LONDON COUNCILS

# Leaders' Committee

## Local Government Finance - update Item 6


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**Summary** This report updates Leaders' Committee on the latest funding announcements related to Covid-19 and the estimated financial impact of the virus on London local government. It also provides an update on lobbying ahead of the Comprehensive Spending Review (CSR) and the fundamental review of business rates due to conclude in the autumn and seeks agreement in principle to continue the London business rates pool in 2021-22 ahead of the Government's deadline of 23rd October.


**Recommendations** Leaders' Committee is asked to:

- note the latest government funding announcements and estimated financial impact of Covid-19 on London local government;
- note the lobbying activity with regard to the CSR and the Fundamental Review of Business Rates; and
- agree in principle to continue the pan-London business rates pool on the same basis as currently in 2021-22.

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**Local Government Finance update**

## Introduction

1. London boroughs continue to play a central role in the response to both the public health and economic crises caused by COVID-19. Both have resulted in additional expenditure and significant income losses for local authorities, while presenting challenges and opportunities for the future economic and social role of London Government.

2. Government funding has not been sufficient to cover the financial impact since March and will fall significantly short of the estimated impact over the full financial year without further investment. This, together with ongoing uncertainty regarding future funding, is severely testing boroughs' financial resilience.

3. The Comprehensive Spending Review (CSR), due in the autumn, was already going to be a pivotal point for local government finance after a decade that saw budgets fall by over a quarter and London's population grow by almost a million people. It now takes on even greater importance for the financial sustainability of London local government within the broader national context of economic recession and the need to repair the public finances.

4. At the same time the Government is also undertaking a fundamental review of business rates: one of the cornerstones of local government funding, with the second deadline for its call for evidence on the subject of 31st October, and a final outcome due in the spring. The review partly focusses on alternative taxes that may partially replace business rates, were they to be cut substantially, which raises questions about who controls such taxes and the possibility of fiscal devolution to London local government.

5. The London business rates pool has provided an initial platform for developing strategic joint governance between the Mayor and Leaders, as well as delivering financial returns for London Government since it was established in 2018-19, and is expected to continue to be beneficial in the current year, despite the impact of Covid-19.

6. This report, therefore, updates Leaders' Committee on the latest funding announcements related to Covid-19 and its estimated financial impact on London local government, provides an update on lobbying ahead of the CSR and HM Treasury's review of business rates and seeks agreement in principle to continue the London business rates pool in 2021-22.

**COVID-19 funding and financial impact on London local government**

Recent funding announcements

7. Following the detailed update to Leaders' Committee in June, Appendix A provides an updated list of all funding measures announced since the start of the pandemic, and London boroughs' share of each one. Overall, they have received around 16% of all direct funding: broadly in line with London's share of the national population. Since June, there have been some further important funding announcements.

8. In July, London boroughs received £87 million (18%) of the **third tranche of emergency funding totalling £500 million**, when it was also confirmed that the recovery of council tax and business rates Collection Fund deficits could be phased over the next 3 years rather than addressed within a single year. The decision on how much – if any - compensation will be provided for tax losses was postponed until the CSR. A **compensation scheme for lost sales, fees and charges (SF&C)** income was also announced, with local authorities forgoing the first 5% of affected budgeted SF&C income, and government compensating authorities for 75p in every pound of losses thereafter. The first data collection and payments (for the period April to July 2020) are due in early October. Section 151 officers are responsible for self-certifying the accuracy and reasonableness of claims. Initial estimates suggest it may only cover around half of the estimated lost SF&C income. A verbal update will be provided to Leaders' Committee, by which time the first payments are due to have been made.

9. On 9th September, a **Local Restrictions Support Grant (LRSG)** was announced for businesses required to close due to local Covid-19 lockdown restrictions, with large businesses (with a rateable value over £51,000) able to claim grants up to

£1,500 every three weeks and smaller businesses (RV under £51,000) receiving £1,000. Payments are triggered by a national decision to close businesses in a high incidence area and made for a 3-week lockdown period. Local authorities will also receive an additional 5% top up amount of business support funding to enable them to help other businesses affected by closures. Final guidance was published on 24th September[1].

10. On 17th September, a second round of **Infection Control funding**, totalling £546 million nationally, was announced. Although allocations have not yet been confirmed, if distributed on the same basis as the first ICF (worth £600 million), it is estimated London boroughs would receive £46 million to continue supporting care providers.

11. On the same day, the **Next Steps Accommodation Programme** allocations were confirmed, totalling £92 million nationally, to support local authorities in preventing those who were sleeping rough or at risk of sleeping rough during the pandemic form returning to the streets, following the 'Everyone In' initiative. Overall London will receive 43% of the national total, with boroughs receiving £23 million and the GLA £19 million.

12. Finally, the Secretary of State for Health and Social Care wrote to all council Leaders on 20th September setting out details of a new **Test and Trace Support Payment scheme** in which people on low incomes who are unable to work while they are self-isolating because they cannot work from home will be entitled to £500. Local authorities will administer the scheme to be implemented by 12th October at the latest.

The August MHCLG survey

13. MHCLG continues to undertake monthly surveys to gauge the scale of the financial impact of Covid-19 on local authorities. A verbal update will be provided on the September survey, which had not been completed at the time of drafting. The fifth survey, undertaken in August, indicated the total impact across London

[1] https://www.gov.uk/government/publications/coronavirus-covid-19-local-restrictions-support-grant-guidance-for-local-authorities

boroughs in 2020-21 was forecast to be **£2 billion**, comprising **£1.1 billion in lost income** and **£923 million in increased expenditure** (broadly the same levels as the July survey). Taking account of the **£587 million in emergency funding** that boroughs have received so far, the funding gap in 2020-21 was estimated to be **£1.4 billion** across London. Table 1 (below) shows the detailed breakdown of the latest estimated impact in 2020-21.

14. Almost a third (£289 million) of additional expenditure has been within Adult Social Care, with unachieved savings accounting for £151 million, and increased homelessness and rough sleeping costs accounting for almost £100 million. Spending is also estimated to increase by around £60 million in each of the following services: finance & corporate and environment & regulatory service; and around £40 million in public health; children's social care; and cultural services.

