CFG INSPIRING FINANCIAL LEADERSHIP

navca local focus national voice

Self-sufficient local government: 100% Business Rates Retention Consultation Response

September 2016

Introduction

About Charity Finance Group

Charity Finance Group (CFG) was founded in 1987. It is the charity that works to improve the financial leadership of charities, promote best practice, inspire change and help organisations to make the most out of their money so they can deliver the biggest possible impact for beneficiaries. CFG has over 1300 members and our members manage nearly £21 billion in charitable income. Our members work at the heart of the strategic development of their organisations, and are at the forefront of delivering a sustainable and efficient charity sector.

For more information on this response please contact Heather McLoughlin, Policy and Public Affairs Office, on 02078715480 or heather.mcloughlin@cfg.org.uk

About NAVCA

NAVCA is the national voice of local social action. We are the national membership charity for local voluntary sector infrastructure - the people who help others set up and run charities and community groups. We are England's largest network of local charities and community groups.

NAVCA's members form the biggest voluntary sector network in the country, giving an unrivalled national knowledge of local voluntary action. The membership of 200 local infrastructure organisations covers over 95% of communities in England and supports over 160,000 local charities and community groups.

For more information this response please contact NAVCA at www.navca.org.uk or 0114 278 6636

Motivation for responding to this consultation

We welcome this review by the Department for Communities and Local Government (DCLG) into self-sufficient local government: 100% business rates retention. The introduction of 50% business rates retention in April 2013 created a major change in the way that local government is funded. Under the proposals laid out in this consultation, the finances and sustainability of local government will be radically changed. We believe that it is vital that any proposed changes to the financing of local authorities' works best for charities and their beneficiaries, communities and people.

It is in this spirit that we believe any changes to business rate retention should be done with these principles in mind:

1. **Sustainability** – changes must give local government the financial capability to meet their statutory obligations and meet the needs of local communities
2. **Equality** – changes should not perpetrate inequality across regions.
3. **Support a strong relationship between the voluntary sector and local authorities –** financing of local government should not undermine dialogue and collaboration between local authorities and voluntary organisations.

Executive summary

- **We welcome this review into self-sufficient local government: 100% business rates retention, and believe that this proposals should be based on the principles of sustainability, equality, and support for a strong relationship between the voluntary sector and local authorities.**
- We are concerned about that with the introduction of 100% business rate retention and the phasing out of the revenue support grant means that all local authorities – regardless of whether they are part of a devolution deal or not – will struggle to be financially dependent on their local economies for the revenue that they need to deliver local services.
- Voluntary organisations have reported a struggle to gain access to LEPs and to be included in conversations about devolution, public services and community developments.
- There is a real risk that without including the voluntary sector, local authorities and business leaders will inadvertently exclude the most vulnerable from having a voice in creating economic growth for their communities.
- We are concerned that devolution of responsibilities will not be "relatively predictable and stable over times". It is unwise to pass on more responsibilities to local government before the existing problems of financial strain and increased demand on services are addressed.

- We are greatly concerned that local authorities abilities to deliver key services, especially to the most needy and vulnerable in society, is considered of lesser importance then economic growth of businesses.
- We also question the stability of 100% business rates retention. The business rates tax base has a few very large payees that can account for a massively disproportionate part of the tax take. As well as increasing uncertainty this policy could create perverse incentives for local government that could ultimately harm economic growth.
- It is unclear whether local authorities will have the capacity, resources and most importantly the authority to be able to collect 100% business rates and to fight expensive and time consuming appeals.
- **We believe that the government should move towards a system of 100% charitable business rate relief, funded by central government, so that local authorities are not penalised from having high levels of social need.**
- This is a risk that the fiscal approach currently being followed could 'mainstream' inequality in the local government financing system. Those councils with a greater capacity for generating revenue through local business rates are placed in a far stronger position than poorer councils.
- **The 100% business rate retention could exacerbate, rather than mitigate, regional inequality – at a time when disadvantaged communities need support more than ever.**
- The voluntary sector has been proactive in discussing the impact that changes to local government could have. **There is a real need for the government and the voluntary to discuss the impact these changes could have on the voluntary sector.**
- **We believe that these proposals should be shelved until more certainty exists about devolution and the impact of the vote to leave the EU will have on local government and the people and communities it exists to help.**

