**APPENDIX B**

# LONDON BOROUGH OF HAVERING'S RESPONSE TO THE CONSULTATION ON THE LOCAL GOVERNMENT RESOURCE REVIEW : PROPOSALS FOR BUSINESS RATES RETENTION

This letter sets out the London Borough of Havering's formal response to the Resource Review.

Broadly, the Council welcomes the return of control over business rates to local authorities. We are of the view that authorities should retain the income generated through business rates, and should be able to reap the benefits from increases, rather than this simply being returned to Government.

We do however have a number of comments on the detailed proposals. There are also a number of key points that we wish to make as part of our response.

## Transparency and Accountability

Like many authorities, we feel that the current local government financial system is not only unfair, it is unwieldy and patently not transparent. We therefore support bringing this system to an end.

We have always felt that the current system, with its relative needs formulae and system of ceilings and floors, plus transfers in and out, has made it extremely difficult to comprehend. This in turn has made it very difficult to explain to our residents why Havering has received such a low level of grant, and why as a consequence our council tax is so high.

Having reviewed both the main consultation paper, and the subsequent technical papers, it is clear that the business rate retention scheme proposed would appear to be as technically complex as the Formula Grant system it is intended to replace. Given the complexity of the proposals and the number of variations to scheme parameters, it is very difficult to accurately model the proposed scheme and fully assess its likely financial impact on local authorities in general, or on Havering in particular. This brings a degree of uncertainty to our financial position.

The new system will, on the basis of the technical papers issued in August, incorporate similar elements, including a needs formula, tariffs and top-ups, and a process for realignment. This runs the risk of not being sufficiently transparent and prone to interpretation, which we believe should be avoided. It will also be the case that councils will potentially not keep all the money generated locally from business rates, as they may be required to "contribute" towards those councils adversely affected. This again risks weakening the transparency of the new system.

Dependent on local circumstances, individual authorities could be subject to a number of adjustments (tariff or top up, levy payments, contribution to national top slices, and so on). These adjustments risk detaching local economic growth activities from actual financial reward. In addition to the complexity, local authorities will be subject to a significant transfer of financial risk in periods of declining growth (although they may find themselves in receipt of safety net funding dependent on the rules).

There are further potential uncertainties arising from:

- The complexity of the system, which will make it difficult to predict outcomes, which in turn means it will be difficult for local authorities to plan and budget for the future/long term use of any additional retained income
- Any decision by the Government to retain discretion about the frequency of resets and the underlying basis for changes to distribution methodology.

Although local authorities will retain control over their own council tax levels, this will be inextricably linked with the level of business rates. Whilst councils will proactively engage to stimulate business growth, leading in turn to higher levels of business rate income, the basic multiplier will remain under central Government control. This therefore does not bring about a wholesale localisation of the business rate process. In addition, if there is no increase in the multiplier, this will create a gap between local authority spend and the income it generates from business rates. Such a burden would either fall on local taxpayers or require further savings.

<u>Funding Levels</u>

We are concerned that the existing system forms the basis for moving to the new system. Havering has suffered under the current system in receiving a much lower level of grant funding than many authorities, and especially our neighbours. Our grant funding has not, in our view, reflected either the needs of our community, nor the demographic demands arising from the make-up of that community.

The starting position for the new system is that authorities should not be worse off. However, our view is that we are already in a disadvantaged position. Our funding level is well below that of our neighbours. We pointed out in our response to the provisional local government financial settlement why Havering was in such a position, and would wish the Government to consider these points again as part of our response. A copy of our letter is therefore attached.

It is essential that the transition to the new system does not continue to penalise Havering. We would wish to see this revisited to ensure that the council receives a level of funding commensurate with local needs and with that which our neighbours have historically received.

It is understood that there will be a number of adjustments to the starting position. This includes academies and the new homes bonus monies. It needs to be clear how the starting position has been arrived at and we would wish as much clarity as possible over this. It also needs to be clear as early as possible whether there are any other adjustments being made to this.

We also understand that any new burdens placed on local authorities will continue to be funded under the proposals. However, as a side effect of impact of system resets, there is a risk that new burdens could be funded from existing business rates rather than from other sources of funding. This would increase the overall burden on local authorities without a corresponding increase of new funding into local government.

Finally, over time, there is a further risk that there will be “winners” and “losers” in the longer term, possibly beyond the end of the current CSR period, as the various adjustments shift the level of funding that authorities retain. Apart from bringing further uncertainty, it will be very difficult for authorities to compensate for any loss in funding without resorting to compensating council tax rises.

