. Consideration was given to changing the responsibilities of the different tiers if their gearing changes. Sharing risk, reward and responsibilities over a wider geographic area was also suggested.
- 4.4 On the **safety net**, the Working Group considered whether its purpose should be as currently determined, i.e. to provide a back-up for when income drops below a sustainable level, or whether it should go further and provide a back-up beyond an authority's determined need when income from growth above the business rates baseline drops significantly.
- 4.5 Under the previous government the **levy** was to be scrapped. The Working Group therefore considered two options for funding the safety net without the levy. These were: using central list income or top slicing business rates income; and the possibility of using a pool to jointly manage risk and reward was also raised.
- 4.6 Following Technical Working Group discussions of these ideas, the Government consulted ratepayers and local government in the Further Consultation on the Design of the Reformed System.
- 4.7 9% of respondents suggested keeping the **tier split** as it is and 31% suggested change. Of this 31%, 19% favoured local agreements and 12% wanted a different split. Some respondents argued that establishing uniform tier splits for the 100% business rates retention system was not appropriate at this stage. There were two dominant lines of argument for this: firstly, that universal tier splits were no longer workable and, secondly, that tier splits should be decided after it is determined what responsibilities will be devolved.
- 4.8 73% of responses were in favour of increasing the **safety net** threshold to a figure between 95 and 100 percent. However, some felt the current threshold was sufficient, noting that the need for the safety-net would be greatly reduced with centrally managed appeals.
- 4.9 The consultation did not ask about the **levy**, but a number of responses commented that removing the levy would take away the main incentive to pooling.

## Developing a new tier split

- 5.1 It is our proposal to retain the tier split mechanism when 75% business rates retention is introduced as the most appropriate way to distribute business rates income in multi tier areas between billing authorities and precepting authorities.

- 5.2 The proposals on tier splits in this section of the paper address potential reform options for the introduction of 75% business rates, aimed to be in 2020/21. Changing the tier split does not require a change in primary legislation.
- 5.3 It is proposed that the tier split for Fire and Rescue Authorities remains unchanged from the current 1% of business rates across the areas they cover and therefore they are not in scope for the reforms outlined in this paper.
- 5.4 In considering whether there should be reform of the tier split mechanism for local authorities going forward two questions need to be addressed. Firstly, has the current tier split operated as anticipated and met the objectives of minimising the risk carried by county councils and providing significant incentives for district councils? Secondly, do those objectives still hold true and is the tier split in its current format the most appropriate way of meeting the objectives of the new system?

### **Distribution of risk and reward in the current tier split**

- 5.5 The table below summarises growth above baseline funding levels by class of authority, based on 2018-19 NNDR1 (National Non-Domestic Rates 1 form) returns. The table includes growth from business rates pilots. The table does not include the impact of the levy on growth or safety net payments so does not represent the income actually retained by local authorities.

<b>Classification of Local Authority</b>	<b>Aggregate Local Growth (£m)</b>	<b>Aggregate Baseline Funding Level (£m)</b>	<b>Growth as a proportion of Baseline Funding Level</b>
Unitary Authorities	407	2,396	17%
Metropolitan Districts	433	2,971	15%
Shire Counties	105	2,565	4%
Shire Districts	612	551	111%
London Boroughs	584	2,127	27%
Greater London Authority	317	1,039	31%
Fire & Rescue Authorities	17	352	5%

- 5.6 Although Shire Districts and London Boroughs have experienced similar absolute levels of growth (~£600m) since 2013/14, it is also clear that Shire Districts have seen significantly higher growth than any other classification of local authority when this is expressed as a proportion of baseline funding. Unsurprisingly Shire Counties (and Fire and Rescue Authorities) have only

seen very small amounts of growth relative to their baseline funding levels as they are top-up authorities.

5.7 Below is a table which summarises the total amount in safety net payments paid to local authorities since 2013 again divided by local authority classification.

5.8 No county has received a safety net payment reflecting the fact that the current tier split has made all county councils top-up authorities. A large proportion of local authorities that have received safety net payments are shire districts, as a consequence of them being highly geared.

