LOCALIS

Press release – *Embargoed until 00.01 Monday March 28th, 2011*

Report calls for reform of business rates to allow councils to drive economic growth

Localis, the localist think-tank, today launches a report – 'The Rate Escape' – which argues that the current system of local government finance in England is opaque, highly centralised and riven with perverse incentives. It goes on to suggest that giving councils more control of their locally collected business rates will empower them to play a crucial role in supporting local businesses, and should form a key part of the Government's plans for national growth.

Click here to see a full embargoed version of the report

Research for the report, produced in partnership with Ernst and Young, shows that the vast majority of councils are straining to throw off centrally imposed constraints and once again be given the freedom to innovate and drive local economic growth. A Localis survey, carried out as part of the report and completed by over 200 English council leaders and chief executives shows that 99.5% of councils want more financial autonomy, and 96% want more control over their locally collected business rates - with equal enthusiasm from both southern and northern councils. The survey also found that financial incentives, including the local retention of business rate growth, would drive a wave of innovation in councils across the country, particularly in the north and midlands, where 4 in 5 councils believe that more incentives would make them more innovative.

The report proposes that councils should be allowed to voluntarily 'buy-out' of the formula grant (the centrally-controlled current system) for a fixed period. This would mean that every council, regardless of whether it was a net contributor to, or net beneficiary from, the current system has an equal opportunity to benefit from local business rate growth. The 'Buy-Out Model' would provide every council with a fair incentive, balancing risk and reward, while ensuring that rich authorities continue to support more deprived areas. However, the Buy-Out Model does not propose allowing councils to set business rates, which will continue to be done at the national level.

The Buy-Out model will empower local government as well as helping to drive and rebalance the national economy, while acting as a significant step towards re-building the trust between local government and the business community.

Alex Thomson, Chief Executive of Localis, said: "The current system is broken, and is in need of reform. Local government agrees. We need to put real financial power in the hands of councils again, but it will take time. In the current economic climate, it is even more important that the Government looks at reforms that are swiftly implementable, and that would have a lasting impact on the local and national economy. Our model will do just that."

The Buy-Out Model will also link effectively with other initiatives to support growth. In particular, councils with full control over business rates revenue will be in a much stronger position make confident predictions of their business rates income, and therefore able to make more effective use of their Tax Increment Financing (TIF) capabilities. The existing Business Improvement Districts scheme and recently introduced Local Enterprise

Partnerships (LEPs) will also work well in conjunction with the ‘Buy-Out Model’, especially since both provide even greater incentives for local businesses and councils to work closely together.

John Baker, Partner at Ernst and Young, who carried out the detailed financial analysis on the report, said: “Councils deserve greater influence and control over their own local economic destiny. These proposals provide valuable impetus to the growth agenda and more scope for local authorities to innovate.”

QUOTES:

Sir Michael Lyons, author of the last major review of local government finance said: “This Localis report is an interesting contribution to the debate and I urge anyone interested in finding a solution to the nagging issues of local government finance to consider its proposals.”

Bob Neil MP, Parliamentary Under-Secretary of State, said: "Localis' report underlines the real importance of Government's drive to end councils' dependence on the whims of Whitehall grants. We've been absolutely clear in our Resource Review that we want to put elected local councils back in control, by letting them retain their local business rates and in doing so give them real a stake in their local economy, creating local jobs and supporting local firms."

Miles Templeman, Director General, Institute of Directors, said: “The Institute of Directors welcomes Localis’ report, which sets out a powerful model for business rate reform. These proposals safeguard business certainty by rejecting local rate-setting powers, while ensuring that councils that foster business are rightly rewarded by retaining more of their rates. The existing business rate system hasn’t delivered the local authority support for private sector growth that we so desperately need, so it’s time for a change.”

Dr Adam Marshall, Director of Policy at the British Chambers of Commerce, said: “Business rates are an emotive subject for companies and local authorities alike. Chambers of Commerce across the country agree that reform is needed, and are keen to explore new ways to link rates to economic growth and development. Proposals for business rate retention, like the model put forward by Localis in this interesting and thought-provoking report, could offer some areas a real and practical way to share in the benefits of growth, rather than see revenues sucked into the Exchequer the moment they are collected. We must remember, however, that further reform of business rates depends upon a fundamental improvement in levels of trust between local councils and local business communities. The time is emphatically not right for the re-localisation of rate-setting powers.”

Roger Culcheth, Local Government Committee Chairman at the Federation of Small Businesses, said: “Business rates place a huge burden on small business as they are the third biggest cost to a business after rent and wages. Aside from this, one of the flaws of the current system is that it fails to create a significant incentive for councils to adopt pro-growth policies. We would therefore be open to looking at ways the retention of business rates revenue can be used to create that incentive, provided it is accompanied by a cast iron guarantee that there will be no localisation of the power to set rates. The Localis proposals present an interesting and innovative option worthy of further discussion. However, the FSB want to be sure that any system is fair, and a thorough review of the options is therefore welcome.”

Cllr Stephen Alambritis, Labour Leader of the London Borough of Merton, said: "The redistribution of business rates has been vital because of the huge differences between the tax base of different local authorities. This does not mean we should not look at reform. However, it must be reform which maintains fairness and redistribution. Localis' report achieves this, whilst also offering a real incentive to councils to support economic growth in local areas"

Paul Carter, Conservative Leader of Kent County Council, said: "The Local Government Finance Review is a once-in-a-generation opportunity for change. We need a system of funding that's open, honest, transparent and needs-led - the current unfairness has to stop. Localis' "The Rate Escape" report offers Government a new way of looking at the Business Rate, incentivising councils to strive for greater autonomy and giving them greater choice. It ensures the Business Rate is a catalyst for local growth and change within wider finance reform in which we must get all the fundamentals right."

Cllr Richard Kemp, Leader, LGA Liberal Democrat Group, said: "This Localis report shows us that we don't need any more reports on this issue. It is now a question of political will. This report makes suggestions about how to deal with a subject that does not appear to be politically difficult - the return of the business rate to local government. The winners and losers are obvious it's how we relate the two that could be contentious. The sooner the Government grasps this nettle the sooner we can then get on to more fundamental aspects of local government financial reform."

The report, **'The Rate Escape: Freeing local government to drive economic growth'**, produced by Localis in partnership with Ernst & Young, will be launched at 3pm on Monday 28th March.

For more information on this report or to arrange an interview, please contact:
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About Localis

Localis is an independent think-tank dedicated to issues related to local government and localism. We carry out innovative research, hold a calendar of events and facilitate an ever growing network of members to stimulate and challenge the current orthodoxy of the governance of the UK. Please visit www.localis.org.uk for more information

NOTES TO EDITORS:

1. **The report also addresses some of the key practical considerations arising from the Buy-Out model**

   - **Two-tier areas**
   In two –tier areas, councils put forward a joint 'federal' proposal for buy-out, with the incentive distribution decided locally
   - **Risk**
   For those few councils with a disproportionately large business rates base, a special risk-sharing arrangement with the Treasury should apply to ensure that the authority will not experience dangerous income volatility. The arrangement will mean that these authorities will have a local element and a national element to their business rates base, which will share any above-projection increase or below-projection shortfall.
   - **Economic shocks**
   A small levy should be taken from buy-out tariffs to create an Emergency Fund. The Fund should be used only in cases of severe and demonstrable economic shocks, and not to compensate for inadequate financial management. Access to the Fund should be strictly controlled, either through imposing a stringent set of circumstances in which it can be accessed, or through a process or peer review for any authority wishing to access the Fund. Money from the Fund should be treated as a loan to the authority in need, to be paid back when that council's business rates revenue returns to above-projection growth (possibly in the next buy-out cycle)
   - **Extra support for the most deprived areas**
   The Government should set up a fund to support areas with a high level of deprivation to invest in Early Intervention Programmes and Infrastructure Projects. Up-front buy-out of the formula grant should be additionally incentivised on the basis that it raises extra money for the Treasury to invest in these funds

2. Full survey results

The survey was sent out to the Chief Executive and the Leader of every council in England, and 195 completed the survey. The results below are from all responses to the survey, although we also analysed the data for geographical and council type variations.

1. Should councils be given greater financial autonomy? (Yes - 99.5%, No - 0.5%).

2. If possible, would you like to see more taxes collected and spent locally? (Yes - 95.5%, No - 4.5%).

3. If it were possible to create a fair system for every council, would you like to be completely independent of central government funding? (Yes - 77.0%, No - 23.0%).

4. Would financial incentives make your council more innovative? (Yes - 76.0%, No - 24.0%).

5. What is more important for local government finance – central equalisation or local autonomy? (Local autonomy much more important - 35.1%, Local autonomy slightly more important- 26.7%, Both equally important -29.2%, Equalisation slightly more important - 3.5%, Equalisation much more important - 5.4%).

6. To what extent can a council impact on the local economy? (A large amount - 42.6%, A moderate amount - 41.6%, A small amount - 15.3%, Not at all - 0.5%).

7. Would you like more control of business rates in some form? (Yes - 96%, No - 4%).

The North and Midlands is defined by the following regions: North West, North East, Yorkshire and Humber, East Midlands, West Midlands