**Table 1 – C19 financial impact on London boroughs 2020-21 - August 2020**

| | £m |
|---|---:|
| Additional expenditure - ASC | 289 |
| Additional expenditure - Unachieved savings | 151 |
| Additional expenditure - All other | 483 |
| **TOTAL ESTIMATED ADDITIONAL SPENDING** | **923** |
| Reduced income - Sales, fees and charges | 451 |
| Reduced income - Council Tax (local share) | 248 |
| Reduced income - NNDR losses other (local share) | 213 |
| Reduced income - HRA | 80 |
| Reduced income - Commercial Income | 56 |
| Reduced income - Other | 46 |
| **TOTAL ESTIMATED INCOME LOSS** | **1,093** |
| **TOTAL ESTIMATED FINANCIAL IMPACT** | **2,016** |
| Emergency funding received so far | -587 |
| **FUNDING GAP** | **1,429** |

15. With regard to income, only around half of the £451 million SF&C losses is expected to be covered by the compensation scheme. With the extent of compensation for lost tax income (totalling £461 million) not known until the CSR, and no indication of compensation for lost HRA, commercial or other income (totalling £182 million), there is significant uncertainty over how much of the financial impact of COVID-19 boroughs will ultimately have to bear. This makes the outlook ahead of the CSR extremely challenging.

**Comprehensive Spending Review 2020**

16. Despite the Budget, previously planned for the autumn, having been cancelled by the Chancellor shortly before the announcement of the Government's Winter Economic Plan on 24th September, the current intention remains for the Government to deliver the CSR this autumn. However, the likelihood of it being scaled back to cover just one year, rather than the planned 3 years, is increasing given the economic uncertainty facing the country. The 24th September deadline for representations suggests the review is likely to conclude in November, based on past experience.

17. London Councils made a detailed representation, accompanied by a short two-page summary (included at Appendix B) under the assumption of a three-year CSR. The key priority is for the Government to take immediate steps to address the short-term impact of Covid-19 on local government funding highlighting the £1.4 billion funding gap and mounting pressures caused by the potential second wave and, beyond that, for certainty over 2021-22 funding and sustained above-inflation investment in local government services over the three-year period. It called for the Government to provide long-term financial sustainability by delivering new sources of revenue and considering greater fiscal devolution and set out a series of detailed asks to support boroughs in delivering the economic and social recovery the country needs. In the event that the Spending Review covers only one year, the most urgent priorities – covering the costs of managing the pandemic and establishing certainty of adequate funding in 2021/22 as soon as possible, will remain essential.

<u>Lobbying</u>

18. With regard to lobbying the following activity has occurred so far:
    - A press release was published on 24th September
    - Associated social media coverage on London Councils' Twitter and LinkedIn accounts.
    - The submission has been shared with BBC London News and discussions with network programming on a set of issue-specific follow-ups.

- The two-page summary has been shared more widely with journalists, London MPs, business groups, voluntary sector organisations and other key stakeholders.
- Oral and written parliamentary questions on issues raised in London Councils' CSR submission were sent to London MPs ahead of October HCLG questions.
- A member briefing has been sent to all London councillors on 29th September.

19. Further lobbying activity is planned in the run up to the CSR including, but not limited to:
    - A template letter will be sent to Leaders in early October for them to write to their local MPs in the lead up to decisions being taken ahead of the CSR.
    - A detailed briefing will be provided for elected officers of the London APPG, who are due to meet the Minister for London, Paul Scully MP, on 14th October.
    - Further media stories focusing on a number of the specific issues within the submission are scheduled throughout October, for example retrofitting and the Green recovery and adult social care, with others to be confirmed.
    - Officers are meeting London business groups in early October to discuss alignment of lobbying messages and potential for joint lobbying in October.

20. The GLA also made a representation and the Mayor has written to the Chancellor outlining his priorities, with many areas in common with London Councils' submission. Officers are in discussion with GLA officers regarding joint lobbying on common priorities in the lead up to the CSR.

**Fundamental Review of Business Rates**

21. HM Treasury launched a fundamental Review of Business Rates at the Budget in March. Its objectives are to reduce the overall burden on businesses; improve the current business rates system; and consider more fundamental changes in the medium-to-long term. Its call for evidence focused on four main areas including:
    - improvements to the Transitional Relief Scheme from April 2021;

- reforms to make the system more sustainable including the basis and frequency of valuation, the effectiveness and operation of different reliefs, how the business rates multipliers should be set, and who pays the tax;
- the administration of the tax, covering the valuation and appeals process; and
- potential alternatives to business rates, particularly taxing land and property.

22. Responses were sought in two phases with views on the multiplier and reliefs sought by 18th September to inform an interim report in the autumn; and views on the remaining areas sought by 31st October. The review is due to conclude by spring 2021.

23. London Councils and the GLA submitted a joint response to the first deadline, which can be found at Appendix C. The response stressed that it is too early to tell what the long-term impact of coronavirus will be on the commercial property market and flagged the potentially far-reaching impact on businesses and property use in Central London and London's wider town centres. As such, it urged the Government to confirm its plans to support businesses in targeted sectors with rates bills beyond March as soon as possible. It also sets out the reforms London Government believes must be implemented once we emerge from the pandemic to help stabilise the economy and support future growth. These include solving the problems of complexity and the overconcentration of the tax on particular geographies and sectors, which largely result from the current, centrally prescribed system. It advocates greater local control over setting of the tax through devolving the multiplier to London Government, and argues that the suite of mandatory reliefs could be much better tailored and responsive to local economic need if devolved to local government.

24. The second response to the call for evidence will broadly put forward similar arguments regarding a more localised system, emphasising that – as the primary aim of the review is to reduce the tax burden on businesses – it will be essential that local authorities have access to replacement or additional taxes to ensure they are not worse off. More fundamentally, these new taxes should be designed

jointly with local government. It is likely to conclude that there is good evidence to support implementing online sales taxes, although ensuring local accountability over them is difficult. Subject to broader agreement with the GLA, it is likely to indicate there is less compelling evidence for a Capital Values Tax (the other tax mooted in the call for evidence). More widely, it will advocate for a principled approach, rather than focussing on the details of individual taxes at this stage, which should consider the broader issues of what local government is funded for and how best to achieve that through a varied basket of local-controlled revenue sources.

25. Officers are also working closely with London business groups to identify areas of common ground and whether there is scope for a high-level joint response to the 31st October deadline. London Councils' upcoming "Business 1000" survey will also be used to obtain supportive data that may reinforce the devolution arguments. As the review will report in the spring, it is further proposed to explore with the GLA the potential for commissioning further independent research regarding business rates reform, and the potential for other taxes to partially take its place. A final response will be prepared for authorisation by Group Leaders in the usual way.

**The London Business rates pool**

26. The Government has set a deadline of 23rd October for local authorities to confirm whether they wish existing business rates pools to continue in 2021-22 and, if not, for any expressions of interest to form new pools.

