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BRIEFING PAPER

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Reviewing and reforming local government finance

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Summary

This note covers matters of current interest in local government finance: how business rate retention works; the Government's proposals for changes to the system; the Government's Fair Funding Review; and the 2020 'fundamental review' of business rates.

The policies covered in this note have effect in England only. Responsibility for business rates, and for local government generally, is devolved to Scotland, Wales and Northern Ireland. For a more general explanation of the business rates system in England, see the Library briefing paper *Business rates*. For more details on the 2017 revaluation of business rates in England, Wales and Scotland, see the Library briefing paper *Business rates: the 2017 revaluation*.

1. The Business Rate Retention Scheme

The Business Rate Retention Scheme (BRRS) governs a substantial proportion of local authority funding in England. This section explains the workings of the scheme at present.

As of 2013, local government retains 50% of business rates revenue (the 'local share') and passes 50% to central government (the 'central share'). Individual billing authorities (district and unitary councils) collect rate revenue from ratepayers (see the Library briefing *Business rates*). A 'tariff' or 'top-up' element is then applied to each authority's 50% 'local share'. The aim of the tariffs and top-ups is to ensure that local authorities do not have access to disproportionately low or high business rate revenue, as levels of rate revenues vary widely between local authorities across England.

Local authorities will then retain up to 50% of additional business rate revenue that they raise in the period 2013-22 (the 'retention period'). 'Additional revenue' is revenue above the 'business rates baseline', based on the authority's average business rate revenue in 2011-12 and 2012-13. This is subject to a 'levy' of between 0% and 50% on the retained growth (see section 1.2 below).

The intention of the system is to encourage local authorities to use local policy – such as housing, planning and economic development policies – to grow their local economies and to be rewarded for doing so by extra revenue.

1.1 Tariffs and top-ups

Each authority's tariff or top-up level is based on the difference between the rate revenue it receives (the 'business rates baseline') and the **baseline funding level**. The baseline funding level is the amount of funding Government determines that an individual authority needs from business rates to deliver local services. The tariff or top-up is fixed in real terms for the duration of a retention period (it is uprated annually to take account of inflation).[1] Fixing the tariff or top-up means that individual local authorities automatically retain their share of revenue growth.

Fixing the tariff and top-up levels has two effects. First, growth is retained against the baseline, meaning that authorities benefit from **growth**, not revenue levels per se. This prevents authorities with strong local economies from 'coasting' by relying on rate revenues that are already high. Second, fixing the tariff and top-up levels makes local authorities' revenue levels predictable. Changing the tariff or top-up

[1] Tariffs and top-ups were adjusted from 2017-18 to take account of the effects of the rate revaluation coming into effect in that year. This was done to neutralise any individual authorities gaining or losing revenue purely as a result of the revaluation. Tariffs and top-ups have also been adjusted for 'pilot' authorities (see section 2.3 below).

regularly would mean that local authorities could not be certain that they would benefit financially from their policies, as intended by the BRRS.

Figures 1 and 2 show examples of the outcomes for a tariff and top-up authority respectively. In Figure 1, a 'tariff authority' collects £40 million in rate revenue in year 1. The 'central share' is 50% (£20 million). A £15 million tariff (the pale block at the top of each bar) is then applied. Thus the authority has access to £5 million in rate revenue in year 1.

In year 2, the tariff authority collects £44 million in rate revenue. The central share is therefore £22 million. The tariff remains at £15 million. The authority retains the remaining £7 million (the two middle parts of the bar). This is £2 million more revenue than it had access to in year 1.

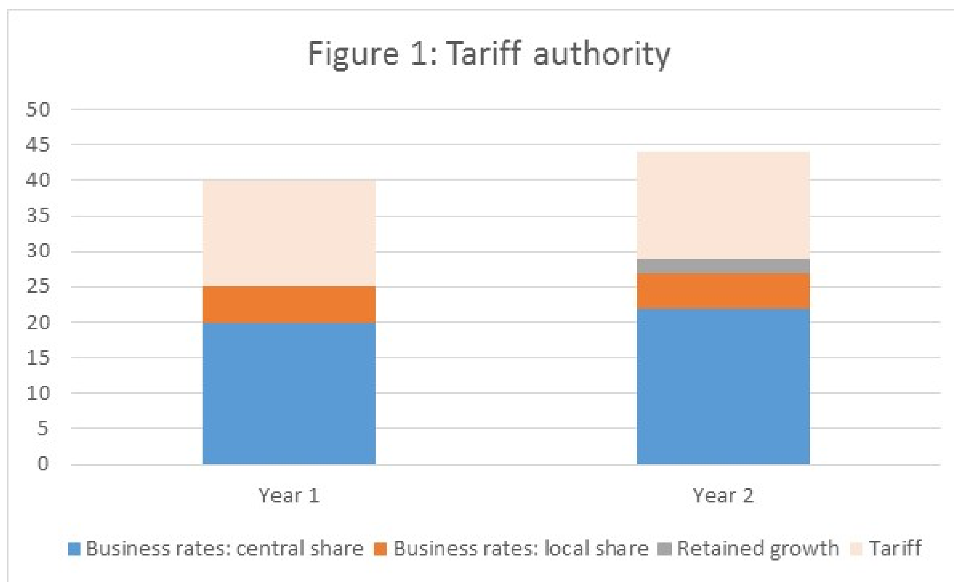
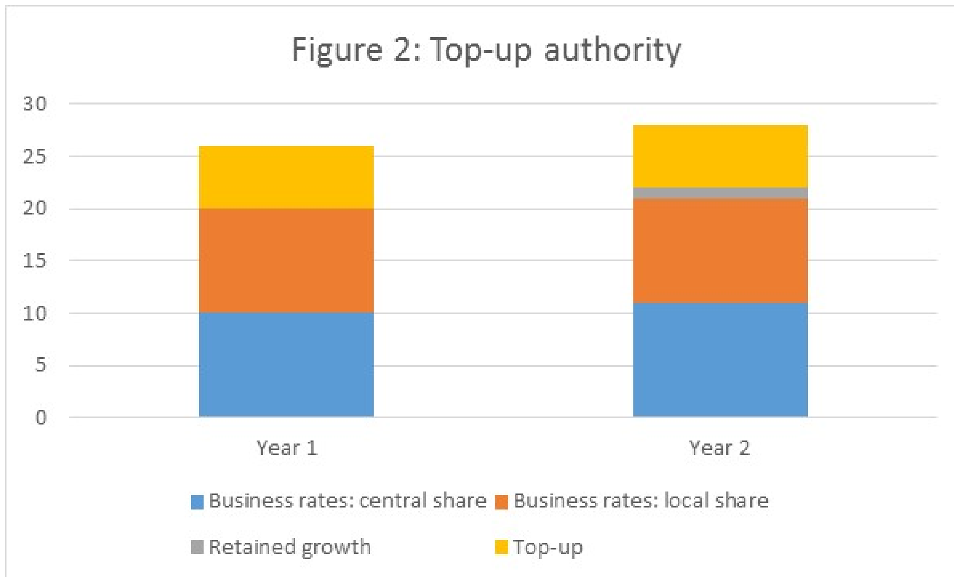


Figure 2 shows the effects on a top-up authority. The authority collects £20 million in rate revenue in year 1. £10 million, or 50%, goes to the central share. A top-up of £6 million is added, meaning that the top-up authority has £16 million in rate revenue in year 1.

