APPENDIX 1

EFDC CONSULTATION RESPONSE TO LOCAL GOVERNMENT RESOURCES REVIEW: BUSINESS RATES RETENTION

COMPONENT 1: SETTING THE BASELINE

Q1: What do you think that the government should consider in setting the baseline?

Local authorities are facing huge financial pressures as a result of the challenging economic climate. Furthermore they are also managing the impact of other significant changes to the local government finance system including the localisation of council tax benefit localisation, the creation of Enterprise Zones and self financing for the Housing Revenue Account. Therefore, EFDC agrees with the government that minimising the impact of the business rates system upon local authorities' budgets in the first year of the new system is of paramount importance.

The Council also recognises that the additional incentives to generate NNDR growth ought to be embedded within the business rates retention system as soon as possible after the business rates retention system is introduced.

The baseline should also include any one-off grants given to fund Council Tax freezes. If such grants are not included local authorities would be penalised in future years funding for complying with Government policy.

Q2: Do you agree with the proposal to use 2012-13 formula grant as the basis for constructing the baseline? if so, which of the two options at paragraphs 3.13 and 3.14 do you prefer and why?

Given the importance of minimising turbulence in authorities' funding positions in 2013-14 EFDC believes that option 1 should be adopted. Reviewing limited aspects of the formula and updating the data used in the formula will create turbulence within a system that will already be subject to significant change.

COMPONENT 2: SETTING THE TARIFFS AND TOP UPS

Q3: Do you agree with this proposed component of tariff and top up amounts as a way of re-balancing the system in year one?

To ensure that authorities do not have problems funding their core services or find they have excess funding a system of tariffs and top-ups as described in the consultation paper would be required.

Q4: Which option for setting the fixed tariff and top up amounts do you prefer and why?

EFDC supports the use of RPI indexing for the calculation of tariff and top-up amounts. The Council recognises that not applying RPI to the top-up amounts could pose significant challenges for top-up authorities who would experience a real terms cut in funding if they experienced stagnation of their NNDR taxbase. Adjusting local authorities' top-up and tariff amounts by RPI would also mitigate against the extent to which top-up authorities would have to rely upon any safety net to protect against reductions in their NNDR taxbase.

COMPONENT 3: THE INCENTIVE EFFECT

Q5: Do you agree that the incentive effect would work as described?

EFDC agrees that in principle the proposal to allow local authorities to retain the increase in their business rates will provide an incentive to grow their business rates taxbase. That said, EFDC already works closely with the local business community, the voluntary sector, and its public sector partners to foster economic growth in the area.

The council is concerned that the incentive effect could be diluted by a number of factors:

1. System complexity and opaqueness: the Local Authority Business Growth Incentives (LABGI) scheme failed to change authorities' behaviour as the approach was convoluted and overly complex. The NNDR retention scheme should be based on transparent financial information and CLG could assist authorities by sharing financial modelling used to design the scheme. In that context EFDC was disappointed that CLG's interactive calculator was of limited use and some financial information such as HM Treasury's forecasts of NNDR growth have still not been shared with local authorities.
2. Set aside: CLG propose calculating the difference between forecast NNDR growth (as yet unknown) and the Departmental Expenditure Limit with the difference, known as the set aside, removed from the local government finance system. The financial challenges facing the country are clear but it must be recognised that local authorities will have to exceed the Government's NNDR growth forecasts to see significant financial benefits from NNDR growth. There must be transparency of the NNDR growth forecasts, local government involvement in the calculation of the forecasts, and CLG should keep the set aside amount under review between resets in case HM Treasury's NNDR forecasts are overstated.
3. Levy on disproportionate benefit: EFDC is concerned that the levy on disproportionate benefit must only be used to fund safety net initiatives. There is a significant risk that setting the levy on disproportionate benefit at too high a level will create a disincentive to generate economic growth.

COMPONENT 4: A LEVY RECOUPING A SHARE OF DISPROPORTIONATE BENEFIT

Q6: Do you agree with our proposal for a levy on disproportionate benefit, and why?

EFDC supports a levy on disproportionate benefit but only if the proceeds are specifically ringfenced to provide support to authorities that experience a significant decline in their NNDR receipts. EFDC would not support a cap on disproportionate benefit such that all NNDR receipts over a defined threshold were appropriated as this would undermine incentives to generate NNDR growth.

EFDC strongly supports the use of pooling arrangements to mitigate the impact of NNDR volatility upon local authorities' net funding positions. The levy on disproportionate benefit should be reduced for pooling authorities to reflect the reduced likelihood of these authorities having to call upon the safety net.

Q7: Which option for calculating the levy do you prefer and why?

The third option is preferable as it provides a more equal incentive.

Q8: What preference do you have for the size of the levy?

EFDC feel that it would be unwise to set a value for the levy prior to seeing the Government's forecasts for business rates. There should also be an estimate of the draw on the levy pot (for example, to fund the "safety net") which should inform any decisions about the levy. This would mimic the situation in current local government finance settlements where the scaling factor and floor are set in order that they are self funding. Obviously under the rates retention it would not be possible to be so accurate, nevertheless the Council feels that it is not possible to set the size of the levy so far in advance.

Q9: Do you agree with this approach to deliver the renewable energy commitment?

EFDC agrees that additional NNDR receipts generated by renewable energy projects should be retained by local authorities and that the associated NNDR revenue should be discounted in the calculation of any levy that might be applied to growth in business rate revenues.

EFDC believes that the sharing of gains from the delivery of renewable energy projects should reflect the following principles:

- The split of NNDR between tiers should recognise the key role of districts in delivering projects in their communities and then being able to directly demonstrate the benefit through local retention of the growth;
- There is no justification for treating the split of growth in NNDR receipts relating to renewable energy projects any differently to other business sectors;
- To avoid burdensome complexity there should be a consistent approach for all renewable energy projects in terms of the split of NNDR between council tiers; and
- There should be a clear separation of the decision to grant planning consent for renewable energy projects from any financial incentives.

Therefore, EFDC believes that retained additional NNDR growth relating to renewable energy projects should be shared by district and county council using the same methodology as applied with the New Homes Bonus of an 80/20 split in favour of district councils. Indeed this split should be used consistently throughout the entire NNDR local retention scheme for rewarding growth.

Q10: Do you agree that the levy pot should fund a safety net to protect local authorities:

i) Whose funding falls by more than a fixed percentage compared with the previous year (protection from large year to year changes); or

ii) Whose funding falls by more than a fixed percentage below their baseline position (the rates income floor)?

Since decline in income will happen for various reasons it would seem sensible to protect authorities from absolute falls in income (when compared with the baseline) in addition to large year-on-year negative fluctuations.

Q11: what should be the balance between offering strong protections and strongly incentivising growth?

A stated objective of the reform is to incentivise growth and for this to happen more emphasis will have to be given to growth than protection.

Q12: which of the options for using any additional levy proceeds, above those required to fund the safety net, are you attracted to and why?

Prior to implementation of the business rate retention system EFDC wishes to see transparent guidelines that precisely detail how any of the levy proceeds over and above the safety net would be either used to support local authorities or reallocated back to them. There ought to be very limited scope for subjective judgements on the application of the levy pot. In particular EFDC does not wish to see a bid based approach for any of the applications of the levy pot.

EFDC supports the use of the levy to provide ongoing support to authorities that have experienced significant losses that take more than one financial year to recover from. EFDC would then like to see the remaining levy pot being redistributed to all local authorities in proportion to each authority's baseline.

Q13: Are there any other ways you think we should consider using the levy proceeds?

No. There should be a clear and transparent rationale for distributing levy proceeds that do not rely upon subjective political judgements. The use of levy proceeds should be focussed upon providing a safety net for authorities.

COMPONENT 5: ADJUSTING FOR REVALUATION

Q14: Do you agree with the proposal to readjust the tariff and top up of each authority at each revaluation to maintain the incentive to promote physical growth and manage volatility in budgets?

EFDC recognises that the process of revaluation is a given; changes in the property market must be reflected in adjustments to the rateable value of properties. Furthermore, without an adjustment to the tariffs and top-up amounts local authorities could see significant turbulence in their funding positions. Therefore, EFDC supports the adjustment of tariffs and top-ups at revaluation. However, further analysis based upon previous revaluations is required to establish what would be the impact upon local authorities if their position switched from a tariff to a top-up authority, or if the extent of their tariff and top-up changed significantly.

Q15: Do you agree with this overall approach to managing transitional relief?

