Proposals for Business Rates Retention technical papers: An overview

1.1. On 18 July, the Department for Communities and Local Government published a consultation paper, *Local Government Resource Review: Proposals for Business Rates Retention*.

1.2. This set out proposals for a rates retention scheme to replace the current local government finance system, under which business rates are distributed as part of formula grant. A plain English guide to the proposals[1] was published alongside the consultation paper.

1.3. This overview provides a technical summary of how the scheme would work, and signposts the more detailed discussion of the various elements provided in a series of eight technical papers, published on 19 August.

Establishing the national business rates baseline

1.4. As explained in the main consultation paper, to deliver a fiscally sustainable system and avoid putting the Government's deficit reduction programme at risk, we will manage the business rates retention scheme within the expenditure control totals for 2013-14 and 2014-15 which were set out in the Spending Review 2010.

1.5. *Technical Paper 2: Measuring Business Rates* discusses how we propose to establish the *forecast national business rates* for 2013-14 and 2014-15. *Technical Paper 1: Establishing the Baseline* explains how we propose to *set aside* the difference between these forecasts and the expenditure control total. The *set aside* would be used to fund other grants to local government.

1.6. Since it would not be possible to alter the *set aside* until any reset, it would need to be based on the lowest (2014-15) expenditure control total. *Technical Paper 1: Establishing the Baseline* discusses how, in 2013-14, when spending figures are higher, the Government would distribute the difference in such a way as to ensure that no authority loses out as a result of this approach.

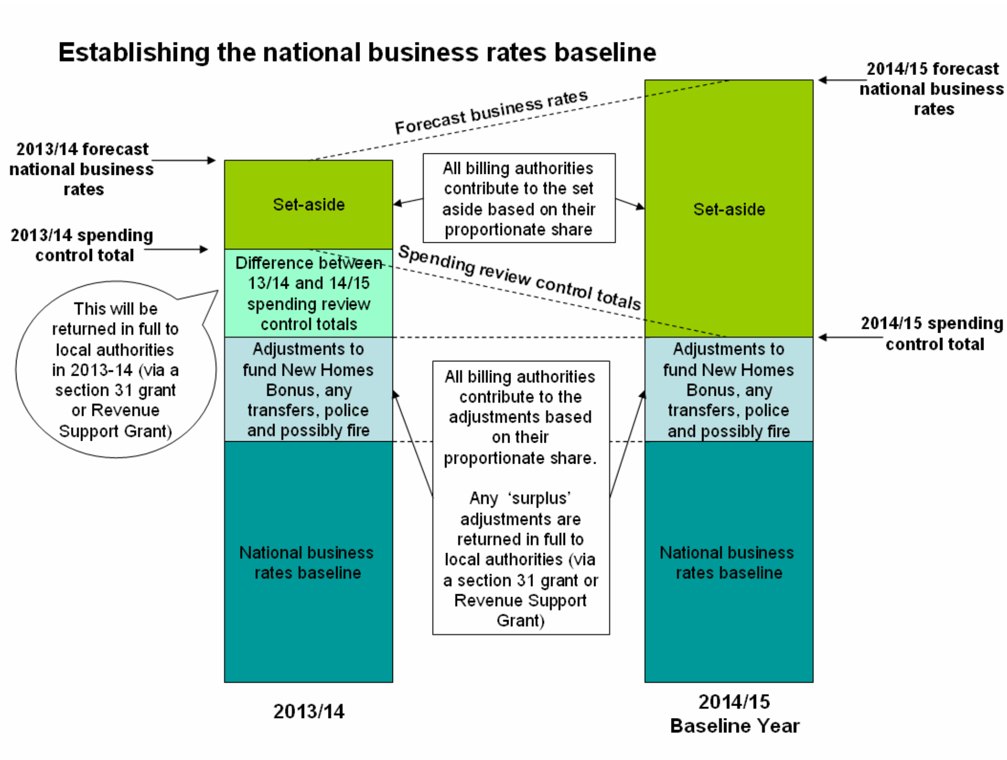
1.7. *Technical Paper 1: Establishing the Baseline* also discusses a series of further *adjustments* to the *forecast national business rates* to provide

[1] www.communities.gov.uk/documents/localgovernment/pdf/1947119.pdf

sufficient funding for the New Homes Bonus, any functions transferred to local authorities, police authorities and, possibly, single purpose fire and rescue authorities. *Technical Paper 3: Non-billing Authorities* discusses options for funding police and fire authorities in further detail.

1.8. The fo*recast national business rates* remaining, after the *set aside* and *adjustments*, would form the *national business rates baseline* for the purposes of the scheme. Any business rates growth achieved against that baseline would be retained by the local government sector.

1.9. This is illustrated below:



1.10. *Technical Paper 2: Measuring Business Rates* seeks views on proposals to establish a *proportionate share* for each billing authority. This would be the share of the aggregate business rates yield (after certain *allowable deductions* for items such as reliefs) that an individual authority collects, expressed as a percentage.