In year 2, the top-up authority collects £22 million in rate revenue. Therefore, £11 million goes to the central share. The top-up remains at £6 million. The authority retains an additional £1 million compared to year 2, and has access to a total of £17 million in rate revenue (£10m + £6m + £1m).



These figures only show changes to business rate revenue. Local authorities also receive revenue from council tax, central grants, and local fees and charges. The impact of the BRRS on an authority's overall revenue will be dampened by these other sources of revenue.

Other things being equal, tariff authorities are more exposed than top-up authorities both to gains and losses from rate retention. This is because top-ups represent guaranteed income: they are not affected by an authority's own rate revenue. In a tariff authority, rate revenue is likely to form a larger proportion of the authority's overall funds, and thus changes to it have a sharper effect on the authority's total funding than in a top-up authority.

Tier splits

In practice, in most areas of England more than one authority will share the 50% of local revenue. In London, 20% of the total revenue goes to the GLA and 30% to the boroughs. In other two-tier areas, 40% of revenue goes to district councils, 9% to the county council, and 1% to the fire and rescue authority.[2] This is known as the 'tier split'. Alternative tier splits have operated in many areas as part of the various rate retention pilots (see section 2.3 below).

The normal tier split, combined with county councils' larger spending commitments, means that all county councils are top-up authorities, whilst many district councils are tariff authorities. The tariff may be substantial, leading to some such authorities retaining only some 10%-20% of the rate revenue they collect. However, such authorities will still retain up to 50% of *additional* rate revenue.

1.2 The 'safety net' and the 'levy'

Retention of 50% of revenue growth may be subject to a further levy on authorities with very high revenue growth. Each tariff authority has a

[2] Where county councils handle fire and rescue services, they retain 10% (9% + 1%) of rate revenues.

'levy rate', varying between 0% and 50%.[3] An authority which has a 0% levy rate will keep all of its growth in revenue. An authority with a levy rate must pay that percentage of their growth in revenue to the Government.

The purpose of the levy is to ensure that authorities with very high potential to increase their rates do not benefit disproportionately from the system.

Authorities are also guaranteed that their business rates revenue will not fall more than 7.5% below their 'business rates baseline'. This is known as the 'safety net'. Where an authority's revenue falls below that level, it will be topped up to reach that level.

The initial intention of the BRRS was for the levy to pay for the safety net. However, in some financial years, the safety net has been paid for via a 'top-slice' of rate revenue at the beginning of the year.

1.3 Resets

When it was introduced, the BRRS was to be subject to a 'reset' in 2020 (seven years after it began). At a reset, tariff and top-up levels would be recalculated, based on a new needs assessment. This would ensure that authorities did not gain or lose disproportionately over time.

At present, a reset is to take place on 1 April 2022 (see section 2.1). This will consist of implementing the outcome of the Fair Funding Review (see section 3). This date has been postponed twice, firstly from 2020 to 2021 and then from 2021 to 2022.

The Institute for Fiscal Studies said:

> …it will therefore be important to have broader resets of the redistributive tariffs and top-ups to prevent divergences in relative funding ratios from growing indefinitely, and to stop certain authorities becoming trapped on the disincentivising safety net. The frequency with which tariffs and top-ups are reset, and the extent to which any divergences in the intervening period are offset at resets, are key policy choices for the government as it develops its BRRS policy.[4]

The Government's July 2016 consultation *Business rates reform: call for evidence on needs and redistribution* invited views on how often the reset should be applied.[5] It suggested examples of a short period (5 years) or a long period (20 years). It also floated the idea of a 'partial reset':

[3] Authorities' levy rates can be found in the Core spending power: supporting information spreadsheet within the 2016-17 local government finance settlement. The levy rates were set at the outset of the BRRS in 2013-14 and remain the same from year to year.

[4] Neil Amin-Smith, David Phillips, and Polly Simpson, *Spending needs, tax revenue capacity and the business rates retention scheme*, Institute for Fiscal Studies, February 2018, p40

[5] This was a consultation document related to proposals for 100% business rate retention (see section 2).

> Under a partial reset we would still adjust for changes in relative need and business rates income but to a lesser extent that under a full reset.[6]

This would mean that individual authorities would retain a proportion of growth permanently. Put another way, a certain amount of growth in the current 'retention period' (2013-22) would be insulated from the needs assessment when the 'reset' takes place. David Phillips, of the Institute for Fiscal Studies, said:

> A partial reset can be seen as an attempt to trade-off the objectives of "equalisation" on the one hand and "incentives" on the other: councils can retain some (but not all) of the growth beyond the end of the period…The appropriate length of time between reset and % reset to adopt should depend on:
>
> - How large divergences in revenues may grow to be in the medium and long term (i.e. do revenue divergences grow between councils or do revenues revert to mean);
> - The extent to which one believes divergence in revenues (and spending needs) reflects impact of council decision making versus wider economic trends. If latter, the "incentive" is not particularly relevant: it is just risk;
> - The tolerance for divergence in revenues (and resulting impacts on service provision) by policymakers and the public.[7]

The Government will also explore the possibility of a transitional period following the reset (see section 3.3 below). This would aim to avoid individual authorities struggling to manage substantial falls in their funding resulting from the reset.

The Government's December 2018 consultation on 75% rate retention introduces the concept of a 'phased reset'. This would involve retaining each year's growth or loss in rates for a fixed number of years, but no longer: the consultation suggests five years. This has affinities with the current operation of the New Homes Bonus. The Government indicated that this option was currently preferred to either a full or partial reset, but it invited further views.[8]

A full reset potentially provides local authorities with an incentive to hold back development that would raise revenue until after the reset takes place. Otherwise, revenues that appear late in the retention period might be taken into account by, and redistributed at, the full reset.[9] That incentive would be reduced by a partial reset along the lines outlined above.

Also, a phased reset and a partial reset could in principle operate alongside one another. For instance, a phased approach could permit local authorities to retain any growth in rates for a period of five years; growth that had been achieved more than five years earlier would then

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6 DCLG, *Self-sufficient local government: 100% business rate retention*, July 2016, p.25
7 David Phillips, "Response to government consultation on business rate retention", 17 June 2017
8 MHCLG, *Business rate retention reform*, December 2018, p11-15
9 MHCLG, *Business Rates Retention Reform*, December 2018

be disregarded (and thus be redistributed). A partial reset might provide that a local authority should be able to retain permanently some of the growth that the local authority achieved more than five years previously.

1.4 Pools

Local authorities are permitted to form 'pools' for the purposes of the retention scheme. A business rates pool has a single tariff and top-up level applying to the entire pool. The pool members themselves decide on how rate revenue should be divided within the pool. The various pilots of higher levels of rate retention (see section 2.3 below) are legally constituted as pools.

In formal terms, pools must be re-established for each financial year. A list of pools can be found in the documentation of each year's local government finance settlement. Though most pools so far have consisted of authorities that are geographically close – e.g. a county and its districts, or groups of metropolitan boroughs within a city-region – there is no requirement for the members of a pool to be geographically contiguous.