27. The pan-London business rates pool has been in existence since 2018-19, when it was established as a 100% retention pilot negotiated with Government, which delivered £397 million of net financial benefit (£216 million of which was retained directly by London boroughs and the City of London). In 2019-20, the pilot was scaled back to 75% retention, and the draft outturn (form August) estimated the net financial benefit to have been £212 million (with £115 million retained by London boroughs and the City of London).

28. Leaders and the Mayor agreed to continue pooling in 2020-21, following discussion at Leaders' Committee in October 2019, despite the pan-London pilot ending (i.e. under the underlying 67% scheme). The rationale being that:

- there would still be a modest financial benefit;
- there would continue to be operational and administrative benefits; and
- the key strategic benefits, which provided the original rationale for negotiating the pilot in 2018, would continue (pooling would continue to signal a small but important step towards London Government's long-term fiscal devolution ambitions, and potentially provide it with a more influential voice regarding the ongoing design of the final 75% scheme).

29. The forecast at the start of the current year was for a net financial benefit of around £36 million to be retained directly by the boroughs and the City (with the Mayor relinquishing the GLA's share of any benefit and the removal of the previously pooled Strategic Investment Pot). The latest in-year monitoring exercise, undertaken in August, suggests that, despite the impact of the pandemic, there will still be a net financial benefit from pooling in 2020-21, totalling approximately £30 million.

30. With regard to pooling in 2021-22, the operational and strategic rationale set out above still remains. Indeed, given the debate over alternative taxes and fiscal devolution within the fundamental review of business rates and potentially in light of the forthcoming Devolution White Paper, the strategic case is potentially even more important.

31. There are, however, a number of uncertainties for Leaders to consider with regard to the direct financial benefit and potential risks involved. These include, the ongoing negative impact of Covid-19 on business rates in the capital; the possibility that the Government my still implement a "reset" of baselines that had been indicated earlier in the year; and uncertainty regarding the continuation of the new reliefs and grant schemes that have supported businesses with their business rates bills in 2020-21.

32. At this stage, the Government has not confirmed whether it will continue with the planned reset of business rates baselines in 2021-22 – although it seems unlikely given the level of volatility this could cause and the current capacity of MHCLG to undertake the reset. Unless the Government confirms this in the CSR, it may not be known until the provisional settlement in December. With regard to whether the emergency reliefs and grant schemes will continue next year, as the autumn Budget has been cancelled and there was no mention in the Winter Economic Plan, this may not be known until the spring.

33. All that is currently known, is that despite the biggest economic slump on record, there is still a modest financial benefit to pooling in the current year. The principles of the pool ensure that no authority can be worse off than its "safety net" level i.e. 92.5% of Baseline Funding Level, and that, if there are enough resources in the pool to ensure no authority is worse off than they would have been individually, then this will be guaranteed. All boroughs are expected to be better off than they would have been had they not pooled in the current year, and there may be collective security from pooling risk in 2021-22 were the economic impact of Cobid-19 to worsen.

34. The 23rd October deadline is to give MHCLG enough time to prepare the provisional settlement in December. It is worth noting this is not the final deadline by which boroughs must decide whether to continue to pool. As with last year, each authority will have until 28 days after the provisional settlement (i.e. likely by mid-January) to decide formally whether it wishes to continue to pool, and each must agree that decision individually through local governance arrangements.

35. The Lead Authority is commissioning Local Government Futures, the pool sub-contractor, to undertake an assessment of the potential financial benefits and risks of pooling in 2021-22, which will be shared primarily with Section 151 officers, and could be further summarised and shared with Leaders in sufficient time to inform individual local decisions from December onwards.

36. GLA officials have indicated that the Mayor of London would continue to support the pan-London pool arrangement on the same basis as in 2021-22, subject to a formal decision. It is, therefore, recommended that Leaders agree to continue to

pool in 2021-22 in principle for the purposes of the initial MHCLG deadline, subject to a fuller assessment of financial risks and benefits from the Lead Authority, and any further clarity from government on the uncertainties set out above which may emerge between now and December in the CSR, provisional finance settlement or any other announcements.

**Recommendations**

37. Leaders' Committee is asked to:
    - note the latest government funding announcements and estimated financial impact of Covid-19 on London local government;
    - note the lobbying activity with regard to the CSR and the Fundamental Review of Business Rates; and
    - agree in principle to continue the pan-London business rates pool on the same basis as currently in 2021-22.

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**Financial Implications for London Councils**

None

**Legal Implications for London Councils**

None

**Equalities Implications for London Councils**

None

## Appendix A – All funding measures announced since the start of COVID-19

| | Date | London Boroughs (£m) | England (£m) | London % share of England |
|---|---|---|---|---|
| Rough Sleeping Fund | 16-Mar | 1 | 3 | 26.6% |
| Hardship Fund | 24-Mar | 90 | 500 | 17.9% |
| Emergency funding (tranche 1) | 27-Mar | 254 | 1,600 | 15.9% |
| S.31 grants paid in advance | TBC | 205 | 1,800 | 11.4% |
| Small Business Grants Fund (SBGF) and the Retail, Hospitality & Leisure Grants Fund (RHLGF)* | 01-Apr | 1,662 | 12,334 | 13.5% |
| Cashflow measures | 16-Apr | 871 | 3,333 | 26.1% |
| C-19 Business Rates reliefs | 22-Apr | 3,040 | 10,131 | 30.0% |
| Emergency funding (tranche 2) | 28-Apr | 245 | 1,594 | 15.4% |
| Infection control fund (tranche 1) | 15-May | 51 | 600 | 8.5% |
| Active Travel Fund** | 23-May | 25 | 222 | 11.3% |
| Reopening High Streets Safely | 24-May | 8 | 50 | 16.0% |
| Test and Trace | 10-Jun | 60 | 300 | 20.1% |
| Welfare support funding | 11-Jun | 10 | 63 | 16.1% |
| Emergency funding (tranche 3) | 11-Jul | 87 | 494 | 17.7% |
| Local Restrictions Support Grant | 24-Sep | TBC | TBC | TBC |
| Next Steps Accommodation Programme | 17-Sep | 23 | 92 | 25.1% |
| Infection control fund (tranche 2) | 17-Sep | 46*** | 546 | 8.5% |
| Test and Trace Support Payment scheme | 20-Sep | TBC | TBC | TBC |
| Sales, Fees & Charges scheme | Early Oct | TBC | TBC | TBC |

*A Local Authority Discretionary Fund was subsequently announced with a value of up to an additional 5% or £617m.
**Boroughs share a joint fund with TfL
***Estimate based on distribution of first ICF grant

# Comprehensive Spending Review 2020

## London Councils' Representation to Government

This Spending Review comes at a pivotal moment for the future of the country as it seeks to rebuild the economy and emerge stronger and more resilient from the global pandemic. It also comes at a time of huge financial risk for local government and its communities. Government is committed to "levelling up" inequalities of productivity, opportunity, wealth and income across the country: but those inequalities are as stark within regions as between them, between people as much as places. London Boroughs are determined to play their part in driving the social and economic recovery our country needs, but to do so they need both financial support and greater freedom to manoeuvre.

