Local Government Association

FUTURE FUNDING
YOUR LOCAL AREA

Business rate retention: the story continues

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Introduction

Since 2010 councils have seen their resources from central government fall by 40 per cent in real terms and will need to have made £20 billion of savings by April 2016. Although many of these have been efficiency savings, according to a survey carried out by the LGA in 2014, 60 per cent of councils that replied were considering stopping at least some key local services due to efficiency savings running out. This will have an effect on local government's ability to improve people's quality of life and support local businesses.

Within this generally bleak picture, the introduction of business rates retention in April 2013 can be seen as a more hopeful feature. Before April 2013 all business rate income collected by councils formed a single, national pot, which was then distributed by government to councils in the form of formula grant. Through the Local Government Finance Act 2012, and regulations that followed, the Government gave local authorities the power to keep half of business rate income in their area by splitting business rate revenue into the 'local share' and the 'central share'. The central share is redistributed to councils in the form of revenue support grant (in the same way as the previous formula grant) and in other grants. The local share is kept by local government[1], but is also partly redistributed.

This change is intended to provide financial incentives to councils to grow their local economies. At the same time, it has resulted in more risk and uncertainty.

Almost two years have now passed since the business rates retention system was introduced in England. In November 2013, the Local Government Association (LGA) first surveyed councils about their early experience of the business rates retention system. It was clear that many local authorities were still trying to develop their understanding of the system, its benefits and disadvantages. As a result, we decided to revisit this analysis one year later.

As we said last year, the experience of councils to date has been varied and no two stories have been the same. However, there are emergent issues that are common among local authorities. By far and away the primary challenges are the level of financial risk that councils face due to appeals and dependence on a small number of large businesses for a significant proportion of business rate income. As this report shows, these are the reasons why the scheme has made a deficit in its first year and there has been a top-slice on the overall settlement funding.

Many local authorities also mentioned the levy mechanism as a counterproductive feature of the system which stifles incentives to grow the local economy – but it is used to fund the safety net mechanism which is welcomed by other authorities.

1 Subject to potential payment of the growth levy in individual cases.

Methodology

This report is based on results from a survey of chief finance officers of all 353 councils in England, conducted during October and November 2014. We received 120 responses, which is 34 per cent of English councils. Whilst these results should be taken as a snapshot of the views of this particular group of respondents, rather than representative of all chief finance officers, this level of response means that the results are likely to provide a good indication of the position of the sector.

The report also uses other evidence and stories that we received from local authorities. It makes proposals to improve the system by mitigating financial risks and provide councils with more financial incentives.

How does business rate retention work?

The business rate retention system was introduced in April 2013. Councils retain up to half of the rates revenue raised from businesses in their local area, with the remainder retained centrally by the government and used to provide grant funding for local authorities.

The government had stated an intention to ensure that each local authority's allocation for the first year (2013/14) was similar to what it would have received in that year, had the Formula Grant system continued. For this it calculated for each individual local authority a **funding baseline**, largely based on the previous formula grant system. It also calculated a **business rates baseline** based on the average of business rates collected in the two most recent years for which data was available. Where an authority's business rates baseline exceeds its funding baseline, they pay the difference to central government as a tariff, which is used to pay for a **top-up** for authorities whose funding baseline is less than its business rates baseline. These tariffs and top-ups are uprated each year by the business rates multiplier, normally RPI. The government's stated intention is that they will otherwise stay fixed until the reset in 2020.

Councils also keep up to 50 per cent of growth in their business rate receipts arising from new or expanding businesses. Local authorities which pay tariffs also are liable to pay a levy of up to half of this type of growth. Levy revenue is then used to fund the safety net system to protect those councils which see their year-on-year business rate income fall by more than 7.5 per cent.

For more detailed information on how the system works, please see our overview of how the system works in our previous business rates report[1], and the guide from the Department for Communities and Local Government[2].

1 Business rates retention: the story so far. LGA, January 2014

2 A plain English guide to business rates retention. DCLG, July 2012

Outcomes in 2013/14 and 2014/15

Since April 2013, councils have had time to get used to operating in this new system and develop procedures to assist with gauging the risks and opportunities of the reform. Two very important trends have shaped their experience.

The national economy is showing signs of recovery, although this is different in different areas. Where there is confidence in private sector growth councils have benefitted through increased business rate income. However, this is not the case everywhere as the economic recovery has not been felt as strongly in some areas in comparison to others.

However, public sector austerity continues apace. With a 40 per cent real terms reduction to its core grant funding over the life of this Parliament, local government has borne a much greater reduction than the rest of the public sector as a whole. Reducing amounts of government grant have started to and will continue to make councils increasingly reliant on local business rate income in their budgets. At the same time, we are hearing that rationalisation of the public sector is increasingly leading to reductions in business rate income from public sector properties. In the context of on-going uncertainty arising from appeals, some authorities will perceive this trend as a major financial risk.

Headline performance of the scheme to date

LGA analysis suggests that the outcome of the first year of the scheme is a deficit of £27 million, with 208 authorities receiving a surplus and 178 suffering a loss. Had it not been for the safety net the overall deficit would have been £200 million more, but that is at the cost of a top-slice for the whole of local government of £195 million over three years. However, had the government taken responsibility for appeals raised before April 2013 we estimate that the scheme would have shown a surplus of £236 million and the top-slice would not have been needed at all.

2014/15 forecasts show an expected rebound. A lot of this change is due to the decisions councils took about making provisions for backdated appeals.

The provisions for pre-April 2013 appeal losses affect levy and safety nets. Some authorities who would have been subject to the levy have instead received safety net payments. This means that the overall top-slice is larger than it would have had to have been had the government taken the risk for pre-April 2013 appeals. Local government is paying the cost of central government's delays.

We revisit backdated appeals this later in the report.

Local experience of the scheme

In our survey, we asked councils a series of questions to summarise their experience of business rates so far. They reflect an experience quite similar to that implied by the scheme's performance in 2013/14.

1. Overall, respondents tend to agree that the retention scheme created a strong incentive to grow the business rate tax base. More than two thirds agreed, and 58 per cent said that this was the single best outcome of the reform. In last year's survey, 29 per cent of respondents said the reform provided sufficient incentives.
2. When asked about the biggest issue their council faces under the new system, the result was clear cut – 74 per cent of respondents named risk arising from appeals.
3. 66 per cent of councils said they were dependent upon a small number of large businesses for their business rate income, and in 21 per cent of council respondents at least some of that income is at risk due to potential closures or appeals going in favour of the ratepayer.

The rest of this report will focus on the largest risks and potential opportunities that councils face after business rate reform, suggesting various changes that would improve the system and unlock the potential of business rates retention.

Table 1. Performance of the scheme, 2013/14 and 2014/15

	2013/14, £m	2013/14 adj, £m*	2014/15, £m
Local share of business rates for retention purposes	10,691	11,162	11,562
Funding baseline	10,899	10,899	11,111
Surplus/deficit before levies and safety net payments	-207	264	442
Total levy payments	25	62	74
Total safety net payments	205	34	8
Retained business rates	-27	236	376

* '2013/14 adj' column assumes no backdated appeal costs (i.e. that the estimated cost of all appeals raised before April 2013 is met by central government)

Here is a selection of councils' comments on **their general experience of the business rates retention system**:

"The biggest issue for us is the failure of the scheme to adequately address changing need. Demographic change, both since the outset of the scheme and in the future, has led and will likely continue to lead to a relatively large increase in need in comparison with other authorities. The fact that the council is also residential and has little business base upon which to grow, has created a combination of circumstances that have meant that we are and will continue to be at a considerable disadvantage until the reset of the scheme at the very least."

"The council welcomes the broad incentive of local government having a greater stake in local economic prosperity. However there are serious conflicts for an area with constrained development opportunities and where the strategic aspirations are to develop jobs and grow Gross Value Added in high tech, high skills roles including in the digital and creative media sectors."

"The incentive is there but it is weak. We are a tariff authority so only keep around 10 per cent of the overall business rates we collect, even less after paying any levy due. Also there are so many other factors outside our control that growth can then be wiped out eg cost of appeals and increase in mandatory relief."

"It provides some incentive to achieve growth. Growth cannot be achieved without working in partnership although it sometimes appears to be the case that growth can be achieved without any real effort."

"The best feature of the system is that the council knows its absolute minimum level of business rate income receivable in that year."

The risks of the business rates retention system

Financial risk

It is not surprising to see that business rate appeals continue to be at the top of the list of issues related to business rates retention. The backlog of appeals that have been lodged but not yet ruled upon has reduced somewhat but remains large. In the Autumn Statement 2013, the Chancellor committed to clearing 95 per cent of the appeals backlog by July 2015. The Valuation Office Agency (VOA) later clarified that this only applied to appeals outstanding as at September 2013 and took no account of appeals which have arisen since then.

