



House of Commons
Communities and Local
Government Committee

**Local Government
Finance—
Supplementary
Business Rate: the
Government's
Response**

Third Report of Session 2007–08



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*Report, together with formal minutes and
Appendix*

*Ordered by The House of Commons
to be printed 8 January 2008*

Communities and Local Government Committee

The Communities and Local Government Committee is appointed by the House of Commons to examine the expenditure, administration, and policy of the Department for Communities and Local Government and its associated bodies.

Current membership

Dr Phyllis Starkey MP (*Labour, Milton Keynes South West*) (Chair)

Sir Paul Beresford MP (*Conservative, Mole Valley*)

Mr Clive Betts MP (*Labour, Sheffield Attercliffe*)

John Cummings MP (*Labour, Easington*)

Jim Dobbin MP (*Labour Co-op, Heywood and Middleton*)

Andrew George MP (*Liberal Democrat, St Ives*)

Mr Greg Hands MP (*Conservative, Hammersmith and Fulham*)

Anne Main MP (*Conservative, St Albans*)

Mr Bill Oler MP (*Labour, Nuneaton*)

Dr John Pugh MP (*Liberal Democrat, Southport*)

Emily Thornberry MP (*Labour, Islington South and Finsbury*)

The following members were also members of the Committee during this inquiry:

David Wright MP (*Labour, Telford*)

Martin Horwood MP (*Liberal Democrat, Cheltenham*)

Powers

The Committee is one of the departmental select committees, the powers of which are set out in House of Commons Standing Orders, principally in SO No 152. These are available on the Internet via www.parliament.uk.

Publications

The Reports and evidence of the Committee are published by The Stationery Office by Order of the House. All publications of the Committee (including press notices) are on the Internet at www.parliament.uk/clgcom

Committee staff

The current staff of the Committee are Huw Yardley (Clerk of the Committee), David Weir (Second Clerk), James Cutting (Committee Specialist), Sara Turnbull (Committee Specialist), Clare Genis (Committee Assistant), Gