Leaders' Committee

Business rates devolution for London Item 5

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Summary

Leaders Committee in December 2015 agreed a set of overarching ambitions for the potential devolution of business rates to London, and established a small working group to oversee the development of proposals. Since then further details of the Government's thinking have emerged, including the commitment set out in the March 2016 Budget to "explore with London options for moving to 100% business rates retention ahead of the full roll out of the business rates reforms." Government intends to consult formally on the approach to business rate devolution in July 2016.

This report sets out the latest position and seeks Leaders' endorsement of a 'statement of principles' for the design and management of devolved business rates in London, as the basis for a potential joint submission with the Mayor of London to Government before the end of June.

Recommendations

Leaders are asked consider the report and to:

(1) amend and endorse as appropriate the 'statement of principles' for business rate devolution in London, as set out in Appendix 2

(2) seek agreement with the Mayor of London to submit the statement of principles jointly by the end of June, and to delegate final approval of any significant amendments required elected officers via the urgency procedure

(3) note that there will be ongoing discussions to explore with Government the early introduction of elements of business rate devolution in a London 'pilot'.

Business rates devolution for London

The Government's reform proposals

1. In October 2015, the Chancellor of the Exchequer announced substantial changes to the way local government will be funded by 2020[1]. The full £26 billion of business rates collected each year will be devolved to local government (100 per cent retention), RSG will be abolished and local authorities will be expected to deliver additional responsibilities with the extra net funding these changes imply. The uniform (national) business rate will be abolished and local authorities will be able to reduce business rates locally to attract businesses. Areas with city-wide elected mayors will be able to levy an increase in business rates (up to a 2 per cent cap), subject to a majority vote of the business members of the LEP.

2. Subsequent announcements in the November Spending Review, the Local Government Finance Settlement in February 2016, and the March 2016 Budget added some detail to the proposals and made changes to business rates which will impact on the future scheme. In summary:

    - Current spending plans include £2.3 billion of RSG in 2019/20; this will be replaced by retained business rates by 2020.
    - Services identified as possible candidates for transfer to local funding included support for people currently receiving Attendance Allowance, the administration of Housing Benefit for pensioners and TfL's capital grants. The transfer of TfL capital grant of approximately £1 billion p.a. from April 2017 was subsequently confirmed in the March Budget.
    - The introduction of 100 per cent retention will be underpinned by a review of needs assessment – which will be required to support future "top up" and "tariff" arrangements to balance councils' resources and relative need to spend.
    - The temporary relief for small businesses was made permanent and the thresholds at which businesses become liable for the tax were increased; the combined effect of these changes will be to reduce the overall taxbase by about £1.5 billion by 2019-20. This will reduce the level of additional responsibilities that can be transferred to local government and funded from retained rates; in the meantime the Government will compensate councils for the loss of income within the current system.
    - From 2020 the rate at which business rates increase will be changed from the Retail Price Index (RPI) to the – generally lower – Consumer Price Index (CPI). As a result the resources available to local government (before taking account of any

[1] https://www.gov.uk/government/news/chancellor-unveils-devolution-revolution

growth or decline in the economy and the business rate tax base) will grow more slowly than would otherwise have been the case. Based on the OBR's current projections for the difference between RPI and CPI in 2020-21, we estimate that by 2040 business rates could be around £9 billion a year lower than they would otherwise have been – a cumulative loss of nearly £80 billion over twenty years.

3. The March 2016 Budget also announced the Government's desire to "explore with London [along with Greater Manchester and Liverpool] options for moving to 100% business rates retention ahead of the full roll out of the business rates reforms."

Context – the current business rates retention system

4. Introduced in 2013-14, the current business rates retention system sees 50 per cent of business rates collected by boroughs pooled centrally by government and used to fund Revenue Support Grant (RSG) and other specific grants. In London, the remaining 50 per cent is split between the GLA (20 per cent) and local billing authorities (30 per cent). A system of equalisation sees 25 boroughs receiving a top up from, and 8 paying a tariff to, central government, in order that boroughs receive an amount assessed by government as meeting their needs (the funding baseline).

