The local government resource review

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The local government resource review, instituted by the Coalition Government, examined different ways of giving English local authorities greater autonomy and financial freedom. The terms of reference for the first stage of the review were published on 17 March 2011, and those for the second phase on 29 June 2011.

The first phase covered a number of issues, including ways of making local authorities less dependent on central government funding. The principal output of the first phase was the Business Rate Retention Scheme, which came into effect from 2013-14 (see the Library research paper *The Local Government Finance Settlement 2013-14 and 2014-15*).

The second phase of the review covered future plans for the community budgets initiative. Current progress on this is covered in Library standard note SN/PC/05955, *Community budgets and city deals*.

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1 Background

In July 2010, Bob Neill, then Minister for Local Government, stated that "the Communities and Local Government Structural Reform Plan, published on 8 July 2010, set a start date of summer 2011 for the local government resource review. The review will end in 2012."[1] In a press release on council tax revaluation in September 2010, Eric Pickles, Secretary of State for Communities and Local Government, stated:

> There are also plans for a broader local government resource review that will examine the way councils are funded, to provide greater financial freedoms and decrease dependency on Whitehall funding, which has previously pushed up council tax in many local authorities due to so-called 'gearing' effects."[2]

On 28 October 2010, Vince Cable said that:

> Rewarding growth is also about fairness in the local government finance system. Local business rate retention will be considered within the local government resource review, which the Government intend to launch in January after a period of consultation on the proposals in the White Paper."[3]

The Local Government Resource Review, and the Business Rates Retention Scheme, apply only in England. Local government is a devolved matter: the devolved institutions in Scotland, Wales and Northern Ireland have not introduced any equivalent of the Business Rates Retention Scheme, nor have they been affected otherwise by the resource review. Local government funding in those territories still takes the form of a block grant from the devolved institution to local authorities.

General information on the review is available on the DCLG website. The review concluded as of April 2013 and the outcomes are now 'mainstreamed' into local government practice. This note provides information about the initiation of, and reaction to, the review.

2 The review

The terms of reference of the review were announced on 17 March 2011. These included the following:

> The first phase of the Review will consider the way in which local authorities are funded, with a view to giving local authorities greater financial autonomy and strengthening the incentives to support growth in the private sector and regeneration of local economies. The terms of reference ... include consideration of changes to the business rates system, in particular:
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> - the optimum model for incentivising local authorities to promote growth by retaining business rates, whilst ensuring that all authorities have adequate resources to meet the needs of their communities and to deliver the commitments set out in the Spending Review;
> - the extent to which these proposals can set local authorities free from dependency on central funding;
> - considering how to fund authorities where locally raised funding would be insufficient to meet budget requirements and control council tax levels, as well as

1 HC Deb 14 July 2010 c767W
2 DCLG Press release, *Pickles pledges – no council tax revaluation rises*, 24 September 2010
3 HC Deb 28 October 2010 c480-2

councils who do not collect business rates, such as upper tier authorities, recognising that some parts of the country are currently more dependent on government funding;

- reviewing the scope for greater transparency and localisation of the equalisation process;
- the position of councils whose business rate yield would be significantly higher than their current spending;
- how to ensure appropriate protections are in place for business, within a framework of devolving power to the lowest level possible;
- how to deliver Tax Increment Financing proposals against a context of greater retention of business rate revenues;
- how various aspects of the business rate system, including business rate revaluation and reliefs, should be treated;
- examining the scope for further financial freedoms for local authorities, while standing up for and protecting the interests of local taxpayers, and
- the wider implications of rates retention for related policies, including the work of the Commission on the Funding of Care and Support and the Government's other incentive schemes (the New Homes Bonus and the commitment to allow communities to keep the business rates for renewable energy projects).

The first phase of the review concluded in July 2011.