Timing

The final design of the scheme will not be known until around November or December 2012, when we assume there will be a provisional announcement. The final funding calculations we understand will not be available until February 2013, less than two months before the start of the scheme.

Havering has responded extremely proactively to the Coalition Government’s austerity measures. Cabinet agreed a report as far back as July 2010, which included an initial schedule of savings proposals designed to respond to the Emergency Budget, and in anticipation of the Comprehensive Spending Review. A further report was agreed by Cabinet in July 2011. The savings proposals now being implemented by the Council will bring some much-needed stability to our financial position, bring confidence to both residents and staff, and enable the Council to maintain council tax at a low level. We believe further savings will not be needed unless further changes made by Government adversely affect our financial position.

Whilst we welcome the recent announcement of further grant funding to enable authorities to freeze council tax for a further year, we are concerned over the timing of final announcements. These will be late in our planning process and leave little time for further corrective action to be taken. In addition, the 2013/14 budget will also reflect both the localisation of council tax benefits and the transfer of responsibility for public health services. The Council would therefore wish to see detailed announcements being made earlier than currently planned.

Conclusion

As stated in our response to the provisional local government financial settlement, our view remains that the local government funding system is neither objective nor equitable in its allocation of resources amongst individual local authorities. As a direct result, Havering's council tax payers are being effectively penalised. We support the move away from this towards a new system, that should bring greater transparency to the allocation of funds and bring greater control to individual authorities.

Our concern about the Resource Review is that, not only does it fail to remove the inequity of the existing system, it runs the risk of being as complex as the existing system. We also feel that earlier announcements on the detailed proposals, and the associated figures, are essential to bring as much certainty as possible into our budget setting process for 2013-14, which is likely to be the most complex for any years.

Attachments

Please find attached:

- A copy of our submission to the provisional local government financial settlement [for the purposes of the Cabinet report for brevity, the letter has not been included as it appears in the report to Cabinet on 9th February 2011, as part of Appendix B, which can be found on the Council's website at this location:] http://democracy.havering.gov.uk/CeListDocuments.aspx?CommitteeId=153&MeetingId=2074&DF=09%2f02%2f2011&Ver=2
- Our response to the specific questions posed in the main consultation paper.

## LOCALISATION OF BUSINESS RATES
## RESPONSE TO GOVERNMENT CONSULTATION

## *Component 1: Setting the baseline*

**Q1: What do you think that the Government should consider in setting the baseline?**

The baseline position will be the starting point for future years grant retention. The need to get this correct is imperative for the future funding for all Local Authorities.

Currently the difference in a postcode results in a considerable difference in funding. The current formula grant takes no account of the huge variation in grant which creates huge differences in services that can be provided to the community.

Below is an extract from the Department of Communities and Local Government website with an added column demonstrating the grant per head for Havering and neighbouring boroughs? Although the boroughs listed below border Havering, their grant allocations are considerably different.

| | Estimated Population 2010/11 [1] | Formula Grant 2010/11 £m's | Grant Per Head £ |
|---|---|---|---|
| **Havering** | 237,456 | 56.532 | 238.07 |
| **Redbridge** | 273,676 | 101.086 | 369.37 |
| **Barking & Dagenham** | 175,528 | 106.050 | 604.17 |
| **Newham** | 239,175 | 219.919 | 919.49 |

*1 Estimated population provided by the department of Communities and Local Government*

A methodology in setting the baseline should be calculated by taking greater account of population and size of authorities. If the continuing method of apportioning grant continues this will continually create a wider division in local authority funding and create larger pockets of deprivation with local authorities either having to increase up Council Tax or reduce disproportionately service to the local community to compensate.

Any methodology in calculating authorities baseline needs to include some methodology in smoothing resources and reducing the effect of "cliff edges". A transitional arrangement could be put into place in order to reduce the postcode lottery already in place.

**Q2: Do you agree with the proposal to use 2012-13 formula grant as the basis for constructing the baseline? If so, which of the two options at paragraphs 3.13 and 3.14 do you prefer and why?**

For the last 15-20 years Havering have been penalised by the method of formula grant distribution as this has not reflected the demographics and pressures that affect Havering. Havering has the 3rd largest area in London; one of the highest populations of elderly in the capital however has one of the lowest grants per head.