5. Any business rates growth above the expected baselines is split between central government, the GLA and the local authority in proportion to these shares, with tariff authorities paying an additional levy to government, capped at 50p in the pound. For authorities that do not achieve the baseline target there is a safety net, which means that an authority cannot lose more than 7.5 per cent of its funding baseline in any one year.

6. London boroughs currently collect £6.6 billion p.a. in rates, with the GLA retaining £1.3 billion and boroughs collectively retaining £2.0 billion prior to top-up and tariff adjustments. However, a number of limitations with the current system, notably the negative impact of business rates appeals, mean boroughs may not achieve these targets in full. London Councils has consistently argued that the current retention scheme fails to sufficiently incentivise growth: this is confirmed by the lack of substantial growth in overall retained rate income across London, and the lack of correlation between growth and rates retained by individual boroughs, since the introduction of the system.

7. Under the current arrangements, the relative needs and resources of the boroughs are broadly balanced: their top-ups and tariffs net out to a small aggregate top-up of £13 million. In addition the GLA pays a tariff of £358 million. As a result, the combined London tariff

results in just over 10 per cent of London's "retained" rates flowing out of the capital to support the rest of England, leaving approximately £3 billion to support London's services.

8. However, the revaluation of business rates planned to take effect from April 2017, will significantly alter this picture. Although there will be some differences between boroughs and between commercial sectors, the GLA currently estimates that the revaluation could increase the business rates payable in London by up to £1 billion. Under the current system the overall national take from business rates will not be affected by the revaluation – a relative increase in London values will lead to a corresponding reduction in rates elsewhere in the country, leading in turn to an increase in London's tariffs, and a greater proportion of London's rates "topping up" spend elsewhere. Without corresponding changes in the accountability for, and management of, business rates, this change could generate considerable concerns for the relationship between London's government and its business ratepayers.

The process of reform

9. The Department for Communities and Local Government and the Local Government Association have established a joint Steering Group to develop proposals for consultation and implementation. The Steering Group is supported by four Working Groups focussing on:
    - Needs and redistribution
    - System Design
    - Additional responsibilities
    - Accounting and Accountability

    The groups are jointly chaired by CLG and the LGA, and the papers published on the LGA website[2]. London Councils, the Society of London Treasurers and the GLA are represented and actively involved in the work of each group.

10. The Government intends to consult in July 2016 on the issues that will require legislative change (largely the technicalities of the business rate system) and on priorities for the transfer of responsibilities (which may require legislation where statutory duties are devolved). Work on the needs and redistribution model is expected to take longer, with substantive consultation in Summer 2018, leading to overall implementation of a 100 per cent scheme in 2019-20.

11. Leaders' previously expressed ambition for reform (see paragraph 13 below) incorporates substantial elements of devolved control over the setting, collection and distribution of

[2] http://www.local.gov.uk/business-rates

business rates. We have been working on the assumption that we would need to set out a collective outline proposition for London devolution to Government in advance of this summer's consultation in order to ensure that the consultation can reflect – or at least not preclude – London's proposals.

12. As noted above, the Government is also keen to explore ways to pilot the introduction of the scheme ahead of full roll-out. Such pilots could not realistically include substantial devolution of control that required legislative change. However, we will review the work undertaken so far, and the design principles set out in in this report, to assess the potential for early implementation of parts of the system.

London Councils' ambitions for reform

13. At its meeting on 8 December 2015, Leaders Committee considered a report setting out the Government's announcements to that point, the way the current 50% retention scheme works, and a set of issues to be taken into account in developing a proposition for a devolved business rates scheme for London. In summary, Leaders endorsed four overarching ambitions for the proposed reforms, stating that rates retention and the transfer of responsibilities should:

    - Be contingent on improvements to the business rates system
    - Support London's ambitions for devolution and public service reform
    - Support the devolved governance of London
    - Be the start, not the end, of fiscal devolution

14. Leaders further agreed to establish a small working group, chaired by Mayor Jules Pipe, to oversee and provide political direction to the work of developing proposals and seeking joint agreement with the Mayor of London. The group includes Councillors Kober, Perry, O'Neill, Roe and Dombey; it has met three times, supported by an officer group with input from Chief Executives, Treasurers and the GLA. The group's terms of reference are attached as Appendix 1.