### Funding Local Government

Local government has been at the forefront of the response to Covid-19, demonstrating its vital role in the social and economic fabric of communities across the country; but the pandemic has put councils' immediate and long-term financial survival in doubt. While we welcome the emergency financial support so far provided, we now urge government to:

**Secure the immediate financial position** by fully compensating councils for the financial impact of the pandemic to date, including support for lost Council Tax and Business Rates. In London – even without a substantial second wave of the virus or local lockdowns, this will require an additional £1.4 billion; without certainty around this funding councils will have to make short term emergency spending cuts which will undermine longer-term recovery

**Create as much certainty as possible for the coming three years by:**

- *urgently announcing 2021/22 funding, grants and council tax principles;*
- *ensuring councils are adequately resourced to fulfil their new and existing roles and in managing the on-going pandemic and associated social distancing in future years*
- *helping London Boroughs close their £2 billion budget gap through annual above-inflation increases that also take account of underlying demand pressures in key services, including Adult and Children's Social Care (£430 million), Public Health (£130 million), Homelessness (£200 million), High Needs education funding (£100-200 million) and supporting people with No Recourse to Public Funds (£50 million).*

**Ensure long term financial sustainability** by engaging local government in debate to resolve key issues including service devolution, social care, business rates reform and new funding sources. We should aim to build a new settlement to underpin the long-term funding of local government, including new sources of revenue and greater fiscal devolution.

### Driving economic recovery

The immediate focus for the government at the CSR must be to deliver the national economic recovery from the consequences of the pandemic. This cannot happen without a strong recovery in London which, before the crisis, contributed 28 per cent of UK GVA, and a fiscal surplus of £39 billion. We set out an investment case for a combination of direct funding, access to project finance and greater operational flexibility to enable London to play its part. This includes asking government to:

**Take immediate steps to shore up London's economy, including:**

- *Support for business, workers and customers through a targeted extension of the schemes for rates reliefs and grants, job retention and customer confidence ("Eat Out to Help Out").*
- *Allocating UKSPF and allowing devolved areas collectively to determine how best to spend it.*
- *Extending the 'Reopening High Streets Safely Fund' to enable enhanced public realm management for councils, police, security staff, marshalls and trading standards.*

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**Equip boroughs to drive the green recovery by:**

- *Investing £350 million immediately to support the £950 million already committed by boroughs to 375 retrofitting projects in 2020/21 that will create more than 2,000 skilled green jobs,*
- *Build on this for the future through a £1 billion multi-year programme, a targeted PWLB rate and new financing mechanisms to retrofit all buildings – homes, commercial and industrial.*
- *Create a national £1.5 billion Clean Air Fund to enable cities to implement Clean Air Zones.*

**Boost housing delivery in London by allowing councils:**

- *Local flexibility to increase rents by up to CPI + 1 per cent, or more where they can demonstrate a positive correlation between additional house building and housing benefit reductions.*
- *Complete flexibility over the use of Right to Buy receipts.*

**Support longer term job creation and productivity by:**

- *Devolving skills and employment, as set out in the Skills for Londoners Call for Action.*
- *Devolving the Apprenticeship levy and setting up a London Apprenticeship Service.*

**Investing in London's strategic infrastructure and roads by:**

- *Funding the National Infrastructure Assessment, which would go a long way to promoting an increase in public transport and getting London back to work.*
- *Devolving VED to help fund much-needed investment in London's highways.*

## Supporting social recovery

There is no getting away from the scale of the challenge posed by the social impact of Covid-19. By 3 September, more than 40,000 people in London had contracted the disease and 8 of the 10 local authorities in England with the highest rates of excess deaths were in London. There is much government can do to support us to rebuild our communities and local services, including:

**Support for health & social care:**

- *Urgently providing a long-term sustainable plan for the funding of social care.*
- *Immediate funding to alleviate both the additional Covid-19 costs and the underlying £130 million shortfall from demographic pressures.*
- *Restoring Public Health Grant to 2015/16 levels in real terms and targeting it where it is most needed - £130 million.*
- *Medium-term funding allocations in adult social care and public health that mirror the NHS.*
- *Further health and care devolution in London over the CSR period, building on the unprecedented collaborative working seen during the pandemic.*

**Investing in children's services:**

- *£300 million to meet the annual shortfall in children's social care.*
- *Increased rates of Home Office grant for UASC and former UASC Care Leavers.*
- *Sufficient High Needs funding for authorities with deficits to deliver realistic recovery plans.*
- *Further support for schools to stay open safely, and a commitment not to reduce funding where school rolls fall temporarily as a result of Covid-19.*

**Tackling London's Homelessness crisis:**

- *Immediate funding to cover in-year the funding gap of £30 million caused by Covid-19.*
- *Long-term funding settlements to help us end street homelessness.*
- *Enable us to provide sufficient homes at social rent levels to prevent homelessness.*

**Supporting some of London's most vulnerable people:**

- *Suspend the NRPF condition for at least 12 months to enable households with No Recourse to Public Funds to access a wider range of benefits during the pandemic.*
- *Direct funding for people with NRPF after the pandemic.*

**This document is a summary. Further details and additional proposals are set out in our main submission**

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**Appendix C – NNDR review call for evidence – first submission**

**HM Treasury - Business Rates Review: Call for Evidence**

**A joint response by London Councils and the Greater London Authority**

**18th September 2020**

## Introduction

1. This is a joint response by "London Government" on behalf of London Councils (representing the 32 boroughs and the City of London) and the Greater London Authority (GLA). It has been agreed by the Leaders of London's local authorities and the Mayor of London.

2. London Government has long held common ambitions regarding a greater role over the setting and retention of business rates and has worked closely together to put this case to government. In recent years we have repeatedly raised concerns regarding the sustainability of the tax, which is in desperate need of reform. The review is therefore very welcome.

3. However, it comes at a time of great economic uncertainty caused by the coronavirus pandemic, in which London businesses have been hit hard. While the grant support and temporary rate relief provided by Government so far has been very welcome, it is clear that substantial challenges will remain for the foreseeable future – particularly in the retail, hospitality and leisure sectors. Central London and its town centres – in common with the centre of cities across the country – face potentially far-reaching changes in business activity and property use, and it is too early to tell what the long-term impact will be on the commercial property market.