As a result, in October 2014 the VOA reported 51,870 of the original appeals as outstanding – progress of 69 per cent[2]. However, after taking into account appeals raised after September 2013, 113,380 cases were unresolved as at October 2014[3]. While it is true that the majority of appeals uphold the existing valuation, local authorities still have to be prudent in their forecasts and budget for the worst case scenario.

Two particular factors contributed significantly to the financial risk that councils faced from April 2013. The information provided by the VOA to local authorities was initially judged to be insufficient to arrive at prudent forecasts, although the VOA is now providing much more information. At the same time, the government adjusted the business rate baseline to account for the cost of appeals from before April 2013 but this still meant that councils had to pick up 50 per cent of the costs of backdated appeals beyond the initial assessment.

Setting the cost of these appeals against the old national non-domestic rates pool would have been a true and fair way to reflect the sharing of risks before and after the introduction of the reform. However, the government has not reviewed its decision in relation to pre-April 2013 business rates appeals – the LGA urges it to do so.

In Autumn Statement 2014, the Chancellor announced that, starting from April 2015 for new appeals and April 2016 for pre-existing appeals, any decisions made on appeals after that date will only be backdated to April 2015. This is welcome as it will reduce the risk of appeals in the short term, but the system still needs reform to ensure that once the new rateable values come into effect from April 2017 the same issues do not arise again.

We asked councils about their perception of appeals risk, and improvements to the system that could be made to reduce it.

- Overall, 47 per cent of councils felt that appeals risk had increased since last year. However, 36 per cent felt the risk had remained unchanged.
- Almost two thirds of councils mentioned further improvements could be made to the system to reduce the risk further. While our 2013 survey results showed the information provided by the VOA was improving, this year the vast majority of authorities suggested further ways to make it even better. One example would be an analysis of likely changes in rateable value as a result of individual appeals and a general likelihood of individual appeals being upheld.

2 www.voa.gov.uk/corporate/News/2014/newsRelease_30_10_2014.html

3 www.voa.gov.uk/corporate/statisticalReleases/141127_Local_Rating_List.html

As noted earlier, a key risk relates to local authorities which are dependent on a small number of large businesses for their business rate income. In such cases, a business closing down or being successful with their valuation appeal would have a severe effect on business rates income as well as affecting the local economy.

Case study Tewkesbury

There are a number of appeals that were raised before April 2013 still awaiting decision in relation to significant national infrastructure installations that are situated within the Tewkesbury Borough Council boundary. One such case is still ongoing but, as a result of the appeal investigations, the current valuation has been reduced and the council will have to cover a large proportion of the losses arising from the reduction.

It is expected that the reduction in rateable value backdated to 2010 will necessitate the council making a refund of £1.6 million to the company and a repayment of £1.1 million of transitional relief to the Government. This will impact on the council's treasury activities as the investment portfolio will need to shrink in order to make the refund. This revaluation alone will see a reduction in annual business rate income from telecommunications of 23 per cent, with an on-going annual impact of this revaluation alone of £147,000. The one-off impact to the retained business rates scheme in the current year is in excess of £630,000 to Tewkesbury.

The council is an active leader within Gloucestershire, driving economic growth across the county and is a member of the county Business Rates Pool designed to facilitate more effective collaboration. The impact of the recent revaluation has severely impacted on the Gloucestershire Pool as they cover Tewkesbury's safety net payment, effectively wiping out £788,000 of Business Rate growth that was earmarked as a key tool to help deliver the wider growth agenda.

At the time of writing, the appeal on the 2005 valuation is still outstanding but is due shortly with an expected substantial reduction in rateable value which would result in a further repayment and added losses. There is no financial benefit to the council if the appeal is rejected, as it was raised before April 2013 – but Tewkesbury still bears half of the risk of having to reimburse the company for backdated costs.

Case study Didcot power station fire

On 20 October 2014, a huge fire erupted in Didcot B power station. Although the fire damaged the equipment, operators nPower clarified that the plant would become operational again shortly.

Had the power station been forced to close for at least a year, South Oxfordshire district council would have lost about £1 million of business rate income per year. This alone would have been enough for the council to become reliant on the safety net.