Phase 2 of the resource review focused on community budgets. Its terms of reference were published on 29 June 2011:

> Greater autonomy brings with it greater responsibility for local leaders across all organisations and sectors, not just local authorities, to work more collaboratively; pooling and aligning resources across systems where that can deliver better outcomes, more effective use of resources and greater value for money for taxpayers. The second phase will explore the extent to which Community Budgets can make a further contribution to achieve this.
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> The second phase of the Local Government Resource Review will, therefore, test how Community Budgets can be used to:
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> - give communities and local people more power and control over local services and budgets
> - develop outcomes, service solutions and a single budget, or options for pooling and aligning resources, comprising all spending on public services in an area.[4]

The DCLG website also presents the Government's policy on community budgets as part of the resource review. Further details on this are available from Library standard note SN/PC/05955, *Community budgets*. The DCLG website also mentions the Local Services Support Grant, provided by DEFRA and the Department for Education to upper-tier local authorities, including further details on the grant and allocations. In 2013-14, DEFRA provided £18 million and the Department for Education £38 million.

[4] DCLG, *Second Phase of the Local Government Resource Review: Terms of Reference*, 2011, p. 1

The introduction of council tax support schemes, which replaced council tax benefit as of 1 April 2013, has also been presented as an element of the resource review. More details are available in the Library standard note on *council tax reduction schemes* (SN/SP/06672).

3 Proposals for business rates retention

As noted, as a result of the first phase of the resource review, the Business Rates Retention Scheme was introduced in the 2013-14 financial year. This now forms a significant part of the local government finance settlement. This note outlines the scoping and development of the scheme: details of the actual workings of the scheme are available in the Library research paper *The Local Government Finance Settlement 2013-14 and 2014-15*.

The DCLG published a consultation paper, *Local government resource review: proposals for business rates retention*, on 18 July 2011. The *Plain English guide* to the proposals notes that the core components of the proposed rate retention scheme are as follows:

> A baseline level with top ups and tariffs to create a fair starting point for all: Government would establish a baseline, which could be based on next year's Formula Grant allocations, for each council in the first year of the scheme (2013-14) so no council is worse off at the outset. Councils that collect more than that baseline would pay an individually set tariff to Government, while those below it would get an individually set top up grant from Government.
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> An incentive so all councils can grow: Tariffs and top up grants would remain fixed during future years meaning councils would retain any business rate growth it generates. Councils such as those in local enterprise partnerships, or districts and counties, will be allowed to voluntarily pool business rates to enable the wider economic area to benefit from growth and reduce any volatility.
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> A levy to recoup disproportionate gain: Government would create a levy to recoup a share of any disproportionate financial gain. It could vary according to each individual council's own circumstances and would be used to manage significant unforeseen falls in a council's business rates income.
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> A reset button to ensure stability: This will allow the Government to adjust top ups and tariffs to balance out changes in local circumstance. A longer period between resets, for example 10 years, would create a greater incentive effect, while a shorter one would allow frequent reassessment of budgets. This reset could be fixed or decided by Government.
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> No change for business: There will be no difference in the way business pay tax or the way the tax is set. Rate setting powers will remain under Central Government control and the revaluation process will stay unchanged. Rate relief to the needy will be unaffected. National discounts and rate relief will continue to be supported, meaning no adverse change to such groups as charities, amateur sports clubs, voluntary groups, those in hardship, and eligible rural or small firms.[5]

Announcing the consultation, Eric Pickles said "we will ensure that no one will be worse off when the new system is introduced than they would have been under the old system."[6] Responding, Caroline Flint, Shadow Secretary of State for Communities and Local Government, said:

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[5] DCLG, *Local Government Resource Review: Proposals for Business Rates Retention, A Plain English Guide*, July 2011

[6] HC Deb 18 July c663-4

> The Secretary of State may just want to talk about year 1, but we want to talk about year 2 and year 3, and all the years after that. What will the funding system look like then? And will the Secretary of State be able to guarantee today that no council will be worse off in five years' time as a result of the reforms that he has announced this afternoon?[7]

As part of the consultation process, the DCLG issued a number of technical papers relating to the review.[8]

4 Reaction to the review

The Communities and Local Government Committee briefly considered the review in their report on *Localism*:

> Greater financial self-sufficiency for councils is a crucial foundation for localism. If the Government truly wishes to promote far-reaching decentralisation, we expect that the more radical options for reforming local government finance will be considered as part of the resource review. In particular, the case for increasing and broadening the tax and revenue-raising powers of local authorities, and their ability to borrow, must be central to the review. Decisions reached on these matters must be justified in terms of localism.[9]

