Local Government Finance Directorate
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Consultation on Business Rates Reform

Cornwall Council welcomes the opportunity to submit a response and contribute to this consultation.

As stated in our response to the Relative Needs and Resources consultation, we believe that the intention to simplify the system of funding and reform Business Rates Retention, will only achieve a successful and sustainable outcome if the level of the overall quantum is addressed through the forthcoming spending review.

Without this being addressed it is expected that any changes will become merely superficial. A long-term funding solution is desperately required to address the significant pressures that local authorities face, especially in the areas of Adults and Childrens Social Care.

We support the Government's aims to give the local government sector greater control over the income that it raises and to incentivise the sector to support local economic growth. However this needs to be considered alongside the overall sustainability of the system and, in particular, the impact on the high street. We would suggest that further consideration needs to be given to address suitable taxation measures of online retailers.

A significant element of growth in business rates in rural areas, such as Cornwall, relates to small businesses. Whilst we recognise that the increase in thresholds for small business rate relief is good news for many rural businesses that no longer pay any business rates at all, there is the obvious concern that such growth will not bring additional income to the local government sector. To that end it is imperative that the Government continues to compensate authorities accordingly.

We look forward to receiving further information in the near future, as the proposals are developed. It is vital that local authorities have early indications of their funding levels, not only for 2020/21, but also for future years in order to ensure that they get a clear understanding for both financial and service planning purposes.

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Our responses to the specific questions within the consultation are detailed below.

Question 1: Do you prefer a partial reset, a phased reset or a combination of the two?

Cornwall Council would prefer to see a partial (50%) reset that is capable of more quickly redistributing resource based on need.

Question 2: Please comment on why you think a partial/phased reset is more desirable.

As stated above, we believe that this would be capable of more quickly and fairly redistributing resource based on need.

Whilst it is recognised that phased resets give rise to a 'smoother' transition, the more regular resets proposed should avoid unmanageable 'cliff edges' arising.

We believe that it should also allow for greater stability. As part of a partial reset, baseline funding levels are, for example, adjusted every five years and then remain in place for a fixed period providing certainty and stability. Under a phased reset model, funding baselines are adjusted annually and means that government funding levels remain in a constant state of change.

Question 3: What is the optimal time period for your preferred reset type?

A reset every five years offers an appropriate balance between fairness, risk and reward, whilst maintaining a strong incentive for growth.

Whilst revaluations have been confirmed to be every 3 years, we consider that aligning resets with revaluations would be a mistake for the following reasons:

- Revaluations are designed to be cost neutral so should not have any overall impact
- It would reduce the incentive for growth
- It is more transparent and would be easier to measure and see the impact of revaluation and resets if they are kept separate. We would have concerns that aligning the two processes together unnecessarily would lead to a more confused funding settlement as and when changes are made (accepting that every 15 years the two processes will naturally coincide anyway).

Government recognises that, due to the slow 'drift' that may arise under a partial reset model away from baseline funding levels that intermittently (e.g. every 15 years) a full reset will need to be actioned. This may provide opportunity to align full resets with the natural intermittent 'coming together' of revaluations and resets on their respective 3 and 5 year cycles.

Question 4: Do you have any comment on the proposed approach to the safety net?

Cornwall Council agrees with the principle that under the Business Rates Retention system, risk and reward should be shared.

We support proposals for the safety net to give protection to those authorities that are unable to generate business rate growth, for whatever reason, and fall below an acceptable level of their assessed need.

However we consider that a 95% threshold represents a significant risk that, in the event, would have an unacceptable impact on local services. We also consider that growth in business rates should not go unchecked and may favour some authorities with greater capacity for growth and do not think the proposals for the levy go far enough.

This seems to go against the objective of fairer funding and business rate retention resets, which is to distribute resources based on need. It increases rewards retained by high growth areas and reduces the pot available for distribution based on need.

We consider that the 'extraordinary' growth level (see below) is too generous and that this threshold should be reduced to:

i. minimise the necessary 'business rates top slice' (benefiting all authorities based on proportionate need)
ii. generate additional funding for the safety net, and
iii. move the safety net threshold closer to 100%

Question 5: Do you agree with this approach to the reform of the levy?