Mitigating financial risk

The Government recognised there is a backlog of appeals and promised action to clear 95 per cent of outstanding cases (as at September 2013) by July 2015[4]. Part of the action plan was an early review of how rateable value was challenged, followed by a fuller review of business rate administration in 2017. The review of the appeals process has now been postponed and coupled with the larger review. The LGA is disappointed that the Government decided not to take action on appeals at this stage.

The current system does, however, provide councils with a few limited ways to mitigate financial risk. For example, local authorities can create business rate pools, sharing risk and reward among a number of parties, in some cases also reducing the levy payable on business rate growth. We discuss pooling later in this report.

In addition, the Government gave councils the option to write off all expected backdated appeal losses in a single financial year, or to profile losses across five consecutive financial years. Councils made their own decisions about how to use this option based on their individual risk profile.

In our sample, 73 per cent of authorities took the option to write off the cost of backdated appeals all at once. This is broadly comparable to the data held by DCLG which implies that 62 billing authorities (19 per cent) decided to spread their backdated appeals provision, with the remainder opting to write it off in a single year.

This helps explain the difference between the performance of the scheme in 2013/14 and expectations for 2014/15. With many councils deciding to take the hit in 2013/14 alone, the appeal costs for 2014/15 are reduced significantly. There have been suggestions that some councils included very pessimistic appeals provisions, hence becoming eligible for the safety net. However, these provisions have to be reviewed by local auditors as part of the usual process of verifying financial accounts. This check helps ensure the provisions are prudent given the very limited information councils have about likely outcomes of appeals.

However, as the analysis above shows, had the government taken on the cost of pre-April 2013 appeals in full, there would have been no overall deficit in the scheme in 2013/14.

The LGA is calling on the Government to provide additional changes to the system which would give councils more financial stability:

1. Central government should bear the full risk of pre-April 2013 appeals.
2. Local authorities should be allowed to contribute to the business rate appeal process. They may hold information that the VOA is not privy to and discourage speculative appeals with their procedural presence.
3. Whether a property is up to date with its business rates could become a relevant consideration in planning and licensing applications. This would improve collection rates and deal with some rogue business practices.

4 Autumn Statement 2013.

Here is a selection of **councils' comments on financial risks**:

"We rely on a nuclear power station for 25 per cent of total business rates income. The main risk is the impact of outages rather than risk of full closure."

"It is very difficult to anticipate the financial impact of successful appeals as there are no bandings, as for council tax, so the potential change in rateable value cannot be predicted. Also, the number of different grounds for appeal are confusing i.e. business often appeals under several different grounds. We have no indication of timescales to settle an appeal and, therefore, when the financial impact will occur."

"There is a risk of unknown appeals and the likelihood of their success which is a cost to the council and not easily predicted, affecting our ability to manage budget projections effectively. The VOA is also not forthcoming with information and has delayed settlement of backdated appeals which again is a financial issue and risk."

"We would like the Valuation Office Agency to give an estimate of the likely rateable value result of appeals. VOA Officers are qualified to do this and should really take more responsibility and give local authorities a better idea of the effects of valuations."

Opportunities of the retention system

While the inherent financial risk arising from local retention of business rate income ranks as the highest challenge to local authorities, the reform has also unlocked various opportunities to benefit from the financial rewards and flexibilities this system provides. The freedom to pool business rates, coupled with extensive discretionary relief powers, allows councils to tailor the system to better match the needs of a local area, either alone or in cooperation with other authorities. However, there are some improvements that could be made to both of these aspects of the system that would allow councils to implement locally tailored improvements to the economy. We address pooling and discretionary relief schemes in turn.

Pooling

The rules of business rates retention allow councils to pool their business rate income on the basis of a voluntary partnership agreement that is reviewed every year – which means that old pools can be wound up and new ones started. The pooling mechanism has the potential to:

1. Share risk and reward among a group of councils, thus reducing the impact of any local economic shocks such as a large business closing down operations in a particular council area;
2. Reduce the growth levy on retained business rate income by joining up top-up and tariff authorities;
3. Unlock partnership working among geographically close authorities;
4. Support the evolution of council groups into combined authorities and other forms of advanced local partnerships.

In our survey, we asked councils whether they considered (or were currently) pooling business rates to find out more about their experience of this feature of the system 18 months after the reform took place.