Classification of Local Authority	2013		2014		2015		2016		2017	
	Total Safety Net Payments (£m)	No of LAs	Total Safety Net Payments (£m)	No of LAs	Total Safety Net Payments (£m)	No of LAs	Total Safety Net Payments (£m)	No of LAs	Total Safety Net Payments (£m)	No of LAs
Unitary Authorities	9.4	4	4.7	4	24.5	2	3.9	1	1.6	1
Metropolitan Districts	52.1	3	0	0	0	0	0	0	0	0
London Boroughs	80.6	4	73.1	3	58.3	2	0	0	0.9	2
Shire Districts	57.3	57	46.7	47	33.8	22	9.6	10	9.1	15
Shire Counties	0	0	0	0	0	0	0	0	0	0
<b>TOTAL</b>	<b>199.3</b>	<b>68</b>	<b>124.6</b>	<b>54</b>	<b>116.6</b>	<b>26</b>	<b>13.5</b>	<b>11</b>	<b>11.5</b>	<b>18</b>

5.9 The tables above demonstrate how fundamental the tier split is to setting the levels of risk and potential for reward in two tier areas. In this respect the tier split has ensured that the risk carried by county councils is minimal and district councils benefit the most from any growth achieved.

5.10 As previously stated the numbers included do not represent the actual growth retained by local authorities and other elements of the system have the impact of lessening the distributional impact of the tier split. Most critical to this has been the levy on growth which has had the impact of redistributing growth around the system. The Government intends to scrap the levy with the introduction of greater business rates retention which would result in a different actual distribution of risk and reward in two tier areas with no change to the tier split. Therefore it is also right to consider, as part of the reforms changing the tier split, whether the aim is to maintain or change the balance of risk and reward in the system (section 7 deals with the future of the levy in more detail).

## **What are the objectives for the tier split in the new system?**

- 5.11 Striking the right balance between risk and reward for all local authorities will remain a core objective for the local government finance system with the move to 75% business rates retention. One of the objectives of a future tier split should be to ensure that there is a sufficient incentive for all local authorities to grow the business rates base in their areas recognising that all local authorities in two tier areas work together to generate growth.
- 5.12 Fairness and consistency of outcomes should also be important considerations in reforming the business rates retention system. Currently the balance of risk and reward differs not only between districts and counties but also between two tier areas and their unitary counterparts. As noted earlier in this paper and in earlier discussions with the Working Group, this is largely a product of differing gearing levels between two tier areas and unitary areas (on the whole).
- 5.13 As the table in 5.5 illustrates, some London boroughs, Metropolitan boroughs and other unitary authorities have been subject to safety net payments in the current system whilst no county council has received a safety net payment. Some representations from local government have pointed out that the protection of county councils from risk through being lowly geared, because they deliver adult social care and children's social care functions could be portrayed as unfair, when the same level of protection isn't offered to unitary authorities delivering the same services. Changing the tier split so that the number of extremely highly and lowly geared local authorities is minimised would therefore better balance risk and incentives in the system.
- 5.14 All local authorities have a role in generating growth in business rates and should be incentivised and rewarded as such. MHCLG will work closely with the both counties and districts, and in particular the County Councils Network and District Councils Network and district and county treasurer associations, to decide on what the appropriate tier split should be.
- 5.15 There are significant interplays between the tier split and other system design elements when it comes to achieving the right balance between risk and reward in the new system. Therefore it is proposed that the work on designing the new tier split will take place through the Spring and Summer alongside the consideration by the Working Group and local government sector more generally of technical papers on reform options for elements of the system.

**TP2 Q1: Do you agree with the rationale for reviewing the tier split for 2020/21?**

**TP2 Q2: Are you happy for MHCLG to work directly with the CCN, DCN and county and district treasurer associations, on developing a proposal for a future tier split for consideration by the Working Group and Steering Group?**

## **The Working Group made the following comments and recommendations:**

### **TP2 Q1**

- The working group supported MHCLG's rationale for reviewing the tier split. As laid out in the paper, striking the right balance between risk and reward for all local authorities should remain one of the core objectives for system reform. Fairness and consistency are also important considerations.

### **TP2 Q2**

- The working group agreed that it makes sense for MHCLG to continue to work with the CCN and DCN and with counties and districts directly on the basis to set the tier split from 2020/21.
- The working group called for more work and more modelling to be done on the issue of tier splits fairly soon.

## **Allowing local areas to propose their own tier split**

5.16 A key element of the current system has been the incentivising of local authorities to form business rates pools as a way of managing risk and reward at a strategic level across a geographical area. As a consequence, local authorities in many two tier areas are working closer together on how best to manage the business rates retention system. (Note: A technical paper on options for pooling will be discussed at a future Working Group meeting).