No. Cornwall Council strongly opposes the proposed changes to the levy.

This is a policy direction that is clearly biased in favour of authorities with greatest capacity for growth and we consider that the existing levy structure should be kept in place.

Proposals to change the levy structure favours high growth authorities and would necessarily increase the top slice on general business rate resources in order to fund the safety net – funding that would otherwise be available for distribution based on need. This is in complete contrast to the overall objectives of fairer funding and business rate retention resets that is to redistribute resource based on need.

Furthermore, Cornwall believes the proposed reforms are fundamentally flawed. We consider that a fixed 'threshold' cannot be set for a period of time over which actual business rates will increase annually with growth, but the baseline funding level/business rate baselines will remain fixed.

Limits of 150%, 200%, 250% of baseline funding levels as mentioned in the consultation are too high and would mean authorities with greater capacity for growth will benefit unchecked from year on year 'extraordinary' levels of growth before reaching the thresholds suggested, if ever at all.

Worse still, this is likely to mean that no levy payments would become due for several years, requiring an extra top slice to the retained business rates for redistribution to fund the safety net.

Instead, we consider that thresholds should initially be lower and then increase annually over the fixed 'period' until the next reset.

Question 6: If so, what do you consider to be an appropriate level at which to classify growth as 'extraordinary'?

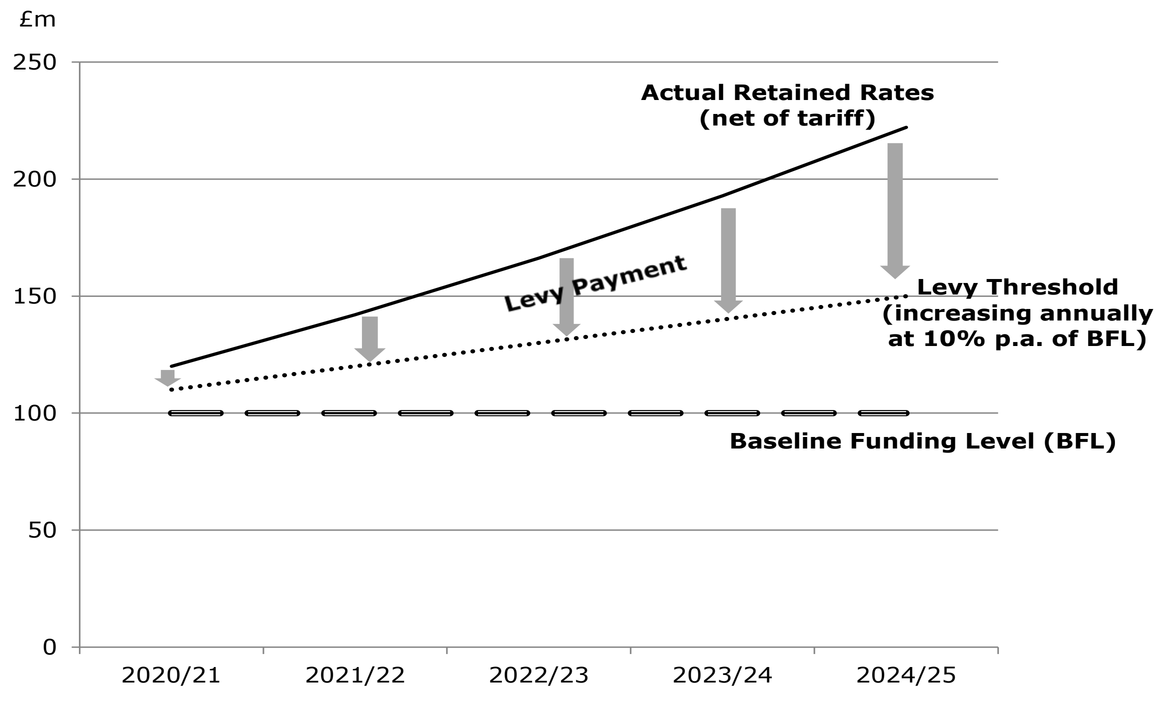
As outlined above, Cornwall Council does not support the proposed reforms to the existing levy system.