4. It is highly likely that some elements of the current support packages will need to continue into 2021-22, and we urge the Government to confirm its plans for business rates support for businesses beyond March as soon as possible.

5. Our response to the review, therefore, represents the fundamental reforms we think are required for business rates to be implemented once we are emerging from the pandemic; such reform could help to stabilise the economy and support future growth.

6. The review sits alongside the Comprehensive Spending Review, due in the autumn, that will set the overall level and priorities for public spending for the next three years. It also comes at an important crossroads for local government finance, with fundamental decisions to be taken soon regarding the overall quantum of funding (CSR), adult social care reform, and further reforms to the business rates retention scheme and Fair Funding Review, which have been pushed back a year due to the virus. We strongly urge the government to take a joined-up approach and view these events in the round rather than considering them in isolation.

7. These decisions, alongside a view about the future role of local government as captured in the forthcoming Devolution and Recovery White Paper, point to the need for a new settlement to underpin the funding of local government going forward, including the potential for new sources of revenue and greater fiscal devolution.

8. Business rates currently fund over 40% of local government spending. Any reforms that reduce the overall tax will reduce funding for local public services unless equivalent alternative revenue sources are identified. We therefore welcome the recognition that the "impact on the local government funding system will be an important consideration in reviewing the tax", but are concerned that this issue is not addressed in the call for evidence.

9. More broadly, any reforms that reduce the tax yield raises questions about the potential for new taxes to replace or supplement business rates and, importantly, who controls them, including whether they can be easily collected and allocated on a local or geographical basis. It is clear that business rates cannot, in their current form, bear the strain required of them, and that a broader range of taxes is required to reflect the modern economy.

10. However, if those alternative taxes are introduced in a blanket manner across the country, they will once again fail to reflect the needs and aspirations of local communities and hamper those communities' efforts to rebuild their local economies. We believe local government should play a central role in designing and controlling such alternatives and will set out fuller views on this and the broader themes of the review in our second submission for the 31st October deadline.

11. This response firstly sets out London Government's general comments on the review, and overarching views regarding the reform of reliefs and the multiplier, before answering the detailed questions in the call for evidence.

**General comments**

12. London Government welcomes the opportunity to respond to this call for evidence and to participate more widely in the fundamental review of business rates. Prior to the pandemic, London was due to generate over £10 billion gross in business rates before reliefs - a third of the national yield. London's economic recovery following the pandemic will be vital to that of the country overall. Any reformed system must, therefore, take into account the views of Londoners, London's rate payers, and its democratically elected politicians.

13. London Government has a strong history of working together in the pursuit of greater devolution of business rates. Both London Finance Commission (LFC) reports (2013 and 2017), supported by London Councils and the GLA, presented clear arguments for full control and retention of the proceeds of business rates. Of particular relevance, the latter called for:
    - devolution of the full suite of property taxes including business rates;
    - devolution of the operation and setting of business rates, including setting the multiplier; and
    - London Government to be granted full control of business rates reliefs, including the flexibility to introduce a more effective small business relief scheme to reflect London's higher rental values.

14. Our joint response to the Government's proposals for 100% retention in 2016 represents the most detailed and worked out proposals to date[2]. It called for the decoupling of London's business rates from the rest of the country's and for London Government to have full control over both the setting and distribution of the proceeds of the tax, and a separate London regional arm of the Valuation Office accountable to London Government similar to the arrangements introduced in Wales in 2015.

15. While the extent of the Government's reforms was less ambitious than this, London Government has demonstrated, through the London business rates pool, continued appetite for further devolution. We have shown that we can work collaboratively and are willing to take on more responsibilities and resources to deliver stronger outcomes for Londoners. The business rates pilot pools in 2018-19 and 2019-20 delivered over £250 million of direct strategic investment – and leveraged a further £700 million that would not have happened otherwise – in

[2] In particular see our joint response to the 2016 consultation on 100% retention: https://www.local.gov.uk/sites/default/files/documents/london-councils-and-gla-j-fde.pdf

housing, regeneration, skills, transport and digital infrastructure across the capital. The fact that London continued to pool in 2020-21 despite a large part of the financial incentive being removed, again shows commitment to collaboration for the benefit of Londoners.

16. The pilots and the current pool are, in our view, a small but important stepping stone towards greater business rates retention and further fiscal devolution of the level set out in the LFC reports, and we remain committed to the long-term goal of full local control over the setting and distribution of business rates in the capital.

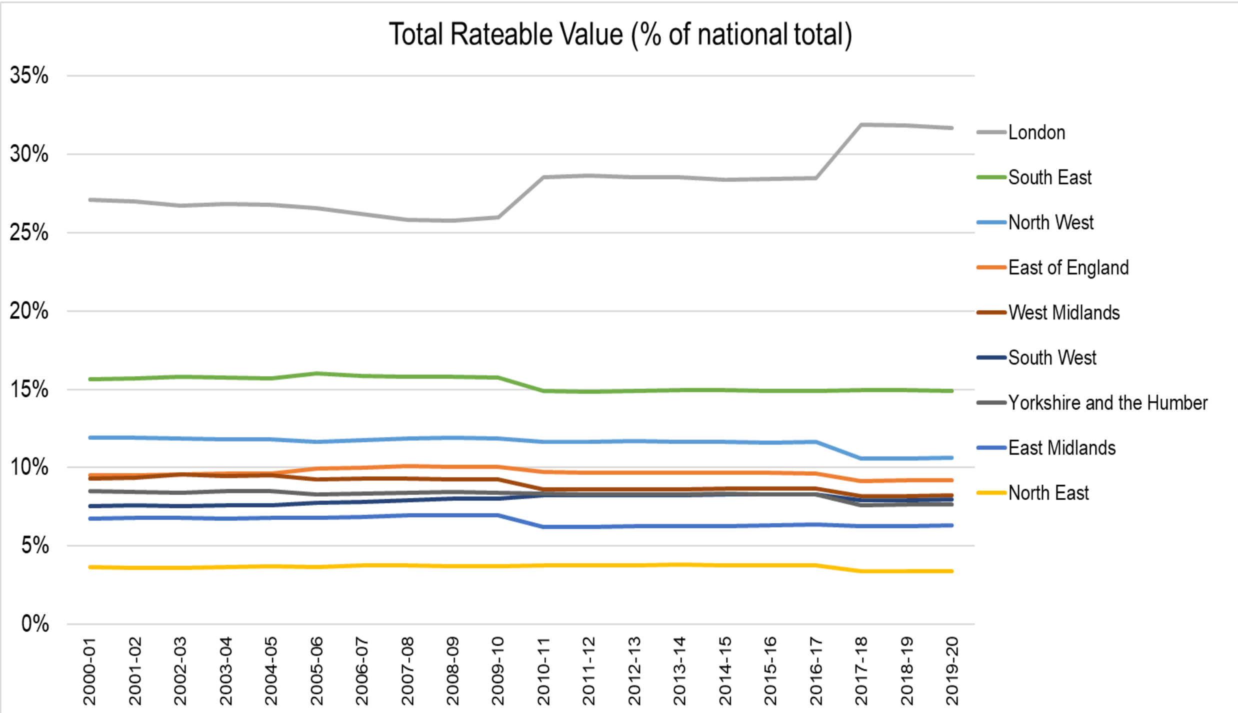
17. However, the tax remains flawed and is in desperate need of reform. It has three major pitfalls. Firstly, it is overly complex for ratepayers and local authorities with a multitude of reliefs and exemptions and qualifying thresholds which can vary from year to year. Secondly, it has been eroded across much of England in recent years, such that it is overly concentrated on particular sectors and geographies. Finally, as it is centrally controlled, it is not responsive enough to local economic conditions or the needs of local businesses and communities that local authorities serve.