While the number of pools has grown from 13 in 2013/14 to 27 in 2015/16, survey results reveal the complexity and difficulty of such arrangements. 43 per cent of our sample were either starting or continuing to pool while almost 49 per cent were not considering it as an option. Worryingly, a small number of authorities were willing to pool but were unable to find suitable pooling partners due to the local characteristics of their areas. The impact pooling may have on the growth levy was thought by the government to be enough of an incentive for high-growth areas to take on some of the risk of low-growth areas in a pool, but some places perceived as high-risk may still present a low potential reward for other parties[5].

5 See, for example, the decision by South Hams district council to leave the Devon business rates pool due to an adverse appeals risk position in comparison to the rewards available: http://www.southhams.gov.uk/CHttpHandler.ashx?id=11055&p=0

Discretionary reliefs

Councils have certain powers to grant discretionary rate relief. The business rates retention reform has affected this. The same powers are used to administer various forms of relief, with differing levels of government compensation:

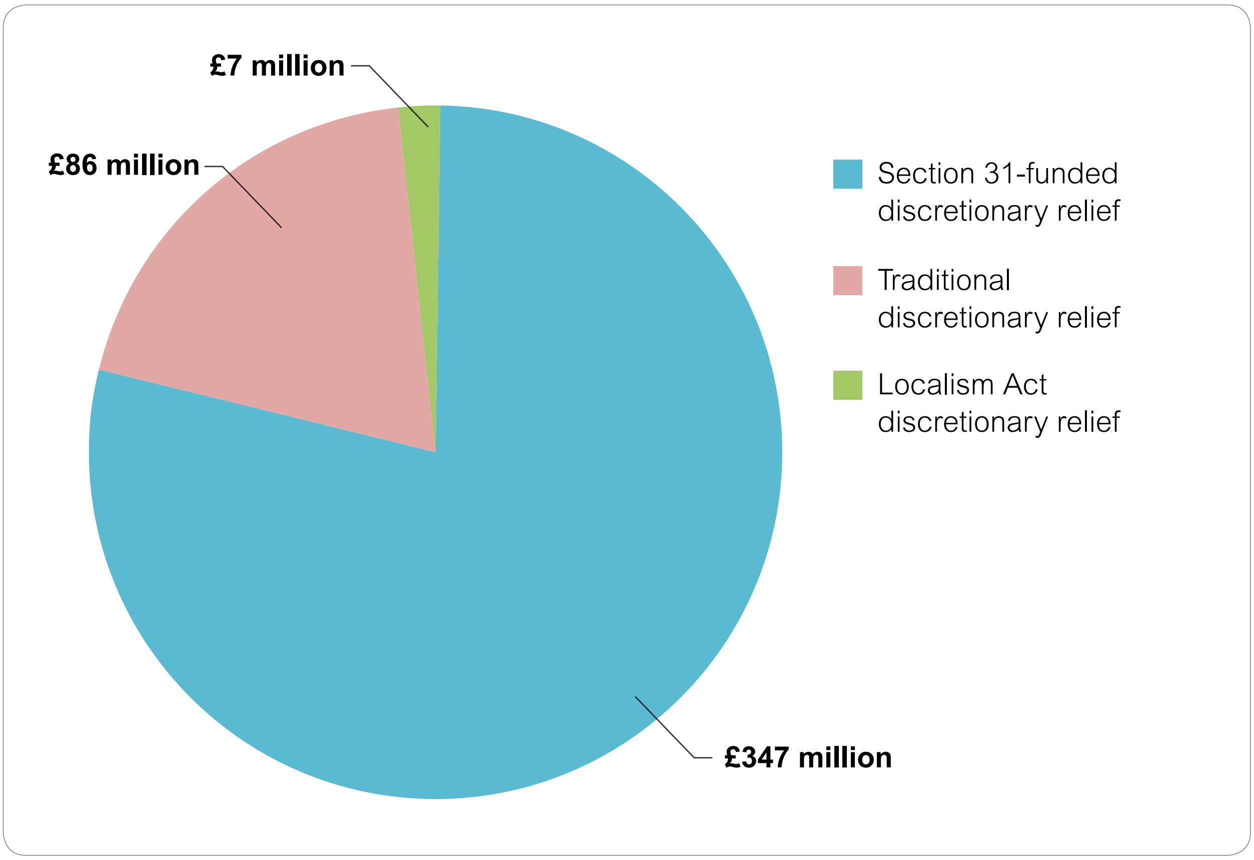
1. So-called 'section 31' discretionary reliefs are used as a mechanism for the government to implement centrally-designed discounts, for example the retail relief scheme. The government provides councils with funding to cover the cost of this relief in full through section 31 grant. In theory, as the reliefs are discretionary, councils can choose not to provide these reliefs, but the vast majority choose to do so as it is 100 per cent funded by the government.

