SYSTEMS WORKING GROUP
25 JULY 2016

ITEM NO. ....

TWO TIER AREAS FOR SYSTEMS WORKING GROUP

SUMMARY REPORT

Purpose of the Report

1. To consider the experiences of the tier splits under the current 50% business rates retention scheme and key issues for consideration in the design of the 100% business rates scheme.

Background

2. Under the current 50% retention scheme, the local share is currently split 80:20 between lower and upper tier authorities. In areas where there is a single purpose fire and rescue authority, the upper tier share is 18% with 2% being allocated to the fire authority. As 50% of the rates are returned to the DCLG, the splits become 40:10, or 40:9:1.

3. When the 50% scheme was introduced in April 2013, the DCLG were clear that

   'The Government recognises that county councils in two-tier areas have significant levers for promoting economic growth in their area, it is right therefore, that they have the opportunity to benefit financially from any growth in business rates. The summer 2011 consultation on proposals for business rates retention scheme confirmed that counties would receive a share of the business rates from each of the billing authorities in their area.

   However, we also made it clear that the strongest incentive for growth should be placed in the hands of the lower tier, which is responsible for taking the vast majority of planning decisions that deliver growth. In the Government's response to the consultation, we confirmed that the lower tier should receive around 80% of growth of the local share. The Government proposes that the lower tier share of the billing authorities' business rates baseline should be set at 80%.

   This means that county councils in two tier areas will receive a 20% share of the billing authority business rates baseline from each of the billing authorities in their area. This will ensure that all such county councils will be top-up authorities, meaning that a significant proportion of their income will be provided through an index-linked top-up payment. This provides a high degree of stability for those authorities responsible for adult social care and children's services.'

4. Across both tiers, there have been comments that this is not a fair reflection on contributions to local growth and some authorities have been concerned at the levels of risk they are exposed to.

5. However, in some ways the split is not the full picture as the top and tariff regime balances out this split in funding in some way, and this can be significant for both tiers of authority.

6. With the reforms for authorities to retain 100% business rates in their local area, for two tier areas, a pragmatic and joined up discussion should take place to enable the fairest sharing of these resources, which impact on the same residents in the area.

7. The key question facing upper and lower tier authorities is should more of the risk and reward of the new scheme be more evenly shared, exposing upper tier authorities to more volatility to their funding and potentially meaning less reward to lower tier authorities with high growth.

Experiences

8. Within two tier areas, a number of key issues have arisen during the last 4 years. Although in most areas, the upper and lower tier authorities have accepted the way this operates, though all recognising some of the issues and challenges this brings. As well as the two tier split, many other issues within the current and proposed scheme have an impact on both the lower and upper tier authorities.

9. The pattern of risk and reward experienced by individual authorities depends critically on the ‘gearing’, i.e. the extent to which their local business rates are higher or lower than their baseline funding.

10. Higher geared tariff authorities gain more from any increase in their business rates than lower geared top-up authorities, with the most highly geared tariff authorities gaining the most of all. Equally, this is reversed in respects of appeal risk and business rates reduction.

11. Within the two tier areas, the move to 100% retention will also increase the effect of the two tier split on the level of risk and reward that each authority is exposed to, and therefore there is a chance to see if this can be reviewed and potentially even this out this in the fairest way.

12. It is also clear that the top-up and tariff arrangements can make the split irrelevant as lower tier authorities can see a significant proportion of their funding lost through a tariff, which in turn is paid to upper tier authorities as a top-up. There is therefore potential to review the two tier split, which in turn will change the top-up and tariff arrangements.

13. Therefore it is likely that all authorities will be focussed on will be their baseline funding position will be, which will be underpinned by the Fair Funding Review, rather than what the split or top-up and tariffs are.

14. Revaluation will also have an impact in two tier areas as it will change the baseline, which in turn will lead to changes in top-ups and tariffs. This could then affect the incentive to grow, or more exposure to risk, which will depend entirely on the prospects for growth and the likelihood of economic decline.

15. Furthermore, the impact of two tier areas of revaluation has shown in the past to impact two tier areas the Metropolitan Districts and Shire Districts have seen some of the most negative changes to their tax base and widest range of changes. The potential of more frequent revaluations could cause increased volatility in two tier areas and put more pressure on the level of funding for services.

16. It is also recognised that the devolution of new responsibilities may also impact how any funding split in two tier areas is considered. Therefore this could lead to disproportionate changes to baselines and retained business rates and needs to be considered alongside all of the proposed reforms.

Conclusion

17. The reforms to 100% business rates do raise some important issues and questions for two tier areas. It is important for the reforms to be equitable, upper and lower tier authorities' work together to find the best possible solution.

18. The split of funding cannot be looked at in isolation, and all of the factors within the recently launched consultation must be taken into account (role of mayors and combined authorities; devolved responsibilities; revaluations; top-ups and tariffs) and ultimately all authorities will be interested in what their baseline funding position is.

19. Ultimately, a balance needs to be taken to understand whether upper tier authorities should be protected from volatility in business rates in order to safeguard funding for adult social care and children's services, or lower tier authorities should share the risk more equally (and the reward).

20. The current consultation document asks for experiences of the current scheme and suggestions for the reforms, which have been partly covered in this report. However, the DCLG may also want to consider whether it would be appropriate to have a pilot arrangement from 2017 in a two tier area which could test out some of these areas.