18. **Complexity** – the tax has been repeatedly altered at fiscal events in recent years as successive Chancellors have added more complexity by creating further reliefs for different sectors. Many of which have often been temporary (such as retail, new build empty relief and retail reoccupation retail which applied in 2014-15 and 2015-16 only or pub relief in 2017-18 and 2018-19 with more comprehensive schemes to support those sectors introduced in 2019-20 prior to the current pandemic). Whilst the Government has set out the justification and purpose of these reliefs, the constant change has made it difficult for ratepayers to understand which reliefs they are eligible for or not and undermines the transparency of the tax. Some high street service businesses have been excluded from eligibility for retail relief and grants this year (e.g. those providing medical or health services or car repairs), whereas other service businesses have qualified even though they have not been adversely affected. Similarly, many supply-side firms and small businesses occupying offices in London above the small business rate relief threshold have received no rates relief or grants at all: the £51,000 rateable value threshold excludes 24% of businesses in London, compared to only 9% elsewhere.

19. The series of additional reliefs has also added further complexity for local authorities in administering the tax and in understanding how these reliefs impact local government funding through the rates retention system. It also weakens the relationship between local economic success and retained revenues – thereby

undermining both accountability and incentives without significantly increasing equality of outcome.

20. **Distortion** – the tax has become more concentrated on particular sectors and geographies over the last 20 years. The national multiplier is set to ensure that, at each revaluation, the total yield does not exceed a Treasury-determined level. In practice this means that London (particularly central London) – where property prices have been rising faster than the rest of the country – bears an increasing share of the overall burden. Following the 2017 revaluation, London now accounts for around a third of the total rates yield in England (see chart below). Indeed in 2019-20 one London billing authority - Westminster City Council - alone collected £200 million more in business rates than Birmingham, Bristol, Leeds, Liverpool, Manchester, Newcastle, Nottingham and Sheffield City Councils combined. One Oxford Street department store paid more business rates than was collected in 2019-20 by around twenty district councils. This is inherently unstable. It also reduces the incentives for local authorities outside London – whose tax bases are thereby suppressed - to deliver additional growth in the way envisaged by the business rate retention system.




21. At the same time, growth in online sales has meant that tax increases have been felt harder by retailers with a physical presence (particularly on the high street) who have struggled in recent years. This longer-term impact on retail shopping habits and commercial office use, particularly in the centre of cities, further highlights the fragility of the tax.

22. **Centralisation** - A single national multiplier covers a huge variety of local economies – in England. Northern Ireland, by contrast, has a regional rate supplemented by locally set rates in each of 11 districts, each with a population comparable to that of a London Borough and much lower business rates tax bases. England's centralised approach is inflexible and results in central government attempting to support particular sectors by using the blunt instruments of nationally set thresholds which fail to take into account variations in rental values and local economies. These include the national multiplier, the system of centrally prescribed mandatory reliefs, and many of the Government funded discretionary relief and grant schemes with rateable value qualifying thresholds ranging from £15,000 to £51,000 to £100,000 depending on the scheme.

23. These issues were apparent before COVID-19, but the pandemic has exacerbated them. The short-term measures to support businesses – the guarantee of £10 billion of business rates bills through emergency reliefs and shoring up businesses with a further £12 billion through various grant schemes – means the Government is now guaranteeing more than one third of the rates income (rising to nearly two thirds in some London boroughs) and the future of the tax beyond this year is uncertain. We urge the Government to confirm as soon as possible how it intends to support business rates for businesses still affected by the pandemic after the current financial year. This will not only provide certainty for businesses but for local authority financial planning.

24. Given these issues, we welcome the stated aims of the review to improve the current business rates system to make it more sustainable; and to consider more fundamental changes in the medium-to-long term.

25. In essence, London Government believes the tax must be made simpler and more responsive to local circumstances. A new single business rate system applied to all local economies risks repeating and reinforcing the problems of the current system: reformed business rates in London should reflect the particular circumstances of the capital's economy and commercial property market. A greater local role in the operation of business rates is needed now more than ever if authorities are to have the necessary tools and levers to drive the local economic and social recovery in their areas. In particular, the government should start by reforming the system of reliefs and the national multiplier.

<u>Reliefs</u>

26. London Government has long called for greater local control over reliefs to enable local authorities to better address the needs of their local economies and

communities. Even prior to COVID-19 mandatory reliefs awarded in London amounted to around £1.1 billion in 2020-21[3]. Four mandatory reliefs account for 95% of all reliefs in 2020-21: the Small Business Rates relief, Empty Property relief, Charitable relief and the retail relief. The parameters around these reliefs are currently set by central government. London Government believes these could be used more constructively to improve local economies - and support local economic recovery - if devolved to London Government.

27. We believe London Government should have the collective ability to set the qualification criteria and thresholds of the existing mandatory reliefs currently set by central government (and the discretionary elements of those schemes), as well as determining new relief schemes periodically when deemed necessary.

28. Locally determined reliefs and discounts would encourage greater dialogue and engagement between London Government and businesses and empower local authorities to respond to the specific needs of their local economies, for example supporting the regeneration of high streets and town centres by incentivising cafes, arts and culture spaces, workspace or civic uses. Collective control over reliefs would also facilitate more strategic planning to meet other statutory duties; for example, by tailoring reliefs to incentivise the provision of healthy food retailers (rather than fast food outlets) they could help promote better public health outcomes.

29. These reforms could create a far stronger platform on which to increase incentives to support economic growth, promote broader policy objectives and link councils more closely to their business communities.