Comments on self-sufficient local government: 100% Business Rates Retention

Finances of local authorities

We are concerned about that with the introduction of 100% business rate retention and the phasing out of the revenue support grant means that all local authorities – regardless of whether they are part of a devolution deal or not – will struggle to be financially dependent on their local economies for the revenue that they need to deliver local services. This is particulary true for areas with a historically low tax base. For example, Blackburn may have problems due to de-industrialisation, but Kensington and Chelsea will be starting from a strong position of growth and will have the resources and capacity to use the 100% business rates scheme to create economic growth. Although the government has provided some transitional grants for local authorities to manage this change, analysis has shown that the way funding allocation has been calculated means that some of the areas with the highest deprivation will not receive any of this funding, where richer areas will.

We are particularly concerned that there will be a lack of support for local authorities should their income significantly reduced from the 'business rates baseline'. While the consultation states that a safety net would still have to exist when a local authority has lost 7.5% of its baseline income from business rates, it is unclear what form this safety net will take. Furthermore, areas already supported by the safety net do not have the current ability to support existing local authority expenditure from business rates. It is logical to assume that under the 100% business rates retention scheme, with the removal of the Rates Support Grant, this problem will become exacerbated. Introducing 100% business rates retention does not necessarily mean that economic development will grow the tax base to meet demand for services. Moreover, the other big problem with the safety net principle is that if a local authority suffers from a slow erosion of their business rates (say 5% a year) that could have a massive impact over time. It is hard to see support from local authorities for a scheme that could have detrimental effect on their finances.

Since 2010 local government has suffered more than many other areas of government spending. The National Audit Office estimates a 37% real-term reduction in government funding to local authorities between 2010/2011–2015/2016. For many small charities and community groups this has created a crisis as local government small grant funding is disappearing. These smaller organisations are increasingly being understood as essential for building community cohesion, social capital and giving a voice to many people and communities who are often ignored. This value of the role of these organisations has gained greater recognition since the referendum result to leave the EU. Voluntary organisations have reported a struggle to gain access to LEPs and to be included in conversations about devolution, public services and community developments. There is a real risk that without including the voluntary sector, local authorities and business leaders will inadvertently exclude the most vulnerable from having a voice in creating economic growth for their communities.

The consultation also says that devolution of responsibilities should be “relatively predictable and stable over times” yet this ignores that existing responsibilities are not. It seems unwise to pass on more responsibilities to local government without addressing existing problems of financial strain and increased demand on services. The consultation places the risk of demand on local authorities’ services growing faster than local tax resource beneath that of the risk that without these proposals local authorities will have no incentive to develop local economic growth. We disagree with this analysis and voluntary organisations on the ground are already experiencing the impact of demand rising faster than local tax resources.

We are greatly concerned that local authorities abilities to deliver key services, especially to the most needy and vulnerable in society, is considered of lesser importance then economic growth of businesses. These problems need dedicated funding and investment by local and central government and cannot just be viewed as a side-lined benefit of economic business growth.

Stability of 100% business rates retention

We also question the stability of 100% business rates retention. The business rates tax base has a few very large payees that can account for a massively disproportionate part of the tax take. As well as increasing uncertainty this policy could create perverse incentives for local government that could ultimately harm economic growth. For example, Sheffield City Council receives 18 per cent of its business rates from the Meadowhall shopping centre. This could mean they prioritise the needs of this large shopping centre over other businesses, charities and community groups, even though growth is often driven by smaller and start-up businesses that can pay no or very little business rates. This problem, of uneven focus, could also been seen under the proposal that local authorities pool their risks together in a Combined authority. This could result in serve inequalities across a region as one area of economic output could be given greater prioritisation than another.

Further concerns are raised by local authorities’ ability to collect 100% business rates. Already local authorities in England are forced to write off nearly £1.5 million in business rates due to a loophole in licensing and business laws. Furthermore, English business rates are subject to appeals worth £4.2 billion or 17.5% of business rates income in 2013/14[1] for local authorities. It is unclear whether local authorities will have the capacity, resources and most importantly the authority to be able to collect 100% business rates and to fight expensive and time consuming appeals.

This proposal will also create much more uncertainty at a time of unprecedented uncertainty, coming as it does following the vote to leave the EU, the unknown impact of devolution for local communities and the upheaval in local government created by cuts and austerity.

Charity rate relief

Charitable organisations have mandatory 80% business rate relief, with councils being able to add a discretionary further relief rate of 20%. Currently the mandatory charitable rate relief is not due to be subject to change, helping to prevent a loss of £1.5bn to the voluntary sector. However, the pressure on business rates locally will put the remaining £40m that the sector receives in discretionary rate relief under threat. Moreover, the new system of mandatory chartiable rate relief means that local authorities are now responsible for paying 50% of the costs of the relief (rather than central government paying for all the reliefs) means that local authorities in areas where there are significant numbers of charities are disadvantaged.

These relief rates are a vital life line for charities and for voluntary organisations providing public services, a reduction in discretionary business rate relief could prove problematic for maintaining financial sustainability. It would also increase the cost of delivering public services because many organisations that deliver public services receive mandatory rate relief. We are concerned that under the 100% business rates retention scheme the focus on LEP's and economic growth through businesses means the value of the charity sector in promoting a social economy becomes neglected by many local authorities. With the focus on localism (either through devolution deals or not) there is serious concern that local authorities reviewing charity reliefs will see them as a burden, and not the economic and social benefit for a community that they are. This problem is compounded by the new system of funding reliefs outlined above.

Furthermore, under the current system there has been a creation of a 'postcode lottery' for charities that are granted 100% business rate relief. This will be exacerbated under the proposed 100% business rates retention as authorities will struggle to grant further discretionary reliefs due to a reduction in income. Again, areas that have seen the greatest amount of cuts in local government income are often the areas that face the most demand on their public services; which charities pay a key part in providing.

[1] http://www.local.gov.uk/documents/10180/11531/The+story+so+far+-+business+rate+retention.pdf/2175c47c-6916-4b93-add8-c2201db60482

Moreover business rate relief is the only charitable tax relief which is dependent on location. Unlike Gift Aid or Inheritance Tax Estate Relief, there is no variation based on location. This is because Parliament has already decided what charitable activities are and there is no schedule of priorities between them. Business rate relief is an anomaly in that this local variation is permissible.

NAVCA and CFG both advocate that all local authorities in England should grant charities 100% business rate relief to help with the economic stability of the sector and their ability to provide key services and benefit to the wider communities. We also believe that central government should fund chartiable business rate relief so that local areas are not penalised for having greater local needs.

Regional inequality

This is a risk that the fiscal approach currently being followed could 'mainstream' inequality in the local government financing system. Those councils with a greater capacity for generating revenue through local business rates are placed in a far stronger position than poorer councils. It's conceivable that voluntary organisations working in areas of low business activity will see a decrease in funding. This, combined with a rise in the threshold for business rates relief for small businesses from £6,000 to £15,000, could see public service providers struggle to bid for a smaller pool of funding. Under proposals for the creation of pooled areas of local authorities to spread the risk of income reductions the voluntary sector might struggle to get our voices heard in such a large pool of potential fund recipients.

Public services benefit from collaboration and sharing. These proposals create a basis for competition between local authorities. This will reduce the potential for the service improvements and savings that collaboration brings. It will make local authorities more isolationists as they are forced to compete with near neighbours.

There is also a danger that the 'social' foundations of growth are undermined due to funding restrictions. Areas which have high levels of health and education as well as low levels of crime are likely to be more economically successful, with both economic and social benefits feeding into each other as a positive feedback loop. By contrast, areas with lower levels of health and education as well as higher levels of crime are likely to see a drag on economic performance, with economic and social disadvantages feeding into each other to create a negative feedback loop. Voluntary organisations are critical to improving the social foundations of growth, but will devolved deals give authorities the ability to strengthen those foundations?

Finally, there is the potential impact of tax competition with devolved areas forced to compete with each other in order to attract businesses. This could further reduce the resources available for funding economic regeneration and the delivering of social services, creating a 'race to the bottom'.

The 100% business rate retention could exacerbate, rather than mitigate, regional inequality – at a time when disadvantaged communities need support more than ever. For the voluntary sector, most needed in just these areas, the importance of engaging in the devolution process is clear. It is not enough for voluntary organisations to assume that business leaders, LEPs and local authorities will decide to include the sector when making financial decisions that could impact on organisations beneficiaries.

