SYSTEMS DESIGN WORKING GROUP

SAFETY NET

1. The local government sector has been very clear about its concerns about the move to a 100% rates retention system. In particular, the fear that the inherent volatility in business rates income from year to year will expose them to significantly greater and highly unpredictable risk that will threaten the sustainability of local services.

2. We have therefore been looking at how to reduce the impact of that volatility on local government, to provide a more stable business rates base. We've been considering options to help better manage the volatility of income associated with successful business rate appeals, and looking again at how to best use the Central List. We hope through these areas to be able to share risk more equitably within the system.

3. Risk cannot – and arguably should not – be eliminated entirely. We know that local authorities will continue to face a risk of reductions of income from business rates once we move to a 100% rates retention system – not least from large rate payers closing in a local area. To ensure local authorities continue to be able to deliver services based on business rates income, we should consider what role a safety net will have to help manage this.

4. The current safety net (under 50% rates retention) was set to support local authorities who saw a drop in business rates income of 7.5%. This was assessed at the time as the level at which local authorities would face significant difficulties in delivering the services they are responsible for. The safety net supported 58 local authorities in 2013-14 (to a total amount of approx. £200m), and 43 local authorities in 2014-15 (to a total amount of approx. £115m). It is worth noting that this may not represent the full picture due to pooling arrangements in some areas.

5. Under the 100% rates retention system, a safety net forms part of a wider question about how to manage risk in the system – in particular, the group may want to consider what level of risk can be held at individual local authority level, what risk could (or should) be held at a wider area/regional level, and what risk should be handled at a nation-wide level.

   Are there different levels of risk that should be held at different geographic levels?

   What impact would this have on individual local authorities, and on wider areas?

<u>Purpose</u>

6. With those questions in mind, the group will want to consider what the purpose of a safety net should be. There are two main options that have been suggested:
   a. To provide a back-up for when income of drops below a sustainable level – ie the type of safety net that currently operates. This has a close interaction with the

length of time between resets, but should be fairly straightforward to administer (based on the current 50% rates retention safety net).

b. To provide a back-up for when income drops significantly year on year – ie a safety net that tracks growth rather than baseline funding expectations. This approach would be much more complicated, and would require some further consideration about what income the safety net would be based on. Depending on the volatility within business rates income for local authorities, this type of safety net could be called into action much more frequently.

What should the purpose of a safety net be? Are there other options that we should consider, beyond the two set out here?

Geographical area

7. Under the current 50% rates retention system, the safety net applies to individual local authorities who are supported by a single national safety net – although the existence of a pool spreads the risk in those areas. If some of the risk associated with business rates was held at an area/regional level (eg power stations, water networks, other regionally located networks), we could consider whether a safety net should follow the same geographical level. This could mean a number of local authorities working together to provide a safety net across that area.

What geographical level would the group consider appropriate for a safety net?

Funding a safety net

8. At present, the safety net is funded through a levy on growth and through a top-slice on RSG. The Government has announced that the current levy will be scrapped under 100% rates retention, which leaves a question of how to fund a future safety net.

9. It is expected that funding for a safety net will continue to be through the 100% rates retention system. This means that the level of funding 'set aside' to pay for the safety net will need to be deducted from the overall quantum of funding available to local government for services.

10. There are two likely options for funding a safety net under 100% rates retention:
    a. The working group paper on the future of the Central List floats the idea of utilising Central List income (and/or 'Area List' income) for a safety net; or
    b. We could use the redistribution system to set aside a sum of money to fund a safety net.

How should a safety net be funded under 100% rates retention? Are there alternative options that should be considered?

Support provided

11. The call of local authorities on a future safety net is likely to depend on other measures to reduce risk and volatility. We will need to carry out modelling to look at likely

scenarios to consider what level of support a safety net may need to provide, and what they would mean for the overall size of safety net funding required.

Does the group have initial views on the level of support that a safety net should provide?