West London Alliance
Economic Prosperity Board
Business Rates Retention

Introduction

The United Kingdom operates one of the most centralised political and fiscal systems in the world. Nearly 90% of taxes are raised and collected centrally, which are then reallocated to government agencies, regional and local authorities. This compares to 50% in the United States and far less in many other countries globally.

Most of the taxes raised in the United Kingdom accrue to the Treasury. These include income tax, corporation tax, inheritance and capital gains tax and VAT. Business rates are collected by Councils, but remitted to central government, who redistribute 50% of this funding back to local authorities. In London, this 50% is split 60:40 between the boroughs and the Greater London Authority, meaning that only 30% of business rates are currently retained by boroughs.

Critics of the fiscal system in the United Kingdom argue that the centralised nature of the system stifles innovation, and restricts the investment in infrastructure at a regional and local level that would promote greater economic growth.

Arguments have been made for some time about greater devolution of tax and spending powers to local authorities. From a London context, the London Finance Commission has argued for London to retain a greater share of taxes raised in the capital, rather than it being gathered centrally and then redistributed.

In 2015, the Chancellor, George Osborne, announced that business rates would be fully devolved to local government by 2020. The process for this to happen, and the mechanics of the system that will emerge, are still subject to uncertainty. However, consultation is underway and some grants are starting to be devolved under the new system. London has been identified as a pilot and will develop a system of business rate retention by 2019.

There are risks and issues associated with business rates being fully devolved to local government as a way of funding services previously funded by Revenue Support Grant (RSG) and ringfenced grants (such as Public Health). For example, local government expenditure is typically driven by demographics and can be counter cyclical (ie. is greater when the economy performs weakly) whereas business rates are cyclical (ie. generate more income when the economy performs strongly). The nature of the economy is changing, to the extent to which a tax based on business property no longer accurately reflects economic activity. There are also risks associated with business rates being devolved to local government to fund services, while the setting of the rates themselves remains the responsibility of central government. Decisions on reducing business rates to stimulate the

economy, or the introduction of discounts and exemptions, will be taken centrally, while the risk of reducing income will sit locally.

However, notwithstanding all of these points, it is important that Councils carefully consider the development of business rate retention to ensure that the system that develops is fit for purpose and properly reflects the risks and opportunities that exist.

Current consultation

The government consulted on the overall principles of a business rate retention scheme in the autumn of 2016. At the beginning of 2017, a more technical consultation was released. The deadline for response is 3 May 2017. The questions posed are as follows:

1: What are your views on the proposed approach to partial resets?

2: What are your views on how we should measure growth in business rates income over a reset period?

3: What are your views on the Government's plans for pooling and local growth zones under the 100% Business Rates Retention system?

4: How can we best approach moving to a centrally managed appeals risk system?

5: What should our approach be to tier splits?

6: What are your views on proposals for a future safety net under the 100% Business Rates Retention system?

7: What are your views on our proposals for the central list?

Rate retention from the perspective of West London

This section sets out the issues where a common approach across West London boroughs can be found, and the issues that would need to be out of scope, should a West London Alliance submission be made to the current consultation. This section has been developed following an initial discussion with West London Alliance Leaders in February, and further views expressed by Chief Finance Officers.

Arguments around **underlying funding levels** are recommended to be out of scope for a West London response. Firstly, this is part of a separate consultation around "fair funding". Secondly, funding levels and funding pressures vary considerably across the sub region, and the development of a common position is not considered feasible.

The concept of a **West London pool** for business rates is not recommended to be pursued, at least not at this stage. A pooling arrangement for the whole of London is being considered at the moment, and will be determined through London Councils Leader's Committee in the autumn. A key factor in London will clearly be the **split of business rates between the GLA and the boroughs**, and this discussion no doubt will be captured by London Councils in responding to business rate retention proposals.