The Centre for Cities report *Beyond Business Rates* proposes that a more comprehensive approach should be taken to the pooling of business rates across functional economic areas. It states that, in city regions, centre-city authorities often have far higher business rates revenue than authorities in their hinterland, which in turn are more residential in character and rely more on council tax for local revenues:

> ...it would not make sense for a predominantly residential local authority with a strong council tax base to chase the business rates revenue of the local authority in which most of its residents work, or to compete with the city centre of the city-region by building out of town shopping centres or business parks.[10]

The final report of the 2014 *Independent Commission on Local Government Finance* made a similar suggestion:

> If local areas are aggregated into groupings of sufficient size and economic coherence (what we describe as sub-national areas) we find that the variation in need between the areas is far less than the variation within them. The proposition is therefore that the national grant settlement is on the basis of the larger geographical area and remains largely stable (perhaps adjusted for changes in population). It would then become the role of the governance within the area to manage equalisation between component parts.[11]

The *Local Government Finance Bill 2016-17* included a provision that would have allowed the Secretary of State to impose pools on areas, provided at least one participating authority agreed. However, the Bill fell at the 2017 general election, and this proposal has not reappeared.

[10] Centre for Cities, *Beyond Business Rates*, 2015, p. 19
[11] LGA / CIPFA, *Financing English Devolution*, 2014, p.26

2. 75% / 100% retention of business rates

In a speech at the Conservative Party conference on 5 October 2015, the then Chancellor, George Osborne, committed to allowing local government to retain 100% of business rates revenue 'by the end of the Parliament'. This was planned to begin in the 2019-20 financial year. However, following the snap 2017 General Election and the subsequent fall of the *Local Government Finance Bill 2016-17*, this policy was paused.[12]

The Government's policy is now to move to **75%** rate retention. This was originally to have taken place from 2020-21, but it was confirmed in September 2019 that this would be postponed by a year.[13] It was postponed further in April 2020 due to the coronavirus pandemic.[14]

In December 2017, the then secretary of state, Sajid Javid, had announced that the Government would seek to move to 75% rate retention from the 2020-21 financial year:

> The aim is for local authorities to retain 75% of business rates from 2020-21. That will be done through incorporating existing grants into business rates retention, including the revenue support grant and the public health grant. Local authorities will be able to keep that same share of growth on their baseline levels from 2020-21, when the system is reset. So from 2020-21 business rates will be redistributed according to the outcome of the new needs assessment, subject to suitable transitional measures.[15]

In response to the HCLG Committee's 2018 report on business rate retention, the Government has also said that it is "committed to working with the sector on increasing business rates retention beyond 75%, when it is right to do so".[16]

2.1 Consultation on additional rate retention

The new 75% rate retention system will not require new legislation. It will consist of a 'reset' of the rate retention system (see section 1.3), taking effect from 1 April 2021. This will consist of alterations to all local authorities' tariffs and top-ups, based on a needs assessment. The Government's approach to needs assessment at this point will be determined by the 'Fair Funding Review' (see section 3 below).

The Government published two consultation papers on 5 July 2016, on the introduction of full retention of business rates by local government and on how to review the assessment of needs that will underlie the introduction of 100% business rate retention. The Government

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12 HCDeb 17 Jul 2017 c539

13 See Dominic Brady, "Shake-up of local government funding delayed by a year", *Public Finance*, 5 September 2019

14 HC WS220 2019-21, 29 April 2020

15 HCDeb 19 Dec 2017 c917

16 HCLG Committee, *Government response to the Housing, Communities and Local Government Committee's Fifth Report of Session 2017-19 on Business Rate Retention*, Cm 9686, August 2018

published a response to these consultations, and a further consultation paper, on 15 February 2017.[17]

A fourth consultation paper was published in December 2018, entitled *Business rates retention reform*. This made various additional proposals, including:

- Funding the 'safety net' through a top-slice of total business rate revenue, instead of through the 'levy';
- Changing the operation of the 'levy'. Instead of applying to all additional revenue, the Government proposes to operate it as a 'cap' on the additional revenue that can be retained locally. The consultation seeks views on operating a 'cap', and the rate at which it should be set (e.g. 100%, 150% or 200% of an authority's Baseline Funding Level). This is a change from previous policy, which was to abolish the levy entirely.[18] The IFS's response to the consultation suggests a more tapered approach to the safety-net and possibly also the levy, to avoid a situation where local authority incentives change sharply above or below a certain quantity of revenue;[19]
- Whether areas should be able to set their own 'tier splits' (see section 1.1 above);
- How to further incentivise pooling.

Appeals

The consultation paper also addressed the issue of appeal provisions and losses. Local authorities must set aside funds to take account of ratepayer appeals, as these can lead to reductions in rate revenue. When an appeal is complete, the ratepayer may receive a refund from the local authority. Any remaining funding that has been set aside can then be used by the authority.

Managing the effects of appeals has been a substantial challenge for certain authorities since 2013, as such changes can strip out substantial sums from an authority's budget. The sums can be enough to wipe out all previous revenue growth, or even to move a successful authority into the safety net.

The consultation paper proposes to adjust tariffs and top-ups annually on the basis of authorities' forecast revenue. This will take account both of authorities' provision for future appeals, and, in time, the outcomes of those appeals. Tariff payments pay for top-ups and therefore they must balance one another across England. In effect, this change would spread the risk of appeal loss amongst all English authorities.

The consultation states that the Government favours this approach, but seeks views on whether it is appropriate.[20]

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[17] See DCLG, *Self-sufficient local government: 100% business rates retention - summary of responses and government response*, 15 February 2017; DCLG, *100% business rates retention: further consultation on the design of the reformed system*, 15 February 2017

[18] MHCLG, *Business rate retention reform*, December 2018, pp16-17

[19] Neil Amin-Smith and David Phillips, *Business Rates Retention Reform: Response to the Ministry of Housing, Communities and Local Government's consultation*, February 2019, pp7-9

[20] Ibid,. p24-27

The proposal is based on a previous paper produced by an MHCLG-LGA working group. That proposal was more extensive: it proposed that tariffs and top-ups should be adjusted to take account of *all* fluctuations in local revenue, not just those caused by appeals. It also proposed a 'reward grant' to run alongside rate retention, paid for by tariff payments. The paper states that the 'reward grant' could be based either on growth in rate revenue itself, or on alternative criteria.[21]

2.2 Phasing out grants

Permitting local government to retain a larger proportion of rate revenue would lead to an immediate rise in its funding levels. In the existing local government funding system, Revenue Support Grant and a number of smaller grants are paid to local authorities, alongside retained business rate revenue. The Government's proposals to date have included plans to end existing central grants to offset the additional revenue that would arise from increasing the 'local share':

> …the core grant [i.e. Revenue Support Grant] from Whitehall will be phased out, and local government will take on new responsibilities. …These new powers must come with new responsibilities, as well as phasing out the main grant from Whitehall, to ensure the reforms are fiscally neutral.[22]

The consultation published in July 2016 included an extensive discussion of which grants were likely to be ended under 100% retention, and the principles used to select those grants.[23] The influence of this discussion can be seen in the grants foregone by authorities participating in the pilots of higher levels of rate retention (see section 2.3). They include Revenue Support Grant, Rural Services Delivery Grant, the GLA Transport Grant and Public Health Grant. In a paper published in July 2018, the Government confirmed that:

> As part of the move towards a reformed business rates retention system in 2020/21, the government intends to devolve Revenue Support Grant (RSG), Rural Services Delivery Grant (RSDG), the Greater London Authority (GLA) Transport Grant and the Public Health Grant (PHG) to local government when the new system commences.[24]

Local authorities have expressed the view that the additional revenue available under 75% retention should be available to meet existing spending pressures, instead of being matched with new responsibilities or being offset by removing grants. The Housing, Communities and Local Government Committee's report of April 2018 said:

> …local government should be allowed to use the additional revenue gained from 75 per cent retention to fund existing cost pressures and not in replacement of Revenue Support Grant, Rural

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[21] Systems Design Working Group, *Simplification of the Business Rates Retention System*, 31 July 2018. See also a note of initial discussions with Government: *Note following BRR Technical Papers*, 16 October 2018

[22] HM Treasury, "Chancellor unveils devolution revolution", 5 October 2015

[23] See DCLG, *Self-sufficient local government: 100% business rates retention - summary of responses and government response*, 2017, pp7-10; see also the discussion on pages 16-21 of the original consultation.

[24] MHCLG, *Invitation to Local Authorities in England to pilot 75% Business Rates Retention in 2019/20*, July 2018, p4

Services Delivery Grant, GLA Transport Grant and Public Health Grant.[25]

Section 31 grants

The Government makes extensive use of 'section 31 grants' to channel funding to authorities, to ensure local authorities do not lose out due to central government decisions.[26] For instance, the adult social care grants introduced in 2016-17 and 2017-18 were 'section 31 grants'. Section 31 grants may be given with or without conditions, and they can be distributed amongst authorities according to their own criteria, without reference to a needs assessment. If the Government does phase out Revenue Support Grant, the power to give section 31 grants will remain in existence.

The Government's December 2018 consultation floated the idea that the use of section 31 grants for this purpose could be replaced in the medium term by adjustments to local authorities' tariff or top-up levels.[27] This suggestion was made in the context of the proposal for annual changes to tariffs and top-ups (see section 2.1 above). However, this would be a change in substance. Section 31 grants constitute, in effect, additional funds from outside the business rate system. Adjusting tariffs and top-ups involves redistributing business rate revenue between authorities: thus any compensation to one authority would require reduced funding to other authorities.

2.3 Pilot schemes

The March 2016 Budget announced the piloting of 100% retention of business rates revenue in Greater Manchester and Liverpool City Region.[28] On 15 December 2016 Sajid Javid, then Secretary of State for communities and local government, announced that pilots would also take place in the West of England, Cornwall and the West Midlands.[29] A pilot for London, to begin in April 2018, was also announced at the November 2017 Budget.[30] Fuller details of the initial round of pilots were published on 22 February 2017.[31]

In September 2017, the Government invited applications for a second round of pilots to begin in April 2018. These were directed in particular at two-tier areas, to test how 100% rate retention would operate between different tiers of government.[32]

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25 Housing, Communities and Local Government Committee, Business rates retention, HC-552 2017-19, 24 April 2018, p4

26 These are named after section 31 of the *Local Government Act 2003*, which provides the Government with a general power to give grants to local authorities for any purpose. This power would not be affected by changes to rate retention.

27 MHCLG, *Business rate retention reform*, December 2018, p26

28 HM Treasury, *Budget 2016*, 2016, p70

29 HCDeb 15 Dec 2016 c976

30 HM Treasury, *Budget 2017*, p55

31 DCLG, *Settlement funding assessment calculation model: business rate pilots 2017-18*, 20 February 2017; DCLG, *Explanatory note on business rate pilots 2017-18*, 21 February 2017

32 DCLG, *Invitation to Local Authorities in England to pilot 100% Business Rates Retention in 2018/19 and to pioneer new pooling and tier-split models*, 2017, p6

Ten applications were successful: Berkshire, Derbyshire, Devon, Gloucestershire, Kent, Leeds, Lincolnshire, Solent, Suffolk and Surrey. Some of the pilots will be operating alternative 'tier splits'.[33] In some pilots, a proportion of any additional retained revenue is being retained in a pilot-wide 'single pot' for future economic growth-related activities.[34]

In July 2018, the Government launched a further invitation document to pilot 75% rate retention for the 2019-20 financial year.[35] The successful areas were Berkshire; Buckinghamshire; East Sussex; Hertfordshire; Lancashire; Leicestershire; Norfolk; Northamptonshire; North and West Yorkshire; North of Tyne; Solent; Somerset; Staffordshire and Stoke; West Sussex; and Worcestershire.[36] These were announced alongside the provisional Local Government Finance Settlement in December 2018. Of the successful areas, only Berkshire and Solent participated in the 2018-19 pilots. 'Leeds City Region' also participated in 2018-19: this area covered part of the area of 'North and West Yorkshire'.

The 2019-20 pilots have now come to an end. The five original pilots that began in 2017-18 remain in place, operating 100% retention. Greater London operated a 75% pilot in 2019-20 and a 100% pilot in 2018-19. In 2020-21 London boroughs have a local share of 67%, and the GLA will have a local share of 37%.[37]

The 2019-20 pilots had a 'safety net' of 95% of baseline funding level, compared to the 97% safety net available in the 100% retention pilots. The 2018-19 pilots included a 'no detriment' clause, which guaranteed that pilot authorities would not lose out financially as a result of the pilot. However, no such clause was included for the 2019-20 pilots.[38]

The pilots: technical explanation

In technical terms, both rounds of pilots work in the same way: this is set out in a short Government document.[39] The participating authorities form a business rates 'pool' and agree to forego their allocations of certain central government grants. As the Government document sets out, *which* grants are foregone differs from place to place.

The grants foregone are, in almost all cases, less than the additional revenue made available by the pilot. The single tariff for the pool is then reset so as to take account of the gap between the grants foregone and the additional percentage of rate revenue. This ensures that

[33] A full list of the participating authorities, and the 'tier splits' being operated, can be found in MHCLG, Local Government Finance Report 2018-19, 2018, pp60-63.

[34] Details can be found in LGA-DCLG Steering Group, 'Pilots paper for Business Rates Steering Group January 2018', 2018.

[35] MHCLG, *Invitation to Local Authorities in England to pilot 75% Business Rates Retention in 2019/20*, July 2018

[36] A full list of the participating authorities, and the tier splits operating in each locality, can be found in Annex G of the *Draft local government finance report 2019-20*.

[37] MHCLG, *Draft local government finance report 2020-21*, 20 December 2019

[38] MHCLG, *Invitation to Local Authorities in England to pilot 75% Business Rates Retention in 2019/20*, July 2018, p7

[39] See MHCLG, *Explanatory notes on pools and pilots: provisional local government finance settlement 2019-20*, December 2018

participating in the pilot does not in itself lead to a financial windfall for the authorities.