15. Discussions with CLG civil servants indicated that the Government would be keen to consider a proposal for a regional approach to devolving business rates to London. This was confirmed by the Secretary of State for Communities and Local Government, Greg Clark, in a meeting with Mayor Pipe and Cllr O'Neill in January 2016.

16. The former Mayor of London confirmed the GLA's commitment to joint work on a collective proposition for London at a meeting of the Congress Executive on 1 March. GLA officials have signalled to the new Mayor the need for early consideration of an outline proposal if a preliminary submission is to be made ahead of the consultation timetable.

17. The Leaders' working group has considered both the overall rationale for seeking a collective devolution deal for London, and each of the key issues that would need to be addressed to design and manage a system that could achieve London's ambitions. Emerging ideas and proposals have been widely discussed with Chief Executives, Treasurers and GLA officials. Group Leaders have also shared the draft paper on an informal basis in recent weeks.

18. The Government's ambition is to increase growth by incentivising local authorities. London's continued economic growth is vital to the country as a whole, but needs to be managed. Devolving business rates will help build and underpin a collective, London-wide approach to incentivise, prioritise and manage both the infrastructure investment and the public services London needs to continue its contribution to the public life and economic success of London and the UK.

19. London's population will continue to grow rapidly – and much more rapidly than that of the rest of the country. This brings opportunities and challenges not only in the successful management of the capital's economic growth, but also in securing a sustainable financial future for its public services. In considering the future assessment of relative needs and the package of services to be devolved, it will be essential that a devolved arrangement for London secures genuinely devolved control over a level of resources sufficient to manage the financial risks involved.

20. A set of principles that could govern the design of a devolved London system and its governance is set out in Appendix 2. Subject to Leaders' consideration and endorsement of this statement of principles, the next steps required will be:

    - For the Chair to seek agreement of the Mayor of London for a joint submission of the statement to Government as soon as practicable. If necessary, any significant amendments could be considered by elected officers via the urgency procedure.
    - For officers to explore with CLG officials aspects of the proposals that could be implemented in advance of the wider rollout of business rate retention. Any such pilot proposals would be reported back for consideration by Leaders at a future meeting.

Recommendations

21. Leaders are asked consider the report and to:

(1) amend and endorse as appropriate the ‘statement of principles’ for business rate devolution in London, as set out in Appendix 2
(2) seek agreement with the Mayor of London to submit the statement of principles jointly by the end of June, and to delegate final approval of any significant amendments required elected officers via the urgency procedure
(3) note that there will be ongoing discussions to explore with Government the early introduction of elements of business rate devolution in a London ‘pilot’.

Financial Implications for London Councils
None

Legal Implications for London Councils
None

Equalities Implications for London Councils
None

APPENDIX 1

Devolution of Business Rates Working Group

Terms of Reference

1. Context

Leaders Committee on 8 December 2015 considered a report on the issues raised by the Government's proposal to devolve 100% of business rates to local government by 2020. The proposed reforms raise a wide range of complex policy and technical challenges. In order to guide London Councils' work and lobbying, Leaders' Committee endorsed the overarching ambitions that rates retention and the transfer of responsibilities should:

- Be contingent on improvements to the business rates system
- Support London's ambitions for devolution and public service reform
- Support the devolved governance of London Councils
- Be the start, not the end, of fiscal devolution.

Leaders also agreed that London Councils Chair (and Finance Portfolio Holder) Mayor Jules Pipe convene a small group of Leaders, supported by London Councils officials, Borough Chief Executives and Finance Directors, to oversee and provide political direction to this work, and to seek joint agreement with the Mayor of London where appropriate.