30. Prior to COVID-19, the largest of these reliefs in scale was **charitable relief** (£2 billion nationally in 2020-21). We believe there should ultimately be full local discretion over the mandatory percentage discount (currently 80%) or, failing that, the ability to vary the threshold within certain centrally prescribed parameters (e.g. between 50% and 80%). The current relief is applied to all properties occupied by charities – whether head office or high street retail - and are applied inflexibly across the country. Arguably this both subsidises charity shops - which may be desirable in its own right, but may also contradict and inhibit local economic development plans - and incentivizes avoidance tactics whereby landlords let large empty buildings coming to the end of their relief period to charities. In London, the particular prevalence of charities in some high streets may be keeping rents artificially high.

[3] Including retail discount relief.

31. Similarly, **empty property relief** (accounting for almost £900 million in 2020-21), has centrally fixed parameters (regarding the length of time they are vacant and are applied to most sectors equally (with longer time period for industrial property). Were these parameters under local control, authorities could make much more targeted and responsive local actions to address vacancies in high streets, business and industrial parks and other areas. We believe this would also help to reduce rates avoidance.

32. With regard to **small business rates relief**, we believe the current national one size fits all approach works particularly badly in London, where many businesses that, by any other measure (the number of people they employ, their turnover or profitability) would be defined as small, do not qualify for 100% relief due to their RV being higher than the £12,000 threshold with tapered relief offered up to £15,000. London has over 1 million SME businesses, many of which will need to be in high rental value properties due to the nature of their business, access to clients and access to talent, and will sit above the threshold.

33. A 2019 survey by the Federation of Small Businesses of their London members showed 72% of their members did not qualify for rate relief; and 74% of their members cited Business Rates as a major issue, with 23% saying that the impact could mean them shutting their business, and only 15% saying it will have no impact.

34. The qualifying threshold to receive a 100% exemption from business rates under the small business rates relief scheme is only £12,000 in England – compared to £15,000 in Scotland under the Scottish government's equivalent small business bonus scheme. The taper for partial relief is also £3,000 higher north of the border and ratepayers retain eligibility if the combined rateable value of their properties is up to £35,000 compared to only £20,000 in England. As a result, fewer than 4 per cent of businesses in Westminster, for example, based on their original 2020-21 estimates submitted in January 2020, qualify for small business rate relief.

35. Finally, the targeted **retail relief** introduced in recent years, prior to the COVID-19 retail relief, is reflective of the broader issues around increasing online sales and the decline of the high street. Again, it has a national RV threshold of £51,000, which may not make sense for retail businesses in London, which are small by all other definitions, but would not qualify for this relief.

The multiplier

36. Given the urgent need for a sustainable system, and the extraordinary circumstances surrounding the current economic climate, London Government reiterates its previous call for local control over the business rates multiplier within a reformed tax system to enable greater local accountability over and responsibility for local economies. We believe that towns, cities and local councils that are more responsible for their own destiny and more accountable for their own success, would design better taxes and provide better services.

37. London Government would wish to explore options for locally determined multipliers, with the Mayor of London being granted the ability to set a proportion of the rate on a London wide basis, and boroughs setting the rest of the multiplier, with those respective proportions to be determined by London Government. As suggested by the LFC, the rate of any increase could potentially be pegged to that of Council Tax increases.

38. There is precedent from the devolved administrations for this, with the multiplier and valuation arrangements being devolved to the Welsh Assembly in Wales in 2015, and a two-tier multiplier implemented between Northern Irish districts and the Northern Ireland Assembly, which has been in place for a number of years. Both of these options are worth exploration in English regions. Scotland has also essentially operated its own separate devolved arrangements, supplemented by the Scottish Assessor valuation model for business rates, since 1854. Many of the recommendations of the independent Barclay review of business rates, relating to reliefs, tax setting, exemptions and tackling avoidance which concluded in 2017 and were subsequently implemented relatively swiftly by the Scottish government, have equal applicability to England. If such arrangements can work in the devolved administrations, resulting in a more dynamic tax which can respond more speedily to emerging developments, there is surely no logical reason why they cannot be made to work in London and in the other regions and cities of England.

39. In the short term, as a way of piloting or transitioning to this more ambitious scheme, London Government would at least wish to have the ability to vary the change to the national multipliers set annually by central government.

**Detailed response to consultation questions**

**Reliefs**

**Q1 - How well do current reliefs and exemptions deliver their intended outcomes and satisfy the principles of good tax design? What changes would you suggest to the system?**

40. London Government does not believe the current reliefs and exemptions deliver their intended outcomes and satisfy the principles of good tax design. As outlined in paragraph 15, the growing number of centrally determined reliefs has created a complex system of compensation arrangements through a series of section 31 grants, each with their own individual methodology. This creates uncertainty in medium- and long-term financial planning, for both businesses and local government, and undermines the transparency of the tax. Simplification should be a priority as part of this review.

41. The current suite of centrally prescribed reliefs is a blunt instrument to effect policy outcomes. As set out above (paragraphs 26-35), London Government believes the system of reliefs should be substantially reformed to enable local authorities to respond better to their local economies. We believe local areas should have the ability to set the qualification criteria and thresholds of the existing mandatory reliefs currently set by central government, as well as determining new mandatory relief schemes periodically where there is local support to do so.

**Q2 - How can reliefs be targeted more effectively? How can reliefs and their administration be simplified?**

42. As set out above (paragraphs 27-29), London Government believes greater local control of reliefs (at the regional and local level) would enable reliefs to be targeted more effectively. A one size fits all approach with nationally set qualifying rateable value thresholds which take little or no account or local economies or rental levels is simply no longer viable. Locally determined reliefs and discounts would encourage greater dialogue and engagement between London Government and businesses and empower local authorities to respond to the specific needs of their local economies, for example supporting the regeneration of high streets and town centres by incentivising cafes, arts and culture spaces, workspace or civic uses. Collective control over reliefs would also facilitate more strategic planning to meet other statutory duties for example, by tailoring reliefs to incentivise the provision of healthy food retailers (rather than fast food outlets) they could help promote better public health outcomes.

43. These reforms could create a far stronger platform on which to increase incentives to support economic growth, promote broader policy objectives and link councils more closely to their business communities.

44. With regard to simplifying administration, COVID-19 Small business grants scheme has exposed how limited the available information is regarding the businesses paying business rates. Any reforms should look at how this can be improved, for example through online registration systems, or potentially via information sharing with HMRC, and or Companies House.