5.17 Also, the applications from pools of local authorities to be 100% business rates retention pilots in 2018/19 contained varying propositions around how two tier areas intended to distribute growth and manage risk. These proposals have included altering the tier split within their area and agreeing to share any growth from the pilot along a completely different tier split or establishing strategic investment funds to invest growth to support joint priorities.

5.18 One option for reform is the possibility for two tier areas to agree with central government a tier split that is different from the 'standard' tier split. This would need to be a proposition for a new tier split agreed by and covering all districts councils and the county council in a two tier area. The 1% for FRAs would also need to be reflected in this.

5.19 Recognising that business rates pools are at differing levels of maturity and have varying approaches to governance, this could be an 'opportunity' for local



areas rather than a 'requirement'. Any proposition from a two tier area to set their own tier split would also need to be agreed with MHCLG as the power to set tier splits outlined in legislation lies with the Secretary of State.

5.20 If the Working Group, and wider sector, are supportive of this proposition in principle, further work will need to be undertaken to understand how it could be enacted alongside the current processes for establishing pools. We would need to develop the principles and perimeters under which local areas could propose their own tier split, how this would interact with the setting of baselines for these areas, and the time period that local areas' own tier split would be applicable for. The experience of the 2018/19 pilots in piloting bespoke tier splits will also inform potential reforms.

**TP2 Q3: Do you think that two tier areas should be able to propose their own tier split?**

**TP2 Q4: Do you think that the ability for areas to agree with central government their own tier split should be an 'opportunity' for areas and not a 'requirement'?**

**The Working Group made the following comments and recommendations:**

**TP2 Q3 & Q4**

- The working group was sympathetic to the idea of allowing areas to set their own tier splits. However, it was noted that more thinking would need to be done in relation to the geography of areas selecting their own tier splits and that there is also a question as to how this proposal will interact with the future of pooling.
- The working group noted that business rates pilots have evidenced that the system can be operated with different levels of tier splits in different areas without any impact on non-piloting areas.
- It was also noted that the working group could spend much time and effort debating an appropriate level of tier split to be applied across local government and end up returning to the current default position.
- MHCLG agreed to further explore the interrelations between tier splits and pooling.

## The role of the safety net

- 6.1 Balancing appropriate levels of risk and reward for local authorities will remain a critical consideration in the local government finance system as business rates retention increases to 75%. We are therefore proposing retaining a safety net mechanism to ensure that the level of risk to local authority funding is transparent and managed.
- 6.2 As noted earlier in the paper, two options for how a 'safety net' mechanism could operate have been discussed by the Working Group before. The safety net could provide protection against income dropping below a certain level (i.e. how the current safety net operates) and/or the safety net could provide protection from large scale drops in income in a single year.
- 6.3 The mechanism of a safety net is best suited as a 'back-stop' to ensure that no local authority's income falls below a minimum level appropriate for that particular local authority. Therefore, the safety net should be set relative to baseline funding levels as it currently is. The consultation on implementing 100% business rates retention in 2017 sought local authorities' views on whether they agreed with this proposition and the majority of local authorities did so.
- 6.4 At the moment, we are not proposing expanding the safety net or implementing a new safety net that addresses year on year falls in income. Reform to other system design elements may contribute to reducing the volatility in income that occurs on a year to year basis. For example, the Government has committed to tackling the risk posed by appeals to local authorities as part of reforms to the system. The impact of successful appeals and local authority behaviour around provisions set aside for appeals are important drivers in annual volatility in income. A technical paper on appeals will be brought to the Working Group in April 2018.
- 6.5 It is therefore proposed that the safety net continues to operate as it currently does, as a 'backstop' to ensure that the local authority funding does not drop below a certain proportion of baseline funding level in any given year. However we will keep possible reform of the function of the safety net open as a possibility until the full package of reform measures is established.

**TP2 Q5: Do you think that the safety net should remain a guarantee that income doesn't fall below a proportion of baseline funding level?**

## **The Working Group made the following comments and recommendations:**

### **TP2 Q5**

- The working group agreed on the need to maintain the safety net in the business rates retention system. There were also arguments for increasing the level of safety net in order to add stability to the system. Some on the working group argued for a 100% safety net to protect all losses.
- The working group considered whether there would be ways to incentivise authorities that are deeply into the safety net and seem likely to remain there.
- Another important factor to consider is if local authorities should continue to carry some risk due to business closures which could partially be attributed to the environment for growth they have created.
- Some members of the working group also thought it might be desirable to look at whether different levels of safety net could be set for areas with different responsibilities (but see Q7 below)

## **The level of the safety net**

- 6.6 The Government's 2017 consultation on 100% business rates retention stated that the Government expects to raise the safety net threshold for the 100% Business Rates Retention system, to reflect the increased proportion of local government funding at stake. Those areas piloting 100% business rates retention are piloting a safety net set at 97% of baseline funding levels.
- 6.7 The sector was broadly in support of the principle put forward in the consultation, with most local authorities specifying that a safety net of between 95% and 100% was appropriate as it protected local authority income from dipping too far below baseline funding levels whilst still retaining some element of risk in line with the overall aims of the business rates retention system.
- 6.8 We are open to exploring whether the level of the safety net should vary for different types of local authority. A key question is whether tolerance of risk to the level of funding for a service should vary for different services. As noted in the previous section of this paper, levels of gearing set through the tier split ensure that county councils do not receive safety net payments. This was done to protect funding for adult social care and children's social care. The

same level of protection is not provided to all unitary authorities that deliver the same services as county councils.

- 6.9 One option to provide a higher level of protection to all local authorities that deliver demand-led services is to set a higher safety net level for those local authorities delivering such services.
- 6.10 We recognise that determining the level of the safety net at this point is not possible as the Working Group have yet to consider proposals for system design elements that will contribute to the overall level of risk local authorities will carry under the new system. Based on the principles outlined previously, a working presumption at this point is that the safety net will be between 92.5% and 97% when local authorities move to 75% business rates retention.

**TP2 Q6: Do you agree that the final safety net level should only be determined once the full package of reforms are known?**

**TP2 Q7: What are your views on whether there should be a higher safety net for local authorities that deliver upper tier functions?**

**The Working Group made the following comments and recommendations:**

**TP2 Q6**

- The Working Group recognised a connection between appeals losses and the safety net, which is why wider system reforms will need to be considered as a whole before the appropriate level of safety net can be set. The level of safety net also needs to be balanced against the need for certainty and how much local authorities are willing to withhold from the system to cover risk.

**TP2 Q7**

- The working group agreed that the proposal should not be ruled out at this stage, however, the question was seen as causing controversy. Bringing in more variables would also further complicate the system.

## Funding the safety net

- 6.11 There are a limited number of options through which any future safety net can be funded. Three have been discussed at the system design working group.

These will be taken in turn below and the viability of their funding the future safety net outlined for the Working Group's consideration.

- 6.12 **Central List income.** The Working Group and representations received through consultations have previously suggested that the business rates income from Central List hereditaments could be a source of funding for the safety net. The central list income is currently returned to the Exchequer and, as per primary legislation, used indirectly to fund local government (e.g. towards grants such as Dedicated Schools Grant). A decision to allocate Central List income directly to the safety net would therefore not be fiscally neutral unless considered at the point of a Spending Review.
- 6.13 **Levy on growth.** The current safety net is partially funded through the levy on growth (between 2013/14 and 2016/17 safety net payments totalled £439 million and levy payments raised £227 million over the same period). The previous Government had announced that the current levy will be scrapped under 100% rates retention. If the government were to proceed with scrapping the levy, there is the question of how to fund a future safety net. Through the 2017 consultation and working group discussions the sector have largely been supportive of abolishing the levy.
- 6.14 **Top-slice of total business rates.** The safety net is also currently funded through a top-slice of Revenue Support Grant, which is due to be replaced by retained business rates when 75% business rates is introduced. A top-slice could be used to fund the safety net once 75% business rates is implemented. However, this would need to be a top-slice of business rates income and not RSG. A larger proportion of the safety net will need to be funded through this route if the levy is to be scrapped or reformed in a way that it only is applicable to 'exceptional growth' (see questions below in section 7). This will have a result of shifting funding of the safety net from being funded by those local authorities who are experiencing growth (the winners) to all local authorities (everyone).
- 6.15 Shifting funding of the safety net from a levy on growth and a top –slice of Revenue Support Grant to a top-slice of business rates income was positively received by the sector through the further consultation on business rates retention, with many local authorities commenting that this was the 'fairest' way of funding the safety net. Such a move would shift funding of the safety net from those that are gaining from the business rates retention to all local authorities effectively paying for the safety net.
- 6.16 If the Working Group agree that the future safety net should be funded through a top-slice a key piece of implementation work will need to be undertaken to understand how best to calculate the level of top-slice needed.