2. Membership

Elected members:

Mayor Jules Pipe (Chair)	Hackney	Lab
Cllr Claire Kober	Haringey	Lab
Cllr Dave Perry	Harrow	Lab
Cllr Teresa O'Neill	Bexley	Con
Cllr Philippa Roe	Westminster	Con
Cllr Ruth Dombey	Sutton	LD

Borough Officers:

Chris Naylor	Chief Executive, CELC Finance Lead	Barking and Dagenham
Nicholas Holgate	Town Clerk	Kensington and Chelsea
Alison Griffin	Director of Finance	Bexley
Leigh Whitehouse	Director of Finance	Kingston-upon-Thames
Duncan Whitfield	Strategic Director of Finance and Governance	Southwark

The group will be supported by London Councils staff.

3. Frequency of meetings

To be determined. The group will hold an initial meeting early in 2016. Thereafter, meetings will need to be arranged to support London Council's effective contribution to the Government's implementation working groups and consultation processes.

4. Role

The working group is not a decision-making body. Its role is to provide a senior forum for discussion and for political direction to the development, promotion and communication of proposals to achieve Leaders' four overarching ambitions set out in section 1. It will be supported in this role by senior officers from London Councils and the GLA.

Specifically, the working group will:

- Consider and prioritise practical proposals for reforming the business rate system in London. Reforms might include, but not be limited to:
    - The valuation and appeal system
    - Changing the basis of taxation to reflect the value of business activity, not just physical business premises
    - Devolved responsibility for setting the rate multiplier
    - Revision of funding baselines to reflect changes in population-driven demand for services
    - The approach to, and frequency of, revaluations and resets
    - A review of the definition and role of the Central List
    - Flexibility to amend mandatory reliefs

- Develop lobbying positions for the additional services to be transferred to London Government and funded by retained business rates. Such transfers should:
    - Promote the service devolution and reform ambitions set out in the *London Proposition*
    - Be accompanied by a real transfer of control, influence and accountability
    - Promote transparency in the funding of local public services

- Consider proposals and develop lobbying positions in conjunction with the Mayor of London for devolved control and allocation of fully-retained business rates within London. Such regional governance should seek to:
    - Manage the risk of income reductions
    - Maximise the incentives for growth
    - Invest some of the proceeds of growth in solving the problems and ensuring the sustainability of the capital as a whole
    - Ensure an appropriate distribution of resources between all parts of London Government

- Consider London's appetite for, and opportunities to promote, further fiscal devolution, in order to secure control by London Government of a greater proportion of the resources it needs, through a wider variety of sources.

The group will report periodically to Leaders' Committee and the Executive Committee in order to update all Leaders on progress, secure broader input into the debate and to seek approval for emerging proposals where appropriate.

APPENDIX 2:

Devolving Business Rates to London: Principles

1 Context

Councils in England will collect around £26 billion of business rates by 2020, exceeding the Government's current funding plans for local government by around £11bn. The Government intends to allow local government as a whole to retain the rates, and to maintain “fiscal neutrality” by phasing out Revenue Support Grant and transferring additional responsibilities to local councils to match the resources available. The 2016 Budget indicated that reform of business rate retention will begin in April 2017 with the GLA retaining additional rates of around £1bn to fund TfL capital grants, and the commitment to “explore with London [along with Greater Manchester and Liverpool combined authorities] options for moving to 100% business rates retention ahead of the full roll-out of the business rate reforms.”

London government has long held the view that it should be granted control of a wide range of local taxes, including business rates – a view expressed, for example, in the London Finance Commission report of 2013. London’s continued economic growth is vital to the country as a whole; maintaining that growth – and managing a rapid increase in population – will be a huge challenge. Devolving business rates (and other revenue streams) will help build a joint, city-wide approach that can incentivise, prioritise and manage the public services and the infrastructure investment London needs to continue its contribution to the public life and economic success of the UK.

London’s population will continue to grow rapidly – and much more rapidly than that of the rest of the country. This brings opportunities and challenges not only in the successful management of the capital’s economic growth, but also in securing a sustainable financial future for its public services. In considering the future assessment of relative needs and the services to be transferred, it will be essential that any London deal secures genuinely devolved control over a level of resources sufficient to manage the financial risks involved.

It is clear that fundamental change in the business rate system will now happen: the way the system operates, the way the income is distributed between councils and the services it funds will all change. The Government intends to begin formal consultation in July. In order to inform that consultation and to respond to the opportunity of a “London pilot”, it is therefore imperative that London government agrees a set of principles that would inform the design of each of the key elements of a devolved retained business rate system for the capital.