2. Traditional discretionary reliefs are supported by the government and are 50 per cent funded centrally. The main example would be charitable relief top-ups, designed to take charities out of business rate taxation altogether. Non-profit making organisations and those where there is a clear community benefit can also receive 50 per cent relief.

3. Discretionary reliefs under the 2011 Localism Act. These are locally designed with central government meeting 50 per cent of the cost. The government has recently encouraged councils to use them for nurseries and cashpoints[6].

6 See Business Rates Information Letters

Chart 1. Breakdown of forecasted discretionary reliefs to be granted in 2014/15



Arguably, it is the latter form of discretionary relief that can be the most valuable to the local economy. Indeed, some councils choose to use their discretionary powers to encourage various outcomes, such as additional employment. Encouraging certain types of businesses to make better use of the skills of the local population is another example of where these powers can be used.

However, the direct cost of these reliefs, especially in the context of government grant reductions, means that not many councils can afford to use them as extensively as they may wish to. In 2014/15, £7 million of discretionary relief is forecast to be granted under the Localism Act powers. Based on our survey, it appears the majority of such relief in 2013/14 was spent on hardship relief schemes which reviewed cases individually, but there were a few innovative examples of schemes which used the discounts as rewards to attract businesses or incentivise them to expand. For example, Brent Council is running a scheme to encourage employers to pay the London Living Wage.

Business rate pools might be in a better position to unlock the benefits of these discretionary powers. Pooling allows councils to share the cost and the reward of such schemes without necessarily compromising on sensitivity to local economic conditions which is a common flaw of national systems. However, as stated above, pooling might not work as well in some areas under current arrangements. We call on the Government to consider how barriers to pooling could be reduced.

Here is a selection of **councils' comments on the topic of financial opportunities**:

Pooling

"There was an assessment of which combination of districts would be best to pool with the county to give the best return and we were not part of that group as we are unlikely to make significant gains due to revaluations."

"Pooling is too dependent on other authorities who may take a much more pessimistic view of the effects of appeals, meaning that a pooling situation is not viable."

"It works well if you can get the right balance of authorities. It does help to keep more money locally but does add complications for financial planning and accounting. Governance arrangements have to be agreed so that the extra growth retained can be spread fairly across pool members. It is important to monitor and report the performance of the pool closely."

Discretionary relief schemes

"We provide an Enterprise zone discount and run a local town centre scheme which in summary provides 50 per cent relief for up to two years to businesses that occupy and trade from shops within a defined area and that meet the detailed scheme criteria"

"We top up mandatory relief for most charities, registered community amateur sports clubs and village halls. We award relief to non-profit making organisations including local sports clubs. We also provide additional relief to local post offices and general stores in addition to the mandatory rural rate relief and support village pubs that fall just outside the mandatory rural rate relief scheme. We are also starting to use business rate discount powers introduced under the Localism Act to help businesses strategically important to economic growth or retention of employment in the local area."

"We operate a local discount policy to provide discounts to businesses which are expanding in the area or relocating to the area. This relief is to incentivise businesses and increase business rates income whilst also increasing the number of local jobs."