The formula penalises authorities with high Council Tax base as it is perceived they have the capabilities to raise more through Council Tax.  However this only results in a need to raise council tax due to the poor method of reallocation of grant.

Other options should be considered in constructing the baseline. The bigger the size of a local authority's taxbase / Council tax the greater authorities are penalised through the current formula grant system. This should be reversed as having a high council tax demonstrates the need for funding thus a provision / allowance should be made for this.. In addition the population and size of the authorities are not weighted enough in the formula grant even though huge pressures arise throughout the borough. Within the borough there are growing pockets of deprivation which due to the current funding method we as an authority cannot address.

## *Component 2: Setting the tariffs and top ups*

**Q3: Do you agree with this proposed component of tariff and top up amounts as a way of re-balancing the system in year one?**

If the baseline set up a fair position, the methodology of top-ups and tariffs would be a logical solution to reallocating grants. The final figures should be made available at the earliest opportunity to ensure enough time is available set the 13/14 budget.

**Q4: Which option for setting the fixed tariff and top up amounts do you prefer and why?**

There would be a greater incentive for Local authorities if the tariff / top-up were not inflated by RPI. This would create a greater drive to promote growth and penalises those authorities that do not.

## *Component 3: The incentive effect*

**Q5: Do you agree that the incentive effect would work as described?**

Potentially, as long as certain conditions are in place and the mix between the need for protecting authorities and allowing them to grow is fair. Local authorities should be able to retain the majority in business rate growth. Otherwise the incentive affect is lost if authorities who potentially could grow business rate growth are subsidising other local authorities. Authorities with high tariffs and levies could potentially have huge financially problems if certain strands of options are select in the retention model.

## *Component 4: A levy recouping a share of disproportionate benefit*

**Q6: Do you agree with our proposal for a levy on disproportionate benefit, and why?**

In principle, however it is dependant on how much is retained by the authority. To promote growth and ensure transparency the flat rate scheme should be provided to all authorities thus giving authorities a level playing field and allow for all authorities to promote growth through a clear, transparent method. By only retaining a percentage against our baseline this reduces any incentive especially as the baseline does not reflect the service needs which the current formula grant fails to identify.

**Q7: Which option for calculating the levy do you prefer and why?**

As above, the levy needs to be able to be low enough to incentivise local authorities to grow. All local authorities should be set equally thus encourage authorities to grow therefore the flat rate scheme provides this incentive and allows a transparent and clear methodology.

**Q8: What preference do you have for the size of the levy?**

Incentive in business rate growth is imperative for the scheme to work therefore the smaller the levy the greater drive for Local Authorities to encourage growth.

**Q9: Do you agree with this approach to deliver the Renewable Energy commitment?**

In principle we are in agreement with the proposed approach of delivering the Renewable Energy commitment.

**Q10: Do you agree that the levy pot should fund a safety net to protect local authorities:**

**i) whose funding falls by more than a fixed percentage compared with the previous year (protection from large year to year changes);**

Yes, this is due to the fact that business rates are extremely volatile thus a safety net is needed to account for periods of volatility. This safety net is need for authorities who are classified as top-up and tariff as the consequence in falling business rates would potentially affect tariff paying authorities more as top-up authorities have more certainty over funding.

**ii) whose funding falls by more than a fixed percentage below their baseline position (the rates income floor)?**

Yes, as above.

**Q11: What should be the balance between offering strong protections and strongly incentivising growth?**

Protection should be available to local authorities who suffer a reduction in business rates. The financial affects of this scheme could potentially harm authorities with high business rate taxbase or tariff authorities as they would be more vulnerable to business rate shortfalls.

**Q12: Which of the options for using any additional levy proceeds, above those required to fund the safety net, are you attracted to and why?**

The majority of business rates should be retained thus providing an incentive thus reducing the available balance within the levy pot.

**Q13: Are there any other ways you think we should consider using the levy proceeds?**

In the event that funds remain from the levy pot, there could be an incentive to promote small business growth to become major contributors to the economy, local authorities should encourage growth for these businesses. Using the additional levy could help local authorities' incentive small business and drive the economy forward.

## *Component 5: Adjusting for revaluation*

**Q14: Do you agree with the proposal to readjust the tariff and top up of each authority at each revaluation to maintain the incentive to promote physical growth and manage volatility in budgets?**

As long as the previous years growth is incorporated into the baseline and the funding remains within the Local Authority.