We expect to work with Government and the other pilot areas to translate these principles into a fully operational scheme and, in doing so, to help inform the development of business rate retention for the country as a whole.

2 “100% retention”

Nobody is proposing that each individual authority keeps all of the rates it collects irrespective of spending need. Some form of “tariff and top-up” scheme will continue to equalise needs and resources. However, it is not essential to manage that equalisation at a national level: the “fiscal neutrality” principle of matching additional responsibilities to the available resources allows for different approaches in different parts of the country, which would be consistent with the recommendations of the London Finance Commission and in line with local and central government’s broader devolution ambitions.

London currently collects £6.6 billion in rates, of which it retains in principle 50%. The needs and resources of the boroughs and the City are broadly balanced: their top-ups and tariffs net out to a small aggregate top-up of £13 million. This reflects the wide disparity of circumstances across the capital. In addition, the GLA pays a tariff of £358 million. As a result, the combined London tariff results in just over 10% of London’s “retained” rates flowing out of the capital to support the rest of England, leaving approximately £3 billion to support London's services.

In future it would be equally possible to design systems in which either London achieves devolved control of business rates whilst continuing to contribute some proportion of those rates to a national system, or where London fully retains 100% of the rates it collects, but where further responsibilities – and therefore spending need – would also be transferred. This would not result in London having extra money to spend on the same services being delivered elsewhere, but in London being required to deliver additional services that are currently funded through other means.

At this stage, London wishes to explore options that could either fully retain the rates collected or continue to contribute some level of resources to the rest of England.

3 The borough/GLA split

In principle the allocation of resources should follow the responsibilities to be funded. ***The future split of rate income between the Boroughs and the GLA should as a starting point reflect the agreed package of responsibilities undertaken by each***. Future revision of that split should be periodically agreed and managed by London government, in line with changes in responsibility over time and any "resets" of the system (see section 6).

However, there may also be an argument – as with council tax – for the Mayor to set a proportion of the rate on a London wide basis, with boroughs setting the largest component. Under such an arrangement, the Mayor might also be able to offer discounts or reliefs on his/her proportion in addition to existing powers which allow the GLA to fund local discounts.

London would want to explore the relative advantages and disadvantages of options for either a defined, periodically-reviewed split of income between the boroughs and the GLA, or for the establishing a separate Mayoral rate. The choice between such approaches should, ultimately, be a matter for London government.

4 Setting business rates

The Government has indicated that it wants councils to have the power to *lower* business rates in their area, and for elected city-wide/combined authority Mayors to be able to raise an additional 2p with the support of businesses through the LEP.

London's rate list is different from the rest of the country: it currently accounts for 28% of the national total Rateable Value, but only 16% of the properties. This implies, on average, relatively fewer, larger businesses, which in turn increases the impact of the key risks of appeals, closure and redevelopment within the current system. The make-up of the list is also very different. 45% of London's list by value is office accommodation; only 9% is industrial: for the rest of the country the figures are 15% offices and 27% industrial. At the same time, the picture is very variable *within* London. Three boroughs (Westminster, Camden and Tower Hamlets) and the City account for 50% of the London total; in Lewisham around three-quarters of all premises are below the small business threshold, and, following the 2016 Budget, will no longer pay any business rates at all.

This distinctive pattern underlines the need for a distinctive, devolved approach for London. For the pilot, London is not seeking the further power to *increase* headline rates (other than the future Mayoral supplement which, we would argue, should be in addition to that already agreed to fund Crossrail until at least 2032 in order to support investment in other potential transport and infrastructure projects.) Following successful implementation of a London scheme, however, we would want to return to the issues of full control of rate setting – including the safeguards that would be required to prevent a disproportionate tax burden on business – along with a broader range of fiscal devolution as envisaged by the London Finance Commission.