**Q3 - What evidence is there on the capitalisation of business rates and business rates reliefs into rents over time? What does any evidence mean for the design of rates reliefs and business rates more broadly?**

45. We are aware of a study by Regeneris[4] commissioned by British Property Federation (BPF), British Council of Shopping Centers (BCSC) and British Council for Offices (BCO) in 2015, which looked at the impact in urban centres. It suggested changes in rates paid are reflected in corresponding adjustments in rental values (at least up to 2008), but that this relationship is stronger in regional markets than in London.

**Q4 - What role should local authorities have in determining business rates reliefs and exemptions? Should reliefs and exemptions be set by central government or set locally?**

46. As set out above (paragraphs 26-35), London Government believes local areas should have the ability to set the qualification criteria and thresholds of the existing mandatory reliefs currently set by central government, as well as determining new mandatory relief schemes periodically where there is local support to do so.

47. In London, we would envisage that where individual boroughs or the Mayor wished to offer additional discounts over and above a collective scheme agreement, this could be achieved through adjustments to their retained rates. We therefore believe the power to offer business rates discounts directly should be extended to the Mayor of London, where these were more generous than those being offered by billing authorities, although these would be paid for from the GLA share of retained rates.

[4] https://www.regeneris.co.uk/business-rates-who-pays/

48. We also believe that the ability to determine which properties are exempt should be devolved to London Government. We are aware that the IFS advocates re-examining the justification for existing reliefs, such as those for vacant land, agricultural property and low-value properties, and would wish to explore further the rationale for the current exempt properties if business rates were devolved further.

**Q5 - Are you aware of ratepayers misusing tax reliefs or other means to avoid paying their full business rates liability? What could be done to tackle this?**

49. The main avoidance concerns regularly raised by London boroughs include:
    - **gaming/abuse of empty property relief** - whereby a property is occupied for 6 weeks, then left empty for 3 months before a "sham" occupation (a few boxes, or a Wi-Fi box/Bluetooth broadcaster); or where a company transfers part of business to another to obtain small business rate relief.
    - **gaming/abuse of charitable relief** - by bogus charities, or where a charity applies for mandatory relief but the property is later found to be unoccupied.
    - **Basic fraud/avoidance** – by "Phoenix" companies that cease to trade, then reopen under a new name; or whereby properties that have continuous changes in the liable party and no rates are paid
    - **Other Gaming –** for example, the use of building as Wi-Fi / Bluetooth broadcasting to obtain lower RV; vacant properties being let to companies who immediately become insolvent thereby passing debt to receivers; informing council/VOA of dividing building into different parts – used for different purposes; and de-activated communication stations.

<u>**The business rates multiplier**</u>

**Q6 - What are your views on how the business rates multiplier is set annually and at revaluations?**

50. London Government has repeatedly raised concerns about the fixed yield valuation system which is making the tax ever more concentrated on – and sensitive to – the central London property market. The continuation of this principle will mean London accounting for ever more of the national business rates tax take (we estimate that, if current trends continue, it could be 40% by 2050). The impact of this is that a larger proportion of funding for the rest of the sector is being generated by London's tariff – i.e. its surplus in business rates. This makes other parts of the country more reliant on top-up grant, undermines the growth

incentive and, in a system that is supposed to incentivise councils to promote growth, makes no economic sense.

51. We believe the solution is to end the fixed yield system and allow true local devolution of the tax enabling London government to be accountable for London's business rates by decoupling its tax base from that of the rest of the country, as part of the devolution of a wider suite of taxes and revenue raising powers that would make London government more accountable to local taxpayers and – we believe - more effective.

52. In the absence of local devolution of control over the multiplier, and in the absence of a business rates retention scheme that removes the risks of business rates appeals, we believe the way the multiplier is set needs to better build in the costs incurred through appeals.

53. We also find that the multiplier rate set each year is confirmed very late in the year, which delays budget setting for the following year and impacts on our business planning. At a time of great uncertainty, being able to plan further ahead is strongly recommended.

**Q7 - How could the multiplier be set in future to ensure the sustainability of public finances and support growth and productivity? What would the impact of any proposed changes be on the level of the multiplier and revenue from business rates over time**

54. As set out in paragraphs 36-39, London Government would wish to explore options for locally determined multipliers, with the Mayor of London being granted the ability to set a proportion of the rate on a London wide basis, and boroughs setting the rest of the multiplier. These two shares of the overall multiplier would be determined by the funding and retention split between the GLA and the boroughs. As suggested by the LFC, the rate of any increase could potentially be pegged to that of Council Tax increases.

55. There is precedent from the devolved administrations for this, with the multiplier and valuation arrangements being devolved to the Welsh Assembly in Wales in 2015, and a two-tier multiplier implemented between Northern Irish districts and the Northern Ireland Assembly, which has been in place for a number of years. Both of these options are worth exploration in English regions. Scotland has also essentially operated its own separate devolved arrangements, supplemented by the Scottish Assessor valuation model for business rates, since 1854. If such arrangements can work in the devolved administrations, there is surely no logical

reason why they cannot be made to work in London and in the other regions and cities of England allowing the tax to be re-engineered in ways that are more suited to and responsive to England's different local economies. It was of course a broadly locally set tax in England from 1603 to 1989.

56. In the short term, as a way of piloting or transitioning to this more ambitious scheme, London Government would at least wish to have the ability to vary the change to the national multipliers set annually by central government.

**Q8 - How should the multiplier and any supplements relate to business rates reliefs? Should these be discrete, or should supplements fund specific reliefs?**

57. We believe, within a devolved London system, there could be greater level of consistency over thresholds applied to business rate supplements and business rates reliefs. The definition of a small business, for example for the purposes of the Small business rates multiplier (£51,000), is different to the definition for SBRR (£12-15,000) and is different to the threshold for the London Crossrail Business Rates Supplement, which is £70,000. The 2017 revaluation transitional relief scheme also used three different thresholds for small (up to £20,000 RV or £28,000 in London), medium (£28,000 to £99,999) and large properties (over £100,000) which determined the speed at which ratepayers moved towards their underlying new liability. Local discretion over the setting of the multiplier, relief and supplements in London, linked to a set of rateable value thresholds reflecting London's higher rental levels, could create more consistency in this respect.

**Q9 - What are your views on introducing additional multipliers that vary by geography, property value, or property type?**

58. Rather than additional multipliers, London Government calls for the transfer of the current multipliers to local government along with the ability to vary them. This would enable better adaptation to local business floorspace, variable by sector and type of organisation, to ensure local need is met and the diversity of the local economy is upheld. Lessons could also be learned from how business rates are operated and set across the devolved administrations including for example the Northern Ireland model where there is a province wide multiplier combined with a variable component at individual local authority level.