Looking into the future

Future of the local share

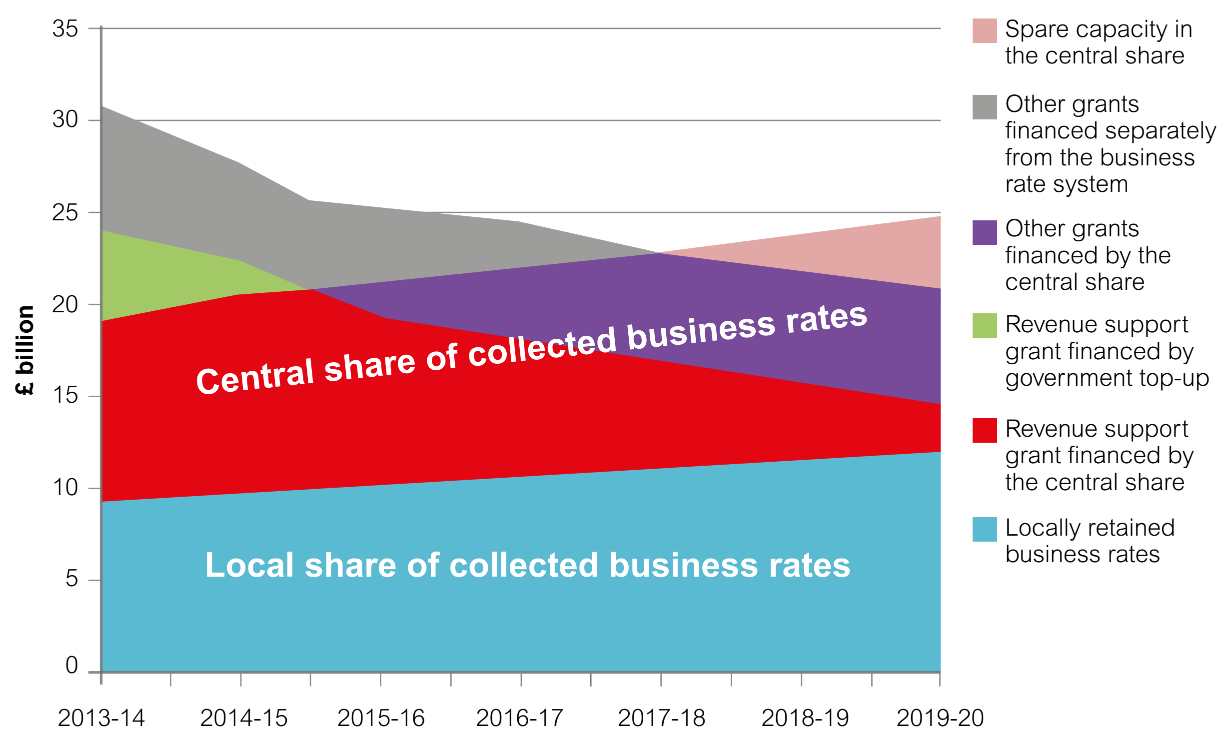
The LGA continues to call for an increase in the local share of business rates, allowing councils to raise and retain more of their income locally. The Secretary of State for Communities and Local Government has publicly indicated that he shares our view by stating that he would like to see the local share increased to about 80-90 per cent[7].

This would have to go hand-in-hand with a revision of the top-up and tariff mechanism to ensure that the system continues to offer protection to authorities with lower business rates taxbases and higher needs.

The reductions in grant funding actually provide the government with a clear and simple way to increase the local share. For the first time, revenue support grant will be worth less than the centrally retained share of business rates in the 2015/16 financial year, as shown in figure 1 below. This means that the government can reduce the share of business rates it retains to match the funding required for the ever-reducing revenue support grant.

7 www.lgcplus.com/briefings/corporate-core/finance/pickles-backs-higher-local-business-rates-share/5072615.article

Figure 1: Centrally retained business rates surpass revenue support grant



Source: LGA Future Funding Outlook Analysis 2014

Future of the tax

The Government has also committed to a wider review of business rates to be concluded in 2016. While the original plans were set to focus mostly on aspects of administration, the scope is now likely to be expanded to look at the basis and relative burden of the tax on various types of business. At the time of writing, the terms of reference have not been published.

During 2014, various lobby groups, think tanks and Select Committees provided their view on the overarching principles of business rates as a tax, with a focus on fair tax bills. Commentators tend to believe that a change in the basis of the tax from rateable value of the premises to a different measure might be the answer.

1. The British Retail Consortium has called for the tax to be based on energy usage, employment or other measures, taking corporation tax bills into account as well.
2. The Institute for Fiscal Studies has called for business rates to be based on the value of land, excluding the value of any buildings on that land.
3. The Business, Innovation and Science Select Committee called for a fundamental review of the basis of calculating business rate bills.

The Independent Commission on Local Government Finance set out its own proposals for reform of business rates in its final report in February 2015[8], arguing that:

- 100 per cent of business rates and business rate growth should be retained by local government
- The incoming government consults on the detail of the business rates retention reset as a matter of urgency, exploring options for a partial reset
- The government consults on options for the localisation of business rate relief as part of the review of business rates.

8 Financing English Devolution. Independent Commission on Local Government Finance, February 2015

We asked councils what they thought the best basis for calculating business rate bills is. Overwhelmingly, 83 per cent of respondents preferred the current property value-based system as it is based on a visible and unavoidable asset, revenue was easily identifiable as related to a particular local area, and the benefits of tax buoyancy.

With the responses in mind, the LGA calls for any business rate system review not to impair locally raised income or its predictability. However, a debate on whether the tax can be made fairer to businesses, especially in the age of e-commerce, is required and welcome.

Here is a selection of councils' comments on the topic of **the future basis of the business rate bill calculation**:

"Whilst understandably not universally popular with businesses, the current system is stable, predictable and understandable. It is important to maintain the overall tax yield from businesses as part of a mixed tax system. Other methods are less predictable and could lead to large variations in tax due from year to year for individual businesses."

"Property value is easily ascertained and is hard to hide unlike revenue or profit. The current system is finally bedding in now that appeals are being settled and realistic values are being attributed to new property. To introduce a new system would reopen a fresh set of appeals which would undermine the system from the start."

"The current system values floor space hungry businesses. Lots of the economic growth in the city is driven by businesses that don't pay very much business rates because they don't have big premises – this is particularly the case for the digital and media industries. Therefore highly successful economic development, jobs growth and environmental impact in the area aren't borne out in business rates growth. We are interested in a mechanism that is more closely linked to our contribution to growing GVA."

"Many businesses do not occupy physical properties in this day and age, so it becomes even harder for businesses with a physical presence to compete against internet businesses, for example."

Conclusions and recommendations

Just like last year, our survey has provided us with an indication of how local authorities' experiences of business rates retention differ, with each local area facing different challenges and financial risks arising from issues such as business rate appeals or dependency on a small number of large businesses. Councils are also discovering different opportunities to grow their economies and benefit financially at the same time. Regardless of such a mix of various experiences, there are some emergent patterns.

1. In the first year the scheme has made a deficit of £27 million even after a safety net topslice which is paid for by reducing settlement funding to all authorities. This is mainly due to the expected costs of pre-April 2013 appeals. Had the government met these costs in full, the scheme would have shown an overall surplus of more than £200 million.

2. Risk arising from business rate appeals remains one of the most important weaknesses of the current system. Councils have no control over or ability to input into the appeals process. The Government's decision to limit the impact of new appeals for two years from April 2015 is a welcome step in reducing this risk in the short term.

3. Some local authorities have economies that are dominated by a small number of large businesses, for example power stations. The economic viability of those businesses and any relevant appeals decisions can have a devastating impact on local finances as a result.

4. Pooling remains a popular method to reduce the financial risk and share the financial reward of economic growth in a larger area. However, some local authorities have found themselves being unable to pool due to their individual circumstances. The pooling mechanism can underpin further collaboration between local authorities in a functional economic area if the right incentives are provided.

5. Some councils have been creative with their discretionary relief powers, providing business with incentives to expand or increase employment. However, the financial stake involved in providing discretionary relief is significant and might be perceived as outweighing any eventual benefits, especially in smaller areas.

6. Local authorities that responded to our survey tended to prefer the current basis for levying business rates, however we accept that the current system might not distribute the tax responsibilities fairly among different types of business, particularly in the context of e-commerce.

With these conclusions in mind, the LGA calls on the next government to

1. Increase the share of business rates that is directly retained by the sector to 80 or 90 per cent, in stages. The equalization mechanism should be adjusted accordingly to ensure that the system continues to offer protection to authorities with lower business rates taxbases and higher needs.

2. Fully fund the cost of appeals raised before April 2013 to ensure that local government does not end up paying the price of delays in central government procedures.

3. Reform the business rates appeal process to allow local authorities to be interested parties in appeals. Authorities may have relevant information about the business that the Valuation Office Agency does not. This would enhance the accuracy of the appeals process and discourage speculative appeals by businesses, which the government accepts is one of the main reasons for the current backlog.

4. Make an assessment of whether a property is up to date with its business rates a relevant consideration in planning and licensing applications. This would help improve collection rates and deal with some rogue business practices.

5. Consider measures to reduce barriers to pooling business rates thus allowing, for example, councils with economies dependent on a small number of large businesses to insure themselves against financial risk without reducing the financial reward available to their partners which face less uncertainty.

6. As part of the 2016 business rate review, commit to preserving overall tax income while considering risk arising from appeals and whether the tax can be distributed more fairly among different types of businesses.

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