In order to improve the effectiveness of business rates as a tool in managing economic growth and development, ***London would seek control of other key elements of the way the tax operates, including setting future tax liability thresholds, discounts and reliefs.***

5 Revaluation

Business premises will be revalued with effect from April 2017, which is likely to lead to an overall increase in business rates in London. Rating agents' forecasts have suggested that underlying business rates liabilities for London ratepayers in 2017-18 could increase by up to £1.1 billion compared to 2016-17, due to the combined effect of the revaluation and the RPI uplift in the multiplier. Significant variations are expected however across London, with some sectors/boroughs seeing large increases and others reductions – so the impact will not be uniform.

Under the current system, this would lead to a corresponding reduction in business rates payable elsewhere in the country. When business rates were only used to fund local government indirectly, the distributional effect of revaluations had no impact on councils. Under a national retention system, however, a relative increase in London rates would lead to an increase in London's aggregate tariff and a corresponding reduction in the growth rewards and incentives available to the rest of the country. We believe this would distort and undermine the government's policy aim of using business rate retention to promote growth across the country as a whole.

It also limits the ability of London boroughs to benefit from the growth in rental values deriving in part from their investment in making their local areas more attractive as a business destination. This is because, while growth from net new floor space/developments is retained in full, the effect of rental growth at revaluations is not – even though the latter is likely to reflect increased profitability and therefore additional tax revenues for central government. In effect, the business rates tax take in London could increase by over £1 billion in April 2017 – without the GLA/Mayor and boroughs deriving any additional financial benefit (although they are likely to bear the brunt of any complaints from ratepayers).

GLA Economics has estimated that if current differential trends in rental value growth continue, then by 2040 over 60% of all business rates income will be generated in London – double the current rate – unless rates in the rest of the country are allowed to increase at a rate which reflects their own economic investment and growth.

As part of the pilot, ***we would therefore seek to manage future revaluations within London, and to "decouple" their impact from the national system*** in order to prevent the capital's robust property market from continuing to distort the operation of the national system.

6 Resets: balancing needs and resources

When the present 50% retention system was introduced it was envisaged that periodic "resets" would recalculate the business rate and funding baselines for each authority, reflecting business growth and changes in relative need during the previous period. It was acknowledged that this would limit the growth incentive by limiting the period in which councils could benefit from any given business development and might introduce perverse effects and incentives in relation to the timing of developments. However, it was considered preferable on balance to ensure that differences between councils' needs and resources did not become too great over time. However, in 2015, the Independent Commission on Local Government Finance concluded that the disparity of needs and resources was as great *within* sub-national regions as across the country[3], and that regional funding systems were therefore feasible without promoting inequality between them.

As with revaluations, ***we would seek to manage future resets of business rate and funding baselines, and their impact, within London***.

[3] See Financing English Devolution, page 26

Top-ups and tariffs are currently calculated by comparing the business rates a council is expected to collect (after deducting central and precepting authority shares) with its relative need to spend (expressed in its funding baseline). To underpin the new system the Government intends to review the way relative need is measured: it is anticipated that this work will take two years. London will contribute to the technical work required through its representatives on the joint CLG/LGA Steering Group and working groups.

It is possible that this national review could lead to significant changes in baseline funding allocations for London authorities, including the GLA, and we will need to present a robust case to ensure that key drivers of need in London are adequately represented in the national formula that emerges.

In particular, London's population continues to grow at a much faster rate than that of the rest of the country. Whilst this in part reflects the success of London's economy – and will help deliver its future growth – it also represents a huge challenge to the financial sustainability of London's public services. Both the overall quantum and the distribution of resources within London will need to be sufficient to manage the risks involved.

While we would not seek to invent a needs formula from scratch, London would wish to be able to vary it over time to reflect London's rapidly-changing circumstances, including significant issues such as housing need, population growth/churn and specific London cost pressures.

Changing needs assessments inevitably creates "winner and losers" and, depending on the scale of change, may require transitional arrangements to protect councils from too rapid a reduction of funds. In practice, however, such "damping" can undermine the incentive effects of retaining growth, particularly if that growth is top-sliced to fund the damping mechanism. There is no simple solution to this problem, but London has previously expressed a clear ambition to take responsibility for itself for balancing competing priorities within a devolved system.