**TP2 Q8: Do you think that a top slice of total business rates is the fairest and most viable option to fund future safety net payments?**

**The Working Group made the following comments and recommendations:**

**TP2 Q8:**

- The Working Group reiterated a view that local government would like to see more transparency on how business rates income from the Central List reaches local government.
- MHCLG agreed to further explore how a top slice could fund the safety net, including the quantum needed and how this would be calculated.

## The Levy on growth

- 7.1 Under the current system, authorities whose business rates baselines were above their baseline funding level at the point of setting tariffs and top ups (i.e. tariff authorities) are subject to the levy, which is capped at 50% of retained growth. In 2016/17 the levy was paid by 67 local authorities and 8 pools. The 67 authorities included 42 district councils and 18 unitary authorities.
- 7.2 As discussed in Chapter 5 of this paper, the levy is a significant source of funding for the safety net. In 2016/17 it funded 51.7% of safety net payments. It also functions within the current system to incentivise pooling as multiple authorities' aggregate baseline funding level is significantly higher, causing the levy to be triggered at a higher point and therefore more growth to be retained across the pool.
- 7.3 In announcing the move to 100% rates retention, the previous Government promised to scrap levy payments. It was felt that this would ensure authorities were fairly rewarded for growing their business rates base. The move was widely supported by the sector and was a central feature of the Local Government Finance Bill.
- 7.4 The levy cannot be abolished without primary legislation. Scrapping the levy will therefore be considered as part of a longer term programme of reform post 2020/21. However, improvement to its functionality as a mechanism could form part of the reform package when 75% business rates retention is introduced.
- 7.5 The Systems Design Working Group has previously asked MHCLG to address excessive growth retention, especially where this growth is not fully a reflection of an authority's promotion of their local economy, for example where apparent growth reflects a valuation error.

- 7.6 It is possible that the level at which the levy is set could be the appropriate mechanism with which to ensure that excessive growth retention does not distort the fairness of the system. There are, of course, other mechanisms of the system through which we could address excessive growth, most notably pooling.
- 7.7 The Local Government Finance Act 1988 requires the Secretary of State to calculate in relation to each authority whether it is required to make a levy payment for a year and the amount of such payment. At the moment this power is used to cap growth at a level that resulted in 67 authorities (out of 239 tariff authorities) and 8 pools making a levy payment in 2016/17. If it were deemed to be desirable, this cap could be raised to capture only excessive growth. Additionally, the percentage of growth falling due in these circumstances as a levy payment could be adjusted, so that all excessive growth was removed from the system through the levy.
- 7.8 There are some existing policies which have an interaction with reform of the levy, including the Community Benefit Fund and incentives for renewable energy. MHCLG will work with the policy owners to ensure that these and similar policies continue to function as intended.

**TP2 Q9: Is the levy an appropriate mechanism to address excessive growth within the system upon moving to 75% business rates retention?**

**TP2 Q10: Should future reform via primary legislation include consideration of scrapping the levy?**

**The Working Group made the following comments and recommendations:**

**TP2 Q9 & Q10:**

- Even though scrapping the levy gained wide support in the Further Consultation on 100% Business Rates Retention (primary legislation is required to do this), many on the Working Group feel that the need for some sort of levy probably still exists. However views on this question were varied and the group would like to continue debating whether there should be a progressive levy where the levy is paid on 'excessive' growth.
- It was argued that the incentive for authorities to continue growing their business rates baseline should be proportionally the same no matter what their gearing is. It was recognised that the gearing effect may limit some authorities' capacity for growth.
- Avoiding levy payments has often motivated the forming of pools among tariff areas. If the levy was scrapped then incentives for pooling would need to be re-considered.

- However, it would be hard to come up with other ways of paying for the safety net that did not in some way resemble the levy. One idea would be to have a progressive levy where an initial proportion of growth would be levy free.
- Whilst levy is a significant source of funding for the safety net it would not be sufficient on its own.