**Q15: Do you agree with this overall approach to managing transitional relief?**

In principle we can understand why you are separating the overall approach from the resource review but as an authority we would like assurances that the costs are met by the retention scheme and not the authority.

## *Component 6: Resetting the system*

**Q16: Do you agree that the system should include the capacity to reset tariff and top up levels for changing levels of service need over time?**

Having a system that, when used appropriately, has the ability to reflect the affect of changing levels of service need over time and can only be seen as positive move. This will also depend on the method of defining needs as the current finance settlement does not reflect the demographics and pressures faced to local authorities.

**Q17: Should the timings of reset be fixed or subject to government decision?**

To reduce the number of changes to this scheme, any potential resets should run in sequence to the revaluation period cycle which currently runs every five years.

**Q18: If fixed, what timescale do you think is appropriate?**

Local authorities need certainty in the timescales thus a fixed pre-determined timescale would aid in budget preparation. A timescale should be incorporated which allows authorities any potential benefit to produce growth but also allows a mechanism to reset in case of material change in local authority needs.

**Q19: What are the advantages and disadvantages of both partial and full resets? Which do you prefer?**

To encourage growth and reflect the needs of each authority, the partial reset should be used. This would encourage growth grow as well as adjusting the baseline to reflect the needs of the authority.

**Q20: Do you agree that we should retain flexibility on whether a reset involves a new basis for assessing need?**

Any basis for assessing needs should take into consideration the cliff edges in funding across authorities.

## *Component 7: Pooling*

**Q21: Do you agree that pooling should be subject to the three criteria listed at paragraph 3.50 and why?**

Yes, and this should remain the case in the foreseeable future.

**Q22: What assurances on workability and governance should be required?**

Whatever arrangements are adopted through pooling we would like assurances that Central Government would accept them. Thereby allowing the pool to be self-governed however managed.

**Q23: How should pooling in two tier areas be managed? Should districts be permitted to form pools outside their county area subject to the consent of the county or should there be a fourth criterion stating that there should always be alignment?**

N/A

**Q24: Should there be further incentives for groups of authorities forming pools and if so, what would form the most effective incentive?** ***Impact on non-billing authorities***

The inclusion of any additional incentives for groups of authorities forming a pool seems superfluous to us as an Authority, as they would result in smaller amounts being levied overall.

**Q25: Do you agree with these approaches to non-billing authorities?**

Due to the lack of transparency of the current formula it is difficult for the Authority to form a view on whether we agree with the proposed approaches.

**Chapter 4: Interactions with existing policies and commitments** *New Homes Bonus*

**Q26: Do you agree this overall approach to funding the New Homes Bonus within the rates retention system?**

Yes we agree in principle.

**Q27. What do you think the mechanism for refunding surplus funding to local government should be?**

Given the New Homes Bonus is a specific calculation it would seem appropriate to reapportion the surplus funding in line with it. As an Authority we would also like the assurances that any refund would be unringfenced.

**Q28: Do you agree that the current system of business rates reliefs should be maintained?**

Yes, business rate reliefs are important for the stability for business. Any reliefs which are statutory should be fully paid from the retention model and not funded through local authorities diminishing funding. Any mandatory reliefs should be the discretion of the authority.

**Chapter 5: Supporting local economic growth through new instruments**

**Q29: Which approach to Tax Increment Financing do you prefer and why?**

We would prefer option 2. This gives greater certainty over the future revenue streams

**Q30: Which approach do you consider will enable local authorities and developers to take maximum advantage of Tax Increment Financing?**

For Authorities with greater scope with their revenue budgets option 1 would allow them maximum advantage of a TIF. However for an Authority like ourselves where we would need certainty over future revenue streams, unless we had these in place, projects funded by TIF's would struggle to be approved

**Q31: Would the risks to revenues from the levy and reset in option 1 limit the appetite for authorities to securitise growth revenues?**

In our opinion yes, without that certainty of revenue to match the additional borrowing costs this would. Members have clearly stated that do not wish to undertake prudential borrowing to finance capital projects.

**Q32: Do you agree that pooling could mitigate this risk?**

No. The only way to mitigate the risk is to guarantee the future revenue streams for the duration of the borrowing costs

**Q33: Do you agree that central government would need to limit the numbers of projects in option 2? How best might this work in practice?**

Yes. Some sort of bidding process, possibly similar to the process for capitalising revenue costs