Translating a relative needs formula into a funding baseline against which business rate baselines can be compared should also take account of the availability of council tax for each authority. In the long run, we would seek the power to amend the way council tax operates within London, where a banding system based on 1991 valuations is no longer fit for purpose, and creates significant distortions and perverse outcomes.

In the short term, however, we recognise the need to incorporate the existing council tax base into the calculation of business rate redistribution within a devolved London scheme.

London therefore seeks the ability to determine and periodically reset funding baselines for its authorities, taking into account the overall balance between spending need, council tax base, the speed of change and the desire to maintain incentives within a devolved system.

7 Additional responsibilities

Fiscal neutrality requires the transfer of responsibilities to match the increased resources to be retained by local government. The Government has already announced that the GLA will retain additional business rates to fund TfL's core capital investment grants – estimated at £960 million in 2017-18. Other grants and services that could be funded directly from rates in future have also been explicitly mentioned, including Attendance Allowance, Public Health, and Housing Benefit administration. A variety of other grants and services is currently being considered by civil servants and by the working group: it is clear that there will not be enough money in the system to fund everything that has already been explicitly or informally floated.

It is also important to recognise that the current system does not fully fund all of the responsibilities which local authorities have been required to fulfil. London faces particular pressure, for example, from the costs of homelessness and supporting those with No Recourse to Public Funds. In finalising the package of additional responsibilities at national level, and in any devolved regional settlement, the government must give due consideration to the future impact of these unfunded burdens.

In advance of the 2017 revaluation, however, and of agreement to the proportion of rates to be retained within London, it is not possible to quantify precisely the resources available to fund any package of additional responsibilities for London. As a principle, ***London will seek to prioritise the transfer of responsibilities that maximise its ability to improve the life of Londoners, the effectiveness and efficiency of its public services, and the future economic success of the capital***.

This will include responsibilities that:

- have a direct relationship to business (such as skills and employment support);
- support our existing proposals for devolution and public sector reform (including health and social care integration, skills, employment and crime); and
- help tackle key infrastructure challenges, including housing and transport.

It would not be appropriate or acceptable to transfer the risk of future spending commitments that London government is unable effectively to influence. ***Any transfer of responsibility must therefore be based on a realistic assessment of its in-built spending pressures and be accompanied by a corresponding devolution of policy control***.

In support of its broader ambitions for devolution and public service reform, London would also wish to continue exploring approaches that transferred service responsibilities – and appropriate revenue sources – above and beyond those that could be financed entirely by retained business rates.

8 Distributing the benefits of growth

Under the current 50% retention system, boroughs in theory benefit from 30% of growth in rates in their area above the assumed baseline: 20% goes to the GLA and 50% to Government. In practice, the impact of appeals and the timing of the initial baseline calculations have meant that there has to date been no real correlation between boroughs' economic growth and retained business rate income.

These problems should as far as possible be designed out of the system in the transition from 50% to 100% retention. In the longer run, the retention and distribution system must be capable of delivering greater and more certain rewards if it is genuinely to incentivise growth.

However, London's economy is a complicated system in which different parts of the capital will have different, but inter-related, roles to play. For the economy to keep growing in a sustainable manner, we need to expand the overall business premises capacity, but also to find ways to house, train, transport and provide access to leisure and culture for millions of people around the capital. We may therefore want to use some of the proceeds of growth to facilitate additional investment, and to create targeted rewards that incentivise contributions to the capital's overall success beyond hosting new business properties. The design of these rewards and incentives should be integrated with that of setting funding baselines.

London would therefore wish to devise its own distribution scheme to reward the boroughs' and the GLA's contributions to London's overall growth, and to facilitate investment.

9 Managing risk – safety nets and the central list

Tax bases can fall as well as rise. At present a "safety net", funded by a levy on growth for tariff authorities, protects councils against a fall of more than 7.5% of their retained rates. The Government has indicated it does not expect to operate a levy in the new system.

The "Central List" includes transport, communications and utilities infrastructure properties not currently allocated to individual authorities. It will account for about £1.4 billion of rates by 2019/20. This could in future be used in part to fund a range of risk management issues, including a safety net, the impact of appeals and civil emergency funding.

Each of these ideas has merit, but all would be dependent on far greater clarity about the composition of the list, accountability for changes, both within the list and between the central and local lists, and use of the overall rates collected.

For example, the central list currently includes a large proportion of Transport for London's network and rail infrastructure, including the London Underground, DLR and TfL station carparks, which might logically be transferred to the local rating list, so that London retains the full benefits of the investment it makes to improve the capital's transport infrastructure. ***We would support transferring all of Transport for London's assessments on the central list to the local rating list in London.***

However, depending on the approach to "100% retention" there may also be a case for broader transfer of properties. Under a fully-devolved approach, which would see London's financial risk as well as potential reward maximised, we would expect to see most if not all of the central list that relates to properties within London transferred to the local list.

London's future approach to managing risk should not be separated from the questions of the overall proportion of rates retained (see section 2) or the degree of devolved control over the business rate taxbase (sections 4-6). ***In essence, the greater the degree of autonomy, the more reasonable it will be to expect London to manage its collective risk for itself. Conversely, the more London remains part of a national system, and the more limited its control of the taxbase, the more London should expect to look to Government to share some of that risk.***

10 Governance

A regional approach to managing business rates in London will require appropriate mechanisms to ensure that robust, timely and accountable decisions can be taken to raise and distribute tax revenues. The London Finance Commission identified a set of principles upon which such governance could be based. These were expanded in evidence submitted to the CLG Committee inquiry into fiscal devolution in April 2014 (and included as an annex to this note).

London government will collectively build on those principles to define and establish appropriate arrangements to manage devolved business rates.

Annex:

Governance Principles

Extract from a joint letter from Boris Johnson, Mayor of London and Mayor Jules Pipe, Chair of London Councils to Clive Betts MP, Chair of the Communities and Local Government Committee, 10 April 2014, submitted as evidence to the Committee's review of Fiscal Devolution:

Following careful consideration, London government is already agreed on the following set [of principles] that reflects and builds on those set out in the [London Finance Commission] report:

1. **Each element of London government should have a stake:** Elected leaders of all London local authorities and the Mayor of London must be able to feel confident about the governance arrangements for the new finance system
2. **No exclusion:** No one borough or group of boroughs can be excluded from the benefits of London's success or become disempowered from addressing local needs.
3. **No over-riding:** Interests of the Mayor cannot be overridden by the boroughs or vice versa.
4. **No deadlock:** Arrangements must prevent or break deadlock. We believe that this can be achieved through suitable voting arrangements and clarity about which tier of government is responsible for decision-making, as reflected in the principles below.
5. **Enforcement:** The system must enforce binding decisions and these decisions must reflect a clear initial consensus – even if there are disagreements from time to time about individual decisions.
6. **Simplicity and clarity:** The reformed system should be as simple as possible. It should avoid the need for annual decision-making between different sections of London government. It should seek to distinguish clearly the responsibilities of the GLA, Boroughs and London Assembly.
7. **Stability…** Existing responsibilities should be maintained where possible.
8. **… But potential for reform.** Provisions in the 'devolution settlement' should enable, by agreement, periodic property tax reform and changes to any within-London distribution arrangements. Such reforms would be distinct from the 'Day 1' operation of a devolved system. There should also be a presumption that the more significant reforms were proposed, the longer they would be phased in.
9. **Practical operations:** decisions would be taken by the Mayor or Borough politicians as appropriate. However, a joint GLA and London Councils Officer Group would provide standing technical advice and support for politicians to decide matters where there is significant joint interest under the above arrangements. This might be independently chaired.
10. **Decision rules:** Any new system would require a set of decision rules, some of which would be reflected in legislation. For instance, Parliament might legislate for periodic property revaluations to be carried out by devolved authorities. There are various options for the rulebook governing changes within London following devolution but here is one example:
    - Mayor would need to agree any decision and by converse would have a veto
    - Boroughs would need to agree to any decision by their own rules (e.g. two-thirds majority)
    - The London Assembly would retain its existing powers to amend or reject the Mayor's tax and spending decisions, which would be enhanced commensurate with the increase in the Mayor's powers.