The Institute for Fiscal Studies have stated that lessons learned from the 2018-19 pilots may be limited.[40] They estimate that the participating councils will gain an extra £873 million in 2018-19, equating to an increase of 3.6% in spending power. £431 million of this gain would occur in London. The IFS notes that local authorities' forecasts of business rate revenues have been too high in previous years, and provides alternative figures revised downwards. These suggest that pilot councils would gain around £650 million extra in 2018-19, of which London would gain £311 million.[41]

40 Neil Amin-Smith, David Phillips, and Polly Simpson, *100% business rate retention pilots: what can be learnt and at what cost?*, Institute for Fiscal Studies BN233, 2018, p15-16
41 Neil Amin-Smith, David Phillips, and Polly Simpson, *100% business rate retention pilots: what can be learnt and at what cost?*, Institute for Fiscal Studies BN233, 2018, p11

3. The *Fair Funding Review* and needs assessment

In February 2016, the then Secretary of State, Greg Clark, committed to revising the 'underlying assessment of needs' contributing to the allocation of local authority funding:

> It is too long since the underlying assessment of needs was updated—it is more than 10 years—and that is why I have proposed to go back to the drawing board and look at the needs and the resources available to each county.[42]

The Government's 2016 consultation *Business rates reform; call for evidence on needs and redistribution* launched the 'Fair Funding Review'. A response to this consultation was published on 19 December 2017. A further consultation (see section 3.2) was launched at the same time. A third consultation was published in December 2018 (see section 3.3).

The Review was to have been implemented from 2020-21, but in September 2019 it was postponed by a year.[43] Then, the Government postponed the implementation of the Fair Funding Review again in April 2020 due to the coronavirus pandemic.[44]

The Government has convened a series of joint working groups with the Local Government Association (LGA) since mid-2016, though these have met less frequently in 2019 and 2020. Minutes of the meetings of these groups can be found on the LGA's website.

3.1 Fair Funding Review and rate retention

The outcomes of the Fair Funding Review are to be implemented alongside the introduction of 75% business rate retention. Implementation of the Review will therefore consist of a 'reset' of the BRRS (see section 1.4). This will assign a new baseline funding level, and thus a new tariff or top-up, to each local authority (see section 1.1).

The needs assessment will therefore take effect at the starting point of a new 'retention period' following the reset. From this point, individual authorities will then, once again, begin to retain additional revenue. This means that, as the new retention period progresses, additional revenue will cause local authorities' overall funding to diverge from the needs-related levels set out in the Fair Funding Review.

It follows from this that the operation of the reset system will influence how far authorities will have to benefit from growth in rate revenue resulting from their policies. Because local authorities' potential to benefit in this way varies, retaining revenues for longer (whether via a 'full reset' or a 'phased reset') will lead to more revenue divergence between authorities. Conversely, the more frequently a needs

[42] HCDeb 10 Feb 2016 c1642

[43] See Dominic Brady, "Shake-up of local government funding delayed by a year", *Public Finance*, 5 September 2019

[44] HC WS220 2019-21, 29 April 2020

assessment is applied and a reset takes place, the less opportunity each individual authority has to benefit from the revenue growth that it generates.

3.2 Needs assessment

The pre-2013 local government finance system included a complex and fine-grained annual assessment of local authority need. This formed the basis of the allocation of Revenue Support Grant and business rate revenue to local authorities. At the time this was used to distribute the majority of local government funding, and thus the annual needs assessment had great influence on the funding available to local authorities. A brief history can be found on pages 15-17 of the December 2017 consultation, *Fair funding review: a review of relative needs and resources - technical consultation on relative need*.

In short, the pre-2013 system used over 120 social and economic indicators to assess local authority spending need. The system also assessed locally available resources (such as the capacity to raise council tax revenue), and applied a 'damping' formula to minimise the change to individual budgets from one year to the next. The system was critiqued as being opaque and hard to understand, and for the limited connection between needs and funding outcomes.[45]

This annual needs assessment was discontinued when the BRRS was introduced. This is because it would be impossible to operate the incentive element of the BRRS if authorities' funding could be adjusted annually on the basis of a needs assessment. Authorities' baseline funding levels are therefore influenced by the most recent needs assessments, in 2011 and 2012.

The Government's December 2017 consultation stated that the new funding formula would seek to measure need by identifying 'cost drivers' – factors that most strongly influenced the cost of providing local services. It intended to use population, deprivation and rurality as the three main cost drivers.

The new formula would use a 'foundation formula', based on cost drivers common to all services, to allocate as much of the available funding as possible. Alongside this, the consultation proposed a series of service-specific cost drivers, that underlie the costs of spending on local government services such as transport, social care, fire and rescue, waste, and children's services. The formula would also include resource assessment (based on the capacity to raise council tax); an area costs adjustment; and is intended to "make the link between local circumstances and funding allocations more visible".[46]

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45 Alex Gibson and Sheena Asthana, "A Tangled Web; Complexity and Inequality in the English Local Government Finance Settlement", *Local Government Studies* 38:3, 2012, pp.301-320; see also LG Futures, *Reforming Local Authority Needs Assessment: Simplifying the Funding Model,* Communities and Local Government Committee, October 2017

46 DCLG, *Fair funding review: a review of relative needs and resources - technical consultation on relative need*, 2017, p9

The Institute for Fiscal Studies published a paper in August 2018 entitled *The Fair Funding Review: is a fair assessment of councils' spending needs feasible?* The paper stated that the Government's proposed approach, of using regression analysis to estimate the relationship between selected social indicators and council spending, had much to commend it. However, the approach's effectiveness was dependent on selecting social indicators accurately and on the weighting given to them:

> Judgement inevitably plays a part in deciding what year of data to use, what indicators to include, and what (if any) adjustments to make to formulas estimated by regression analysis if there is a concern that they are being biased by non-needs factors.[47]

3.3 Fair Funding Review: 2018 consultation

A further consultation was published alongside the provisional Local Government Finance Settlement on 11 December 2018. This consultation provided some clearer outlines of the Fair Funding Review.[48] The key elements underlying the new funding formula are to be:

- A relative needs formula, including an area cost adjustment;
- A relative resources formula;
- Transitional arrangements.

Relative needs

The consultation proposes that relative needs will be measured via a 'foundation formula' plus a number of additional formulae that are service-specific. The foundation formula will take account of levels of need for public transport, housing and homelessness, cultural, environmental services, waste, planning and regulatory services. The service-specific formulae would be for adult social care; children and young people's services; public health; highways maintenance; legacy capital finance; flood defence and coastal protection; and fire and rescue. Separate allocations will be made for upper-tier and lower-tier services.[49]

The consultation proposes that the foundation formula should be allocated purely on the basis of population. This means that the formula will measure 'need' for public transport, housing and homelessness, cultural, environmental services, waste, planning and regulatory services solely by the number of people living in an authority's area. The consultation discussed whether rurality or deprivation should also be used as a 'cost driver' for the foundation formula. It stated that its analysis showed that "…population alone explained 88.1% of all variation in past expenditure. Adding deprivation as an additional cost

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47 David Phillips and Tom Harris, *The Fair Funding Review: is a fair assessment of councils' spending needs feasible?*, Institute for Fiscal Studies, Aug 2018, p10

48 MHCLG, *A review of local authorities' relative needs and resources*, December 2018

49 A comparison between the existing and proposed needs assessment formulae can be found in an Excel spreadsheet entitled Review of local authorities' relative needs and resources: technical paper.

driver increased the proportion of all variation explained by 4.0 percentage points".[50] These figures have been critiqued (see below).