EFDC agrees with the approach to transitional relief as the best way of mitigating against the exposure of local authorities to financial pressures over which they have no control.

COMPONENT 6: RESETTING THE SYSTEM

Q16: Do you agree that the system should include the capacity to reset tariff and top up levels for changing levels of service need over time?

The current local government finance system is based upon an assessment of each authority's needs and resources. Local authorities provide a wide range of services which are not all linked to the generation of economic growth, and in some areas (e.g. where there is a focus on high technology or service industries that generate significant economic activity from a small property base) the link between economic growth and NNDR growth is weak. EFDC is concerned that the consultation leaves open the possibility of no reset to the system and the abandonment of the link between service demand and funding. EFDC supports the capacity to reset tariff and top-up levels for changing levels of service need.

Q17: Should the timings of reset be fixed or subject to government decision?

EFDC believes that there should be a fixed period between resets. This will maximise transparency and certainty in the local government finance system. Furthermore it will mitigate against Government undertaking resets to reflect changing political priorities and will limit the extent to which local authorities are incentivised to lobby for resets to reflect their particular interests.

Q18: If fixed, what timescale do you think is appropriate?

A five year period between resets would offer a balance that incentivises local authorities to grow their NNDR taxbase but that maintains the link to underlying service pressures facing local authorities.

Q19: What are the advantages and disadvantages of both partial and full resets? Which do you prefer?

EFDC is concerned that there is a lack of detailed information on how a full or partial reset would operate. This makes it difficult to draw any conclusions on the advantages and disadvantages of each approach. A partial reset may be inadequate to reflect the changing balance of service needs across the country.

Q20: Do you agree that we should retain flexibility on whether a reset involves a new basis for assessing need?

The current assessment of need is subjective and does not reflect actual levels faced by individual local authorities. The timetable for implementation of the business rates retention system and the importance of avoiding turbulence in authorities' funding allocations, rule out introducing a revised assessment of need before the NNDR retention system is introduced in April 2013. However, in advance of the first reset local and central government should work together to agree a revised approach to the assessment of need.

COMPONENT 7: POOLING

Q21: Do you agree that pooling should be subject to the three criteria listed at paragraph 3.50 and why?

EFDC agrees with the three criteria for pooling in the consultation paper.

Q22: What assurances on workability and governance should be required?

Central government should only require the minimum of assurances for pools to be approved. Local government interest groups should be tasked with working together to establish minimum governance arrangements. Each group of local authorities that

decide to explore pooling should then have the freedom to tailor the governance of pools to their requirements. The following issues would need to be addressed:

1. Terms of reference of pooling arrangements
   The aims and objectives of pooling arrangements must be clearly set out before the pool is established.
2. Apportioning growth in NNDR amongst pool members
   Whilst this could be a contentious area, EFDC believes that if the default is sharing NNDR growth amongst pool members on the basis of their actual contribution to NNDR growth this would leave authorities in a no better no worse position.
3. Management of the pool
   The management arrangements for the pool should be clearly articulated and agreed to by all pool members. This would have to address factors including how members would be involved in decision making, the links to each authority's governance procedures, the chairing and secretariat for the pool.
4. Apportioning the costs of managing the pooling arrangements
   As per EFDC's response to Q24 the lead authority should be provided with funding to support the management of the pool.
5. Dispute resolution
   There are a range of factors including the scale of the financial benefits at stake, potential different political control of local authorities in the pool, self interests of pool members etc. that a clear dispute resolution process covering the operation and administration of the pool must be agreed.
6. Termination arrangements
   The governance documents for the pool should set out the circumstances under which the pool would be terminated or individual members could withdraw from the pool should be addressed.
7. Dissolving the pool
   Arrangements for dissolving the pool such as sharing the costs of closing the pool should be agreed by pool members.

Q23: How should pooling in two tier areas be managed? should districts be permitted to form pools outside their county area subject to the consent of the county or should there be a fourth criterion stating that there should always be alignment?

Districts ought to be permitted to participate in pools outside of their county area if that allows the benefits of pooling to be realised more successfully than pooling with the county and districts in the county area. There should be the freedom for authorities to create pooling arrangements with other districts or unitaries without the relevant county council being involved in the relevant pooling arrangement if this serves to manage billing authorities' NNDR volatility and maximise economic growth.

EFDC believes that if any districts decided to enter into pools with authorities outside of their county area then they should only be able to do so in 2013-14 when the new system is implemented or when the partial or full reset takes place.

Q24: Should there be further incentives for groups of authorities forming pools and if so, what would form the most effective incentive?

Authorities that express an interest in creating a pool should be provided with funding to develop pooling proposals including procuring legal and financial advice. Upon implementation central government should recognise that there will be a lead authority for each pool and the costs of administering the scheme ought to be an

allowable deduction that is not subject to the pool on disproportionate levy. Such arrangements are not incentives but merely eliminate disincentives to establish pools; they would put pooling authorities on a no better, no worse position relative to non pooling authorities.

To overcome authorities' potential concerns that they will lose control of NNDR growth strong incentives to form pools need to be built into the business rates retention system. To achieve this local authorities entering into pooling arrangements should see a reduction in the levy on disproportionate benefit applied to the pool. The reduction in the levy should be sufficiently large to incentivise authorities to come together to form pools

IMPACT ON NON-BILLING AUTHORITIES

Q25: Do you agree with these approaches to non-billing authorities?

EFDC agrees with CLG that police and fire authorities have limited influence over the generation of NNDR growth in an area. The council therefore supports the removal of police and fire authorities from the business rates retention system. Following the end of this Spending Review period EFDC would support an approach that provided all government funding for police and fire authorities through the Home Office rather than providing a proportion through the local government funding system.

EFDC acknowledges that county councils have some influence upon economic growth and that therefore they should be allocated a proportion of NNDR receipts for their area. However, the reward share for growth should be consistent with the 80/20 split of New Homes Bonus (NHB) funding between districts and counties.

CHAPTER 4: INTERACTIONS WITH EXISTING POLICIES AND COMMITMENTS

NEW HOMES BONUS

Q26: Do you agree this overall approach to funding the new homes bonus within the rates retention system?

EFDC welcomes the commitment that central government made to ring fence £1bn for the NHB during this Spending Review period. We also recognise that there was a commitment that any additional costs of the scheme during this Spending Review period and beyond would be financed from centrally pooled business rates. The proposal in the consultation paper appears to step back from this commitment and proposes funding the ongoing costs of the NHB from centrally pooled business rates after the calculation of the set aside adjustment. EFDC does not agree with this approach. Instead EFDC would strongly support the set aside adjustment being calculated after reducing forecast NNDR for 2013-14 and 2014-15 by the projected costs of the NHB scheme.

Within two-tier areas the NHB grant is split 80/20 amongst districts and counties. This properly reflects the limited role county councils play in new homes development. As stated above, this split should also be used for sharing growth in NNDR to reflect the key role of district councils in driving growth in their areas and provide consistency in funding methodologies.

Q27. What do you think the mechanism for refunding surplus funding to local government should be?

EFDC supports the return of surplus funding to local government in proportion to their 2012-13 baseline funding levels. The surplus funding must not be top sliced to fund any new burdens; any such adjustments ought to be met from within the 'set aside' amount.

BUSINESS RATES RELIEF

Q28: Do you agree that the current system of business rates reliefs should be maintained?

Given the breadth of the changes to the local government finance system EFDC agrees that the system of business rate reliefs should be maintained.

However, EFDC believes that the element of the current system of reliefs that is determined centrally should not be part of the business rates retention system i.e. they should not be deducted from NNDR projections before the calculation of tariff and top-ups. Fixing tariffs and top-ups between resets such that a level of reliefs is assumed passes the risk that the actual level of reliefs exceeds forecasts to individual local authorities. Given that the level of mandatory reliefs granted is volatile and that local authorities have no control over the level of reliefs then mandatory relief should be managed using the same approach proposed for transitional relief. This approach would ensure that local authorities continue to be incentivised to increase take-up of mandatory relief for those recipients that government wishes to target with financial assistance.

CHAPTER 5: SUPPORTING LOCAL ECONOMIC GROWTH THROUGH NEW INSTRUMENTS

Q29: Which approach to tax increment financing do you prefer and why?

Local authorities will be free to undertake projects that would be captured by option 2 under their prudential borrowing powers. Under CIPFA's prudential code local authorities will have to satisfy themselves that it remains prudent, affordable and sustainable to borrow to fund infrastructure projects that generate additional NNDR growth. The key factor that authorities will consider is the certainty that they will be able to retain the associated additional NNDR growth. EFDC believes that it appears unlikely given the levy on disproportionate benefits, potential resets, set aside adjustments etc. that there will be a significant number of TIF projects funded by additional prudential borrowing. Therefore, whilst EFDC welcomes the additional infrastructure opportunities provided by the NNDR retention scheme it is clear that this is a fortunate by-product of the reforms rather than an option that needs central government approval or action to be implemented.

Experience from TIF projects in other countries suggests that projects are successful when they:

1. are small scale;
2. very clearly generate additional (i.e. not just displacement) local tax receipts over and above that which would have been generated without the TIF infrastructure investment;
3. have a relatively low ratio of capital investment to additional local tax receipts; and
4. are bankable i.e. if they are to facilitate additional borrowing then projects must have certainty that over the lifecycle of the TIF project the lead partner will continue to receive any additional tax receipts generated.

To fulfil the fourth condition NNDR receipts must therefore be ringfenced as is proposed under option 2. Whilst this will reduce the resources available to protect against NNDR volatility EFDC believes that if the second condition identified above is fulfilled then the number of projects will be limited to those projects that generate additional NNDR growth that would not otherwise have been created.

Therefore, EFDC would accept central government approval of TIF projects delivered under option 2 if the following preconditions are applied to the evaluation of the projects:

- Clear and unambiguous demonstration of the additionality of NNDR growth;
- More frequent than quinquennial revaluations of properties covered by the TIF project area;
- Robust governance procedures e.g. identification of lead authority in two tier areas;
- Demonstration of the support of all LAs affected by the TIF scheme;
- Use of standard form contracts e.g. financing documentation; and
- Compliance with a common approach to financial modelling of TIF benefits. For example, common assumptions on interest rates, modelling NNDR growth, discount rates etc.

EFDC is disappointed that of all the additional tax receipts that would be generated by a TIF project only additional NNDR growth will be included within the remit of any TIF project. This is not how TIF projects have been made to work successfully in other countries. Local authorities alone will take the risk that additional infrastructure investment generates additional economic growth that leads to growth in the taxbase. If a TIF project succeeds then central government would reap the benefits of additional VAT, corporation tax, NI etc. receipts generated by the TIF project. Central government should bear some of the financial risk associated with the success of the TIF project or alternatively the local authority leading the TIF project should take a share of all additional tax receipts generated.

Q30: Which approach do you consider will enable local authorities and developers to take maximum advantage of tax increment financing?

For the reasons cited in the response to Q29 describing infrastructure projects delivered under option 1 as TIF projects relies upon a very wide interpretation of TIF – they are merely capital infrastructure projects funded by prudential borrowing. Nevertheless, the more certainty and transparency of the NNDR retention system, the more likely authorities will be able to undertake prudential borrowing to finance infrastructure projects that generate additional NNDR growth.

Q31: Would the risks to revenues from the levy and reset in option 1 limit the appetite for authorities to securitise growth revenues?

For the reasons identified in Q29 EFDC believes the uncertainty associated with retained NNDR growth under the new system will not allow LAs to ‘securitise growth revenues’. The inherent uncertainty of NNDR receipts for local authority areas, rather than NNDR growth relating to specific developments, and the impact of the levy, resets etc. means it is likely that there will only be a marginal increase in prudential borrowing to fund infrastructure projects.

Q32: Do you agree that pooling could mitigate this risk?

No, pooling authorities will still be subject to the funding uncertainties identified in the responses to Q29 to Q31. Furthermore pools would have to manage the added complexity of having to establish how the downside risks of a failing TIF structure would be managed between pooling authorities.

Q33: Do you agree that central government would need to limit the numbers of projects in option 2? how best might this work in practice?

EFDC recognises that projects delivered under option 2 would have to be limited because approving these projects would take NNDR receipts out of the NNDR retention system. However, EFDC is more concerned that TIF projects delivered under option 2 must be able to clearly demonstrate that any infrastructure investment will generate additional NNDR growth over and above any growth that would have been generated had the TIF project not been undertaken. Subject to fulfilment of the preconditions identified in Q29 then projects should be taken forward. Additionality of NNDR receipts means that there would be no reduction in the NNDR receipts available to manage volatility or to provide a safety net for authorities.