Issues around business rates from the **expansion of Heathrow** are also recommended to be out of scope at this stage. Uncertainty exists around the timescales, extent of business rate growth, and the impact that expansion will have on the local area. All of these are vitally important factors in determining the approach to business rate distribution and therefore it is currently not possible to capture this in a consultation response at this stage. Notwithstanding this situation, West London boroughs are interested in how any surplus is managed, and certainly agree that it should remain within the sub-region rather than be redistributed over a wider area.

There is common ground across West London, and indeed London more widely, that **additional responsibilities** should be devolved to London alongside the surplus of business rates that accrues to London by 2020 compared to indicative levels of funding at that point. These responsibilities should align to areas where West London boroughs, individually and collectively, can have a real positive impact on outcomes for local people. The table of additional grants that London Councils have lobbied to be included in business rates is set out below. West London boroughs have indicated strong support for many of these, for example Adult Education and Public Health, while expressing slightly more concern over 16-19 funding and transfers in responsibilities for welfare budgets.

Existing grants & new responsibilities - Suitable candidates for transfer in Addition to TfL Capital Grant

	Existing grant or responsibility	Estimated London value in 2019-20 (£bn)
Adult Education Budgets	New responsibility	0.227
Skills - 16-19 funding	New responsibility	0.449
Careers Service	New responsibility	0.009
Work and health programme	New responsibility	0.014
Youth Justice	New responsibility	0.054
Valuation Office Agency	New responsibility	0.05
Affordable Housing capital funding	Grant	0.417
Transport capital (outside London)	Grant	n/a
Revenue Support Grant	Grant	0.538
Public Health Grant	Grant	0.628
Early Years Block of DSG	Grant	0.748
Improved Better Care Fund	Grant	0.247
Independent Living Fund	Grant	0.019
Housing Benefit Admin Subsidy	Grant	0.033
Council Tax Support Admin	Grant	0.015
Rural services Delivery Grant	Grant	n/a
Total grants & responsibilities		**3.448**
Total "headroom" in 2019-20		**3.975**
Remaining capacity		**0.527**

The second area of agreement across West London is the support for **local growth zones**. Infrastructure is a key enabler of growth, and the current business rate and tax system does

not incentivise investment in infrastructure at a local level. A future system should encourage growth zones to promote economic activity and address the infrastructure requirements of the sub region. Local growth zones could encompass existing areas of growth such as Brent Cross, Wembley and Old Oak Common, but also capture other areas such as the Golden Mile in Hounslow and other emerging infrastructure requirements and growth opportunities in the area. A West London response may want to articulate the specific infrastructure requirements and opportunities within the area and the extent to which they will drive growth and benefit the economy as a whole.

A business rate retention system needs to consider the extent to which it **"rewards" growth** (by allowing boroughs or regions to retain increases in business rates) and the extent to which it "resets" the system to account for fluctuations in service demands. On balance, feedback from West London Finance Directors suggested that growth should be incentivised; however, the downside risk should be protected with a **5 year reset**.

Managing appeals is another important part of a future system. Feedback from West London Finance Directors suggest that appeals should be managed centrally funded through an annually reconciled top slice of business rates with residual funds allocated back to local authorities. This would reduce the risk of appeals to local authorities and equally leave the decision making around providing for appeals with the VOA/DCLG as they will be making decisions around revaluations and appeals.

There were no significant concerns expressed around the way the **central list** is currently managed, clearly any new arrangement that saw this changing would need to ensure that future delegated decision making did not give rise to conflicts (for example between London and elsewhere).

<u>Conclusion</u>

Many of the arguments made here mirror the London position, particularly around additional responsibilities and the retention of the proceeds of growth in the capital to invest in local infrastructure and stimulate future growth. It could therefore be argued that West London boroughs could support the London wide position rather than develop a sub-regional response.

However, given the opportunity to stress the importance of West London and the local infrastructure requirements, it is recommended that a West London response is developed to the current consultation in line with this paper.