MHCLG arrived at these figures by conducting a regression analysis using local authorities' actual spending figures between 2014-15 and 2016-17 and population data by local authority. Regression analyses are used to determine the strength of relationship between two data sets. This approach is based on treating local authorities' spending decisions in prior years as a reliable guide (in statistical terms, a 'proxy') to the level of need for local authority services. This is an accepted approach to measuring need where detailed individual data is unavailable: however, it cannot take 'unmet need' into account. More sophisticated measures of need are sometimes used in funding formulae for education or health services (for instance), based on extensive data on the past behaviour of individuals.[51]

An 'area costs adjustment' will also be included within the overall formula. The Government proposes that this will take into account a 'rates cost adjustment', which will take account of commercial rents; a labour cost adjustment; and a remoteness adjustment. 'Rurality', or 'sparsity', was one of the three factors identified in previous consultations as likely to play a significant role in variations in costs between local authorities. The Government argued that "sparsity and remoteness can have a significant effect on the cost of providing some services, rather than being factors which drive additional demand".[52]

Decisions have not yet been made about how to weight the various formulae in relation to one another. The December 2018 consultation includes a graph showing the relative levels of spending between 2015 and 2018 that fall under each of the elements of the proposed formula.[53]

Taking account of deprivation

MHCLG has faced criticism for not proposing to include deprivation in the foundation formula. The Institute for Fiscal Studies states that this approach "is likely to lead to lower needs assessments for urban and deprived areas than both existing formulas and an updated formula which incorporated deprivation".[54] Their modelling shows that authorities in the North-West and metropolitan authorities would see reduced funding, whilst most shire county authorities would gain.[55] This analysis only covers the effects of the foundation formula: it does not take into account the effects of the service-specific formulae, or revenue from council tax, growth in business rate revenue or other sources.

An analysis from the University of Liverpool challenged the MHCLG claim that only 4% of variation in local authority spending was related

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[50] MHCLG, *A review of local authorities' relative needs and resources*, December 2018, p19-20.
[51] For instance, see NHS England, *Technical guide to allocation formulae and pace of change*, 2016
[52] Ibid., p21
[53] MHCLG, *A review of local authorities' relative needs and resources*, December 2018, p43
[54] Ibid.
[55] Ibid., p8

to deprivation. The MHCLG figures are based on comparing the variation in total spend between *authorities* on the services to be covered by the foundation formula. The University of Liverpool analysis used *per capita* spending figures for the foundation formula services, and stated that, using this approach, 16% of variation in local authority spending was explained by deprivation.[56]

In similar terms, the IFS stated that the close relationship between population and spending was a product of the large variations in local authority population size.[57]

The IFS also note that, whilst the use of past spending patterns as a proxy for need is a recognised approach, the results obtained may be very different according to *which years* of past spending patterns are used. Local authority spending has fallen considerably since 2009-10, and this fall has been most acute in local authorities experiencing the highest levels of deprivation.[58] This suggests that, if a regression were carried out using spending figures from 2009-10 or earlier, it might show a larger proportion of spending being linked to deprivation than was linked in 2014-17. The University of Liverpool reran their analysis described above using 2009-10 figures and found that, using that approach, 40% of local authority spending variation could be explained by deprivation. As the IFS note, the decision over which spending figures to use is a matter of "expert and political judgment".[59]

It is not yet clear how much influence the debate on the foundation formula will have on the *overall* effects of the proposed funding formula on local authority budgets. In addition to the other service-specific formulae, which are based on needs, the new approach will also include a resource element (see 'Relative resources' below).

The December 2018 consultation indicates that other elements of the needs formula *will* take deprivation into account. Deprivation will form a part of the service-specific formulae for adult social care, children and young people's services, public health and fire & rescue services.[60] In addition, the formulae for children and young people's services and

[56] See Benjamin Barr, "Local government funding review: how can we better help the areas that need it the most?" *Better Health for All*, 18 February 2019
[57] Neil Amin-Smith, Tom Harris and David Phillips, *Needs and Resources: Response to the Ministry of Housing, Communities and Local Government's Consultation*, February 2019, p6
[58] See David Innes and Gemma Tetlow, *Central cuts, local decision-making: changes in local government spending and revenues in England, 2009-10 to 2014-15*, Institute for Fiscal Studies, 2015; Mia Gray and Anna Barford, "The depths of the cuts: the uneven geography of local government austerity", Cambridge Journal of Regions, Economy and Society, 11, 541-563, 2018; Adam Tinson, Carla Ayrton, and Issy Petrie, *A quiet crisis: local government spending on disadvantage in England*, New Policy Institute, September 2018
[59] Neil Amin-Smith, Tom Harris and David Phillips, *Needs and Resources: Response to the Ministry of Housing, Communities and Local Government's Consultation*, February 2019, p6
[60] MHCLG, *A review of local authorities' relative needs and resources*, December 2018, p21

public health will make use of individual-level data, whilst the formula for adult social care will use 'small area data'.[61]

Sector views

The plan to exclude deprivation from the foundation formula has led to disputes within the local government sector. The County Councils Network was reported as stating that the proposals "rightly recognised that current weightings for deprivation were disproportionate… and rightly put rurality and [population] density on a more equal footing".[62] A spokesman also said that "if its inclusion was to be reconsidered, our view is the current evidence only shows deprivation accounts for 4% of variation in spend. Any weighting can only be as large as the evidence supports".[63]

Other sector experts have disagreed with this perspective. Tony Kirkham, director of resources at Newcastle-upon-Tyne City Council, said:

> The Foundation Formula is probably going to be around 30% of the local government need and to suggest, when you look at the factors in there, that it will not be driven by deprivation I find very difficult to comprehend….You are looking at a pool of services covered by the Foundation Formula which are less statutory in nature, which means … that when we've been taking money out of the system, we've been taking it out of there rather than taking it out of the social care side….If you say deprivation doesn't impact homelessness, deprivation doesn't impact benefit claims, deprivation doesn't impact concessionary fares, then I think you're not being honest in your analysis.[64]

A response to the consultation from SIGOMA stated:

> Whilst the average picture may be of a roughly even profile of spend per head, the proposed method of calculating distribution will, by MHCLG's own measure, consistently and significantly underfund the poorest authorities to the benefit of wealthier ones.
>
> It would be fundamentally unfair not to include a deprivation weighting in the foundation formula.[65]

The Local Government Association, meanwhile, said:

> …given the widespread support for consideration of deprivation as part of the Government's previous consultation, and potentially a not insignificant 4% explanatory power, we believe that the starting point should be for deprivation to remain as a factor in

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61 MHCLG, *A review of local authorities' relative needs and resources*, December 2018, p23

62 Ann McGauran, "Mets feeling deprived over funding formula", *Municipal Journal*, 7 February 2019

63 Ibid.

64 See Ian McDiarmid, Q&A: Newcastle's Tony Kirkham on the Fair Funding and Spending Reviews, business rates retention, and the way government money is shared out among local authorities, Room 151, 28 February 2019

65 See Colin Marrs, "Counties offer olive branch on deprivation role in fair funding", *Room 151*, 27 February 2019. SIGOMA is the Special Interest Group of Metropolitan Authorities, representing a number of metropolitan and unitary authorities outside London.

> the foundation formula, with development of a clear evidence base for the weighting for this cost driver.[66]

The service-specific formulae

The consultation document summarises the indicators that are expected to be used to measure need in each of the service-specific formulae. The Government's intention was to focus on 'cost drivers' – i.e. indicators that measure the cost of providing the service - as opposed to measures of 'need' per se.

The consultation also noted a number of other service areas which were raised in responses to the previous consultation, but for which it does not propose to introduce a specific formula. These include concessionary transport; bus support; waste; homelessness; unaccompanied asylum seeking children; and people with no recourse to public funds. The intention is that these would be accounted for by the foundation formula.

Relative resources

The overall funding formula will also take account of the resources available locally to individual authorities. This principally consists of the 'council tax base' – each authority's capacity to raise revenue locally. The formula will express the resource element as a negative number. In basic terms, this will mean that authorities with higher local resources will lose more funding, and authorities with fewer local resources will lose less.[67] It is not yet clear whether the formula will equalise fully for relative resources (which was the historical practice) or whether it will do so only in part.

The Government proposes to use the council tax base for the relative resources element of the formula. The approach will be based on the following principles:

> - our approach to assessing relative resources will result in no redistribution of council tax or sales, fees and charges resources between authorities,
> - we do not intend to reward or penalise authorities for exercising local discretion, and
> - local authorities with a lesser capacity to fund services through locally raised resources will receive a smaller reduction to their relative needs share.[68]

The Government intends that the formula will take into account the effects of mandatory exemptions and discounts from council tax. This will ensure that, for example, an authority that collects less council tax revenue because it has a higher proportion of properties attracting single-person discounts does not lose out as a result.

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[66] LGA, "Review of local authorities' needs and resources (Fair Funding Review)", 20 February 2019, p3

[67] Ibid., p49: see the equation at paragraph 3.1.3. This reflects the operation of local government funding formulae between 1990 and 2013.

[68] MHCLG, *A review of local authorities' relative needs and resources*, December 2018, p49-50

The consultation proposes that the formula will use a single notional level of council tax, rather than actual local rates. This will ensure that the formula takes into account the *capacity* to raise council tax rather than local decisions about *how much* to raise. In other words, the formula should not penalise authorities which have chosen to set either higher or lower council tax rates than the average.

The consultation also raises the issue of whether the resource formula should be adjusted regularly. A resource measure that is fixed would benefit authorities where the number of houses grows after the formula is implemented – because the new houses would not be taken into account in the measure of the council tax base. An alternative is to use projections of council tax base levels for future years.[69]

The consultation discusses the possibility of taking local revenue from sales, fees and charges into account, but broadly rules this out, with the possible exception of income from parking charges.[70] Income from parking charges is ring-fenced to be spent on transport-related matters, and thus it is not an additional source of income for any and all local authority functions. The consultation invites views on whether local council tax support schemes should be taken into account.

Transitional funding

Any new funding formula for local government carries the risk that individual authorities will experience very sharp changes at the point of transition, which cause them to struggle to manage their budgets in the short term. To accommodate this, previous funding formulae have included transitional measures. In the 1990s and 2000s this practice was known as 'damping'. The consultation paper invites commentary on four principles to govern a future transitional system: stability, transparency, limited in time, and flexibility.[71]

3.4 Local government funding: broader issues

Neither the Fair Funding Review nor business rate retention address the issue of how much funding should be made available to local authorities, nor do they address how this question should be answered.

Total funding for local government in England is determined by the annual Local Government Finance Settlement (see the Library briefing on the 2020-21 settlement). In the annual settlement, the Government determines the redistribution of rate revenue between local authorities via the tariffs and top-ups in the Retention Scheme (see section 1). It also determines the distribution of other grants such as Revenue Support Grant, Rural Services Delivery Grant, the New Homes Bonus, and the Improved Better Care Fund.

There is no automatic link between the statutory duties faced by local authorities and the funding made available by the Government to

69 MHCLG, *A review of local authorities' relative needs and resources*, December 2018, p61
70 Ibid., p.62-3
71 Ibid., p66

enable them to carry out their duties. Many local authorities have stated during the later 2010s that, if grant funding continues at prevailing rates, they will struggle to meet their statutory duties in the early 2020s. The practice of central governments legislating to require local authorities to do specific things, but providing insufficient funding for them to do so, is known in academic literature as 'unfunded mandates'.

The Institute for Fiscal Studies published a briefing paper in late 2019 entitled *English local government funding: trends and challenges in 2019 and beyond*. This made the following points:

- Rising need for social care funding was likely to outstrip projected increases in business rate revenues through the early 2020s. This would be true even if council tax rose by an average of 4% per year throughout the 2020s. It would also not be offset by the increases in funding proposed in the autumn 2019 Local Government Finance Settlement;
- This effect will differ between local authority areas: there is no connection between projected (or possible) rate revenues and levels of social care need in a given geographical area;
- Grant reductions in the 2010s were greater in more deprived local authority areas. As noted above, the Fair Funding Review *could* be conducted such that the effects of those differing reductions were taken as the new starting point. This would mean that the effects of those grant reductions were 'baked in' to the post-2021 system;
- Reductions in grant funding in the 2010s have led to reductions in service provision in services where statutory requirements are fewer or more general in character, such as culture, planning and housing. Social care spending has increased by a small proportion in most councils between 2009 and 2019.

4. Fundamental Review of business rates

4.1 The Review

The Conservative Party's 2019 General Election manifesto committed to a 'fundamental review' of the business rates system:

> We will cut the burden of tax on business by reducing business rates. This will be done via a fundamental review of the system. As a first step, we will further reduce business rates for retail businesses, as well as extending the discount to grassroots music venues, small cinemas and pubs.[72]

The Government reiterated this commitment in the Budget of 11 March 2020. They also published terms of reference for the review, as follows:

> HM Treasury will conduct a fundamental review of business rates with the objective of:
>
> - reducing the overall burden on businesses
> - improving the current business rates system
> - considering more fundamental changes in the medium-to-long term
>
> The work of the review will focus on 4 main areas: These are:
>
> - improvements that could be made from April 2021, alongside the forthcoming revaluation including regarding the Transitional Relief Scheme
> - reforms to the current business rates system to put the tax on a more sustainable basis. This will include:
>   - whether a tax on open market rental values remains the best base for commercial property
>   - how open market rental values are determined, and how often
>   - the effectiveness and operation of different reliefs
>   - how to minimise the impact of business rates on investment and growth, including the treatment of plant and machinery
>   - how the business rates multiplier(s) should be set
>   - who pays the tax
> - the administration of business rates, covering the valuation and appeals process; billing; and compliance with the tax
> - exploring alternatives to business rates, particularly within the taxation of land and property.
>
> Alongside supporting the government in its core aims regarding the economy, productivity and its fiscal rules, the review will also have particular regard to:

72 Conservative Party, *Get Brexit Done, Unleash Britain's Potential*, 2019, p32

- the role of business rates in the funding of local government and local services, and the impact of any changes on business rates retention
- the delivery of existing reforms to the business rates system
- the practical challenges involved in any reforms, and necessary compromises
- the implications of the current and future subsidy control regimes
- the implications of any changes for the devolved administrations

The review will not consider the overall level of funding for local government.

HM Treasury published a call for evidence on 21 July 2020.[73] This covered the following subjects:

- The operation of reliefs and exemptions, in particular where properties are eligible for multiple or overlapping reliefs; reliefs being offset by landlords raising rents on properties; narrowing of the taxbase owing to large numbers of reliefs; and the potential for abuse;
- The operation of the business rate multipliers: how to set them "to ensure the sustainability of public finances and support growth and productivity".[74] Possible changes noted include introducing different multipliers for different sectors and/or regions; ending the system whereby the multiplier is adjusted to balance the effects of revaluation;[75]
- The valuation process. This included:
  - A discussion of frequency of valuations. This was addressed in the 2014-16 business rate reviews (see below). That debate led to the Government's decision, in 2017, to move from five-yearly to three-yearly valuations from 2021 onwards. That decision has now been overtaken, as the effect of the next revaluation has been postponed to 2023 in the light of the Covid-19 outbreak in 2020;
  - The possibility of moving to using geographical zones, or council tax-style bands, to value properties. These options were also discussed in the 2014-16 reviews;
  - Regionalising the revaluation process;
  - Requiring ratepayers to provide rental information more frequently, to ensure rateable values are based on up to date information. This is addressed in both sections 4 and 5 of the call for evidence. Section 5 includes the suggestion that a legal duty should be introduced on ratepayers to provide lease details, or details of changes that could affect their property's rateable value, to the VOA;

73 HM Treasury, *Fundamental review of business rates: call for evidence*, 21 July 2020
74 Ibid, p14. See section 1 of the Library briefing *Business rates* for an explanation of the multipliers
75 See section 4 of the Library briefing *Business rates* for an explanation of this system.

- How to treat plant and machinery within the valuation process.
- Standardising and automating the process of billing for business rates. This was raised during the 2014-16 reviews.

The call for evidence also invites responses on alternatives to business rates. This reflects the findings of the Treasury Select Committee's 2019 report *The impact of business rates on business*. This report anticipated many of the concerns in the fundamental review's call for evidence. It discussed five alternatives to business rates: a land value tax; an online sales levy; a sales or turnover tax; a profits tax (essentially corporation tax); and a 'single consolidated tax'. The Committee recommended "that the Government prepares a consultation in time for the next Spring Statement to identify potential alternatives to the current system of business rates and form the basis for a subsequent detailed evaluation of viable options".[76]

An article in the Times in March 2020 had suggested that one of the options considered by the review would be replacing business rates with a land value tax:

> The review will examine proposals for a tax on the land rather than buildings based on its "permitted planning" use, meaning that farmland would face a lower levy than developed areas.
>
> The tax would be levied on landlords, delivering a potential tax cut for hundreds of thousands of small businesses which rent premises.
>
> A government source, however, emphasised that the land value tax plans would be considered over the "medium to long term". A separate package of measures will be included in the budget to provide more short-term relief.[77]

However, the call for evidence was restrained in its discussion of alternatives. The Government said:

> ….this call for evidence focuses on an alternative means of taxing non-residential property as a potential replacement for business rates and, due to the prevalence of concerns about online retail trends and divided public opinion, an online sales tax. Given that an online sales tax would be unlikely to raise revenue sufficient to replace business rates, we expect that any such tax would exist alongside business rates.[78]

The document invited representations on two alternatives:

- A capital values tax. This would seek to assign values to properties on the basis of their capital value rather than their rental value. In other jurisdictions, property owners rather than occupiers are often liable for such taxes;
- An online sales tax. This concept is intended to address an issue often raised by critiques of business rates: that high value businesses with minimal property needs – which conduct much of

[76] Treasury Select Committee, *The impact of business rates on business*, HC-222 2019-21, 31 Oct 2019, p47

[77] Steven Swinford and Oliver Wright, "Rishi Sunak budget: Tories 'to save high street' with land tax to replace business rate", *The Times*, 22 February 2020

[78] HM Treasury, *Fundamental review of business rates: call for evidence*, 21 July 2020, p31

their business or add much of their value via the Internet – may pay less than businesses with high property needs but lower profit margins. Retail is often given as an example of the latter.

Business rates generate some £30 billion of revenue annually. This revenue forms a major element of local government funding. The call for evidence says that "the impact on the local government funding system will be an important consideration in reviewing the tax".[79]

The call for evidence set a deadline of 18 September 2020 for comments on business rates reliefs and multipliers, and committed to an interim report in the autumn. The deadline for responses on the other parts of the call is 31 October.

4.2 Business rates reviews, 2014-16

In the 2013 Autumn Statement, the Government stated that it would review the business rates system.[80] Terms of reference for this review were published in February 2014.[81]

A discussion paper was published on 10 April 2014. A summary of responses to the paper, and an interim response from the Government, were published on 10 December 2014.[82] The interim response addressed the following points, which had arisen during consultation:

- A majority of respondents wanted more frequent revaluations (than the standard five year period), but a significant minority did not. The interim response included an analysis of the costs and benefits of more frequent revaluation. This led to a Government commitment to introduce three-yearly revaluations from 2021. However, that has been put on hold due to the coronavirus pandemic, and the next revaluation is now scheduled to take effect in 2023;[83]
- The consensus was that individual valuations of properties should continue. The Government had raised the possibility of introducing a 'banding' system, similar to that used for council tax, but this found little favour;
- Proposals to reform the process of appealing to the Valuation Office Agency (VOA) against a property's rateable value.[84] This led to the introduction of the Check, Challenge, Appeal system (see section 7 of the Library briefing paper *Business rates*);

Following this publication, the 2014 Autumn Statement said:

> The government will carry out a review of the future structure of business rates to report by Budget 2016. The review will be fiscally neutral and consistent with the government's agreed financing of local authorities. The government will also publish its interim

[79] HM Treasury, *Fundamental review of business rates: call for evidence*, 21 July 2020, p4
[80] Ibid., p. 93-4
[81] HM Treasury, Business Rates Administration Review: terms of reference, February 2014
[82] See also the published responses to the interim response, from July 2015.
[83] DCLG, How might we expect more frequent revaluations to affect business rates bills?, Annex A to the *Administration of Business Rates Review: Interim Findings*, December 2014
[84] DCLG, *Administration of Business Rates Review: Interim Findings*, December 2014, p. 19

> findings from the review of business rates administration in December 2015, setting out how it will respond to business' calls for clearer billing, better information sharing and a more efficient appeal system.[85]

The 'review of business rates administration' mentioned in this quote is the first review, discussed above. In the event, the two reviews mentioned here were rolled into one, now to be published alongside the 2016 Budget.

The terms of reference for the second review were published in March 2015, in a consultation paper entitled *Business rates review: terms of reference and discussion paper*. The consultation ran until 12 June 2015.[86]

85 HM Treasury, *Autumn Statement 2014*, 2014, p. 46

86 HM Treasury, *Business rates review: terms of reference and discussion paper*, 2015, p.8

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