1.11. Each billing authority would contribute to the *set aside* and *adjustments* on the basis of their *proportionate share*. *Technical Paper 4: Business Rates Administration* discusses how such contributions to the *set aside* and *adjustments* would be paid to central government.

Providing a fair starting point through tariffs and top ups

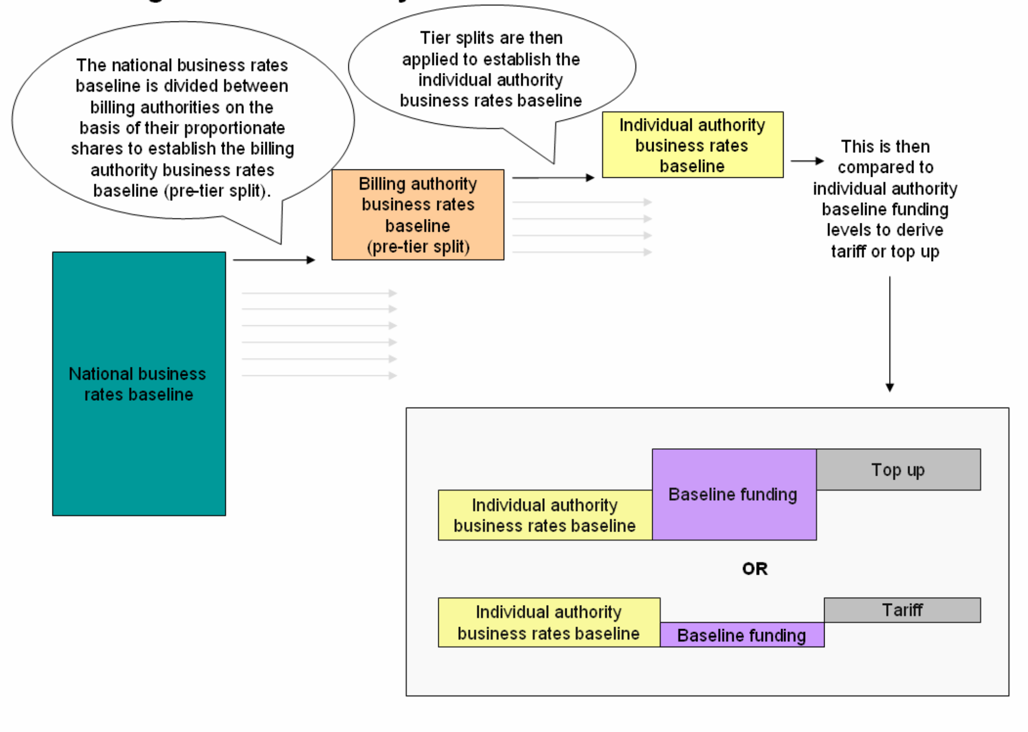
1.12. As set out in the main consultation paper, the Government intends to establish a fair starting point, so that no authority loses out as a result of its business rates base at the outset of the scheme.

1.13. It proposes to achieve this through a rebalancing of resources in the first year of the scheme. Authorities with baseline business rates in excess of their baseline funding would pay a *tariff*, whilst those with less business rates than their baseline funding would receive a *top up*. *Tariffs* and *top ups* would be self funding at the national level.

1.14. *Technical Paper 2: Measuring Business Rates* discusses how we propose to establish *individual authority business rates baselines*, from which *tariffs* and *top ups* would be derived. Billing authorities' *proportionate shares* would be used to apportion the *national business rates baseline* and determine *billing authority business rates baselines (pre-tier split)*. In two tier areas, billing authorities' baselines would be further apportioned between billing authorities and their county councils to establish *individual authority business rates baselines. Technical Paper 3: Non-billing Authorities* seeks views on *tier-split shares*.

1.15. *Individual authorities' business rates baselines* would then be compared with their *baseline funding levels* to determine *top ups* and *tariffs*, as illustrated below. As explained in the main consultation paper, we propose to establish individual authorities' *baseline funding levels* on the basis of 2012-13 formula grant, and *Technical Paper 1: Establishing the Baseline* seeks views on detailed options.

Establishing individual authority business rate baselines



1.16. *Technical Paper 4: Business Rates Administration* discusses how *tariffs, top ups* and *tier split shares* would be paid.

A strong incentive for growth, with protection from a safety net

1.17. *Tariffs* and *top ups* would be self-funding and would be fixed in future years, so that authorities benefit from achieving business rates growth.

1.18. *Technical Paper 1: Establishing the Baseline* considers the implications of fixing *tariffs* and *top ups*, including options for dealing with any mergers or boundary changes, changes in local authority functions and new burdens that arise between resets. It also discusses proposals for the future of revenue support grant and for retaining a local government finance report.

1.19. *Technical Paper 5: Tariff, Top up and Levy Options* discusses how the benefit an authority sees from growing its business rates would be affected by its *gearing* (i.e. the relationship between its *individual authority business rates baseline* and *baseline funding* level). It seeks views on options for index-linking *tariffs* and *top ups* to the retail prices index or fixing them in cash terms, and considers how these options would affect different authorities depending upon their *gearing*.