We are concerned that the proposal for 100% Business Rates Retention will harm local people and communities as it risks increasing inequality between and also within local government areas. We also believe that it will place further pressure on local government budgets which in turn will mean less support for charities and community groups supporting many of the most disadvantaged people and communities.

The consultation suggests that the reforms will increase self-sufficiency yet it also says that this will be fiscally neutral. These two statements are not consistent. These plans may well decrease self-sufficiency as less wealthy areas will become even more dependent on external support and be less able to set their own destiny.

This proposal and the inequality it creates between areas because of the vast differences in ability to raise funding through business rates just gives more power to central government. There is a danger that will only increase levels of disengagement with politics and local democracy.

There is an underlying assumption within the consultation document that local government can easily create economic growth – or that they can be barriers to growth. There is no acknowledgment of the differences between areas. It implies that lower business rates alone are the key to growth. The areas with the highest levels of Business Rate revenue per head tend to share geography rather than any other characteristic. It is important that the efforts of local authorities to support businesses in less affluent areas are acknowledged.

Devolution and the Voluntary Sector Summit

The voluntary sector has been proactive in discussing the impact that changes to local government could have. There is a real need for the government and the voluntary to discuss the impact these changes could have on the voluntary sector. At CFG, Locality, NAVCA and Children England's Devolution and the Voluntary Sector Summit, key stakeholders in the voluntary sector laid out key financial principles to underpin good devolution:

1. No financial settlement can be agreed with an area until there has been an opportunity to map and assess what needs and resources (including voluntary and private sector assets) there are in the local area.
2. Rebalancing and redistribution should not be abandoned, there needs to be a way for distributing resources post-devolution so that inequalities are not locked in.
3. A good process supports better outcomes - financial decisions should be made in an open and democratic way.

These three financial principles are supported by a further thirteen principles (on voice and advocacy and public service reform) to help promote growth, equality and opportunity for communities and people across England.

Responses to specific questions in the consultation document.

Question 15: This mentions 'riskier' hereditaments. When talking about risk it is important to understand who pays for risks that do not pay off. With local authority funding it will ultimately be local people in that area who suffer through no fault of their own.

Question 21: If local government is to have the power to reduce the multiplier they should also be given the ability to raise it. Otherwise there is an assumption that local government funding can only be on a downward trajectory, which is something that should be decided by communities themselves, rather than imposed by central government.

Questions 27 & 31: LEPs, although their make-up varies across the country, are often viewed as un-represented by smaller businesses and the voluntary sector, who are a major employer. Whilst consultation with local businesses is desirable, LEPs have not always proved themselves to be an appropriate bodies to provide genuinely accountable consultation. We therefore reject the proposal that LEPs should be given powers to approve levies and infrastructure projects as they do not represent wider community engagement.

Question 29: There should be a wider definition of infrastructure that should include social infrastructure including social assets and investing in prevention.

Question 30: We support multiple levies as a way to get a broader range of local priorities funded.

Conclusion

The proposal for local government to retain 100% of Business Rates is flawed. It is flawed because it only looks at one element of the complicated picture of local government funding. A whole new settlement should be sought that addresses all funding, local government responsibilities and devolution. As this consultation looks at proposals concerning just one element we cannot support the proposals for local government to retain 100% of business rates and to phase out the Revenue Support Grant.

Although the aim expressed in the consultation document is to make the system simple, it appears very complicated. Any system that starts out with wide variations in the ability to raise income will invariably require a way to make the system fair. There is a worry that this will either create a very complex system but fair or a very simple but unfair system.

There is an underlying assumption within the consultation document that local government can easily create economic growth – or that they can be barriers to growth. There is no acknowledgment of the differences between areas. It implies that lower business rates alone are the key to growth. The areas with the highest levels of Business Rate revenue per head tend to share geography rather than any other characteristic. It is important that the efforts of local authorities to support businesses in less affluent areas are acknowledged.

For these reasons we recommend for the proposal for 100% business rates retention to be scrapped.

This should be replaced by a wider consultation process bringing together central government, local government, voluntary organisations, businesses and, most importantly, citizens to decide on how local government should be funded in the future. This would include what forms of taxation should be used to fund local authorities and what power they would have to vary these forms of taxation.

At the very least, the proposals should be shelved until more certainty exists about devolution and the impact of the vote to leave the EU will have on local government and the people and communities it exists to help.