However, if reforms are to be introduced, then the proposals as presented are fundamentally flawed and should be reconsidered.

Cornwall Council suggests the following:

- That only tariff authorities should continue to be subject to levy payments (as in the current system). The consultation neither confirms that this will continue to be the case under proposed reforms, nor suggests otherwise.
- That growth of 10% p.a. above an authority's Baseline Funding Level (BFL) should be classified as 'extraordinary' and should form the basis of levy payments.
- Therefore that, in year 1 following a business rate reset, the threshold should be set at 110% of the BFL and that any growth over this level should by subject to 100% levy (effectively capping annual growth to 10% of the BFL).
- Going forward, and to reflect the passage of time against the fixed baseline, the annual threshold should increase by a further 10% p.a. such that, for example, in year 5 the threshold has increased to 150% of the BFL.
- This ensures that 'extraordinary growth' is recognised annually (and cumulatively) throughout the fixed period and that levy payments are made to fund the safety net without requiring further top slices to the retained business rates available for redistribution (based on need).
- This continues to offer significant incentive for growth.

This is illustrated in the following diagram:



Question 7: What should the fall-back position be for the national tier split between counties and districts, should these authorities be unable to reach an agreement?

Question 8: Should a two-tier area be able to set their tier splits locally?

Cornwall Council, as a Unitary Council, is not affected by this issue and has not provided a response.

Question 9: What fiscally neutral measures could be used to incentivise pooling within the reformed system?

Pooling arrangements were initially put in place to share the risk (and rewards) arising from the introduction of business rate retention. Under proposed reforms, those risks have been reduced and the incentive for pooling lessened.

To further incentivise pooling, the Government should give consideration to extending business rate retention from 75% to 100% for pooled areas such that all growth is retained locally.

Alternatively the Government could award pooled areas with an improved safety net offer, although this should not be at the expense of other (non-pooled) authorities.

Question 10: On applying the criteria outlined in Annex A, are there any hereditaments which you believe should be listed in the central list? Please identify these hereditaments by name and location.

Question 11: On applying the criteria outlined in Annex A, are there any listed in the central list which you believe should be listed in a local list? Please identify these hereditaments by name and location.

The proposed criteria for allocating classes of hereditament appear reasonable. Cornwall Council has not identified any other category of asset that should fall within either the local or central list and is not covered by the existing proposed criteria.

Question 12: Do you agree that the use of a proxy provides an appropriate mechanism to calculate the compensation due to local authorities to losses resulting from valuation change?

Subject to further guidance on how this will work in practice (e.g. the impact on opening Business Rate Baselines, Collection Fund Accounting treatment etc) Cornwall Council supports proposals for the centralisation of appeals and valuation changes risk.

Whilst the use of a proxy is not perfect, it is a workable mechanism. Indeed this is consistent with the existing system that already uses a proxy for appeals risk of 4.7% within the established business rate baselines.

We recognise that proposals will ‘even out’ the disproportionate distribution of risk across the sector. However it is important that any ‘surplus’ in the topslice is, in due course, returned to the sector in full based on need.

Question 13: Do you believe that the Government should implement the proposed reform to the administration of the business rates retention system?

We agree that the four alternative options presented at paragraph 3.3.6 of the consultation do not offer an acceptable solution for the reasons outlined in the document.

It is recognised that proposals to reform the administration of the system would, in some ways, lead to a simpler system that:

- Provides certainty of funding (but for the forthcoming year only)
- Addresses/removes volatility caused by appeals/valuation changes
- Continues to incentivise growth

However we would stress, in no uncertain terms, that this revised system should not be considered a simple system, nor do we consider that this is necessarily a positive move for local government finance.

Much work is still clearly required to be carried out in order to ascertain how this will work in practice. Alongside this, the additional burdens by bringing forward completion of the annual NNDR1 return and associated system requirements to collate the required information must be considered in depth.

Most significantly we have serious concerns at the necessary 'lag' within the system which would mean growth that is achieved locally could not be recognised within the budget until two years later (e.g. growth achieved in 2020/21 would be calculated from the NNDR3 return that is completed in July 2021 and would feed in to the revised top up/tariff in 2022/23).