1.20. An authority's *gearing* will also affect the extent to which it is exposed to the natural volatility in the rating system, which is discussed in *Technical Paper 6: Volatility.*

1.21. Local authorities will be responsible for managing a certain degree of natural volatility in business rates income, and may choose to pool with other authorities to smooth the impact. Authorities that experience significant negative volatility in their business rates income - or that are less able to respond to the growth incentive – would benefit from support from the *safety net* proposed in the main consultation paper. *Technical Paper 5: Tariff, Top up and Levy Options* discusses options for *safety net* support in further detail.

1.22. *Technical Paper 5: Tariff, Top up and Levy Options* also discusses options for the levy to recover a share of disproportionate benefit from business rates growth. As explained in the main consultation paper, the proceeds of the *levy* would be used, in the first instance, to fund the *safety net*. *Technical Paper 4: Business Rates Administration* explains how we propose to capture information about authorities' *pre-levy income*, from which to determine their liability for the *levy* and about authorities' *post-levy income*, from which to determine their eligibility for support from the *safety net*. It also discusses the flows of money and information that will be required in two tier areas between billing authorities and their county councils.

1.23. We have published an *interactive calculator* to illustrate the interactions between the different *tariff*, *top up* and *levy* options, and the effects that different combinations could have on authorities, depending on their gearing. The *interactive calculator* does not predict the outcome of the scheme on local finances. This will depend on local circumstances, such as individual authorities' baseline business rates, baseline funding levels and future business rates growth; on national circumstances, including future growth in the retail prices index and, consequently, in the centrally set tax rate; and on the final design of the rates retention scheme following consultation. However, the *interactive calculator* enables users to explore and compare the possible effects of different combinations of *tariff, top up* and *levy* options, based upon their own assumptions about local circumstances and the future tax rate.

Revaluation and transition

1.24. Business properties are re-valued every five years to reflect changes in the property market. The Government adjusts the national non-domestic multiplier rate to ensure that overall, the tax burden on business does not increase as a result of revaluation. This means that - whilst businesses in particular sectors or locations that have seen above average rental growth may see their contribution to the overall business rates yield increase - revaluations do not generate any additional revenue at national level. They simply adjust the contribution each business makes to the overall rates yield to reflect changes in the rental value of its property relative to that of others.

1.25. Because central government ensures revaluations do not generate any additional revenue, allowing the impact of revaluation to feed through would introduce significant turbulence in local budgets. Areas could see the value of business property in their area increase, yet still experience significant drops in income at revaluation - only those seeing above average growth in rental values would see their business rates increase. At the 2010 revaluation, over 200 authorities saw reductions in the amount of business rates collected locally. *Technical Paper 7: Revaluation and Transition* discusses proposals to adjust *tariffs* and *top ups* at revaluation to ensure, as far as possible, that business rates income at local level is unaffected.

1.26. Generally, a transitional relief scheme is put in place at each revaluation to phase in significant increases in rates bills for businesses whose rental values have grown significantly more than the average. Transitional relief is funded by also phasing in reductions in bills for businesses whose rental values have grown significantly below the average. Whilst the transitional relief scheme is designed to be self funding as far as possible at the national level, at local level it would significantly distort business rates income. The Government therefore proposes to manage the transitional relief scheme outside the business rates retention scheme, as discussed in *Technical Paper 7: Revaluation and Transition*.

Resetting the system

1.27. The proposals set out in the main consultation paper include the option for government to reset the system if it was felt that resources no longer sufficiently met service pressures within individual local authority areas (for example, because of population movements, or the characteristics of the area changing).

1.28. A *reset* would involve re-assessing individual authorities' *baseline funding* levels, potentially on the basis of a completely new assessment of need rather than formula grant, and recalculating *tariff* and *top ups* accordingly. *Technical Paper 1: Establishing the Baseline* discusses and seeks views on the options for resetting the system, including the timing and frequency of *resets*.

1.29. Business rates income from new renewable energy projects, together with any uplift in business rates in Enterprise Zones, would not be included in any reset. This reflects the Government's commitments to enable communities hosting new renewable energy projects to retain all of the additional business rates they generate; and to enable local enterprise partnerships to retain all additional business rates in Enterprise Zones for 25 years.

1.30. *Technical Paper 8: Renewable Energy Projects* seeks views on which properties should qualify as new renewable energy projects. *Technical Paper 4: Business Rates Administration* explains how we propose to identify the business rates from new renewable energy projects and the uplift in business rates in Enterprise Zones, in order to ensure that they are disregarded in assessing liability for the *levy* recovering a share of disproportionate growth and in any *reset*.

Responding to this consultation

1.31. Taken together, the consultation paper and technical papers raise a number of questions about the proposed rates retention scheme, on which the Government is seeking views. The consultation will close on Monday 24 October 2011. Details of how to respond can be found on page 7 of the main consultation paper[2].

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[2] www.communities.gov.uk/documents/localgovernment/pdf/1947200.pdf