Caroline Flint, Shadow Secretary of State for local government, has written:

> ...any reform has to include a fairness mechanism that allows the hundreds of councils who rely on business rate distribution not just to survive, but to flourish. All parts of the country deserve the chance to build strong, healthy local economies, built on a thriving private sector. Moving to an immediate local retention of business rates, without any kind of phasing or fairness mechanism, at a time when the government has no plan for growth and many areas are still struggling after the recession would be an enormous gamble. The government is said to be promising an element of redistribution in the new system. This is vital and we will hold them to it. Because without it, the system cannot, in the short term at least, be fair. Less fortunate areas must not be allowed to wither and die by a thousand cuts at the expense of those that are already the most economically vibrant.[10]

The Local Government Group published a consultation paper on the review in May 2011, available here. Following the consultation, the Group published an analysis of local business reaction to the review in June 2011. It included the results of a survey undertaken as part of the consultation exercise:

> 66% preferred business rates to be retained by their council and distributed locally, compared to 20% who favoured them being sent to central government and redistributed according to a nationally determined formula;
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> 44% thought their local economic climate would remain the same over the next year; 32% believed it would worsen and 22% thought it would improve. Businesses in the South of England were the most optimistic (30%), those in the East were most pessimistic that it will improve (13%);

[7] Ibid c 664

[8] See DCLG, *Local government resource review: technical papers*, 2011.

[9] Communities and Local Government Select Committee third report of 2010-12, *Localism*, HC 547 2010-12, p45

[10] "The Labour Party on business rates equalisation", by Caroline Flint, *Rating in Brief*, Issue 24 Summer 2011

> 69% expected to have the same number of staff in a year's time as they do now; 16% expected to have more and 13% less. Businesses in London were the most optimistic about recruiting staff (17%), whilst those in the East were the most likely to believe they would have less (16%).

The Group also published a 10-point plan for reform of the business rates system, which included the suggestions that any change should be based on stability and a continuing commitment to resource equalisation across the country, which would end councils' dependence on grant distribution decisions by the Secretary of State, and which would ensure that councils whose business rate income grows faster than their spending needs make a contribution to equalisation.[11]

Following the publication of the terms of reference of the second phase of the review and Mr Clegg's speech, Sir Merrick Cockell, Local Government Association Chairman, said:

> It is encouraging that the Deputy Prime Minister has acknowledged that the current system of local government funding is in need of reform. Now more than ever, we need to put in place a funding system that will support local public services and generate economic growth. Councils are dealing with the consequences of steep reductions in central government grant, and so it makes sense to move towards a system that gives them greater freedom and flexibility. The current system of funding local government is incredibly complex and does not meet the needs of all the people we serve. Local residents and businesses do not understand the relationship between the money they pay and how much the council has to spend on services. This undermines local accountability and democracy. It is important that any new system recognises the current imbalance in local economies and ensures that there is no localisation without a fair system that allows every community in the country to benefit from the nation's and their local area's economic growth. Reform must also ensure that those areas that do not have the capacity to raise huge amounts of funding through business rates do not lose out.[12]

Reacting to the speech, the Local Government Chronicle noted,

> With business rates reform it seems clear that the government is only considering allowing councils to keep, rather than set the rates – it is retention of the rates, rather than full localisation. With a business lobby trenchantly proposed [sic] to measures that would let councils raise rates, it seems that has been a bridge to far.[13]

On 5 September 2011, Eric Pickles made a number of comments about the review, including that the consultation makes it clear that local authorities will have the ability to bring business rates down, but not to put them up. Mr Pickles also noted that "we will be encouraging, though we will not be prescribing, local authorities to pool the business rates" and "If business rates go through the roof, they will be caught by the "disproportionate" rule and those sums will be taken away and distributed to poorer areas."[14]

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[11] LG Group media release, *Businesses want rates to stay local*, 27 June 2011

[12] Local Government Group media release, *LGA responds to local business rates announcement*, 1 July 2011

[13] Local Government Chronicle, *In praise of Nick Clegg...sort of*, 29 June 2011

[14] HC Deb 5 September 2011 c2-3