Under the current system, all local business rate growth is recognised in the year it is achieved (per NNDR1) and any additional gains that are identified in the NNDR3 return are distributed in the following year.

Under the revised system, those gains would temporarily be deferred through the 'variable' top up/tariff, effectively capping the annual budget to baseline funding level.

This is unacceptable and seems to be a heavy price to pay in order address appeals risk. Indeed, left unchecked, this will likely lead to a reduction in the annual budget that is available for the delivery of services whilst authorities wait two years for funding levels to 'catch up'.

It may be that with further work, this 'lag' can be addressed through additional transition arrangements put in place at the outset of the reforms. However, it is also unclear how this will work within a system of 3-5 year resets? With funding levels always two years behind, this is likely to lead to an extremely unclear and contentious settlement. It is therefore essential that settlement calculations are presented transparently and in a clear and understandable manner.

It is disappointing that the consultation does not advise on what measure of actual 'growth' will be brought into the settlement, with reference made to both gross and net collectible rates.

Cornwall Council contends that this should be based on gross rates to ensure that, for authorities with a higher proportion of small businesses, all growth is recognised in the system fairly and equally and is not is not then lost to small business rate relief.

Question 14: What are your views on the approach to resetting Business Rates Baselines?

It is pleasing to see positive confirmation that existing growth within the system will be redistributed across the sector on the full reset of the Business Rates Retention system in 2020, alongside and as part of the wider review of relative needs and resources.

It is essential that this is transparent in the settlement and is not used to offset other additional 'stealth' government funding cuts within the spending review.

We are disappointed to see that transition arrangements from one system in 2019/20 to new baselines in 2020/21 are not part of this consultation. Given the close timeframes, this creates considerable uncertainty for financial planning and it is essential that proposals are brought forward for consideration as soon as possible.

Proposals to reset the Business Rate Baseline are reasonable but, in particular, we advise:

<u>Non Collection Levels</u>; should be constructed using an average of the last three years data to ensure that estimates are robustly based on actual collection levels over a reasonable period of time.

<u>Appeal Provisions</u>; it is recognised that assumptions on appeals are more difficult to make and likely to create greater volatility within the system.

Forecasting is made harder due to the low number of actual valuation changes arising out of the 'check, challenge, appeal' process and is exacerbated by the differing accounting policies and methodologies that have been applied across the sector.

For that reason, it is unlikely that local authority appeal provisions are based on any reliable and quantitative data but more likely continue to be founded on the underlying appeal allowance of 4.7% that was initially built into the settlement by government on revaluation 2017.

Therefore, whilst not perfect, we consider that the Government should continue to base the appeals deduction on its own estimate of future appeal losses (as proposed at option b) in paragraph 4.10 of the consultation), aggregated and apportioned between authorities based on their business rate base.

This will at least impact equally across all councils and would remove any incentive to 'play' the system that could otherwise be the case under options a) and c) by deliberately over estimating an authority's expected level of future appeals.

Question 15: Do you have any comments at this stage on the potential impact of the proposals outlined in this consultation document on persons who share a protected characteristic? Please provide evidence to support your comments.

As stated in our introductory commentary, it is clear that the overall quantum available to the sector is not enough. It is imperative that first and foremost this must be addressed in the forthcoming spending review.

The proposed reforms to the Business Rate Retention system merely redistribute resources between authorities.

We have previously highlighted the impact on equalities for those residents in rural areas such as Cornwall, where the pressures of having a larger proportion and increasingly growing elderly population are greater than those living in London Boroughs and Metropolitan areas.

Cornwall Council will continue to make every effort to prioritise resources to support the most vulnerable members of the community. However, without sufficient funding, it is impossible to provide services without impacting on the level of support for all service areas. Whilst we would always seek to protect the most vulnerable in our community, it is almost certain that this will impact on protected characteristic groups.

A fairer distribution of resources which ensures that rural councils like Cornwall receive a fair share of the funding allocation is vital to help mitigate these concerns.

If you have any questions regarding this submission, in the first instance, please contact Anthony Humphreys on 01872 324506 or anthony.humphreys@cornwall.gov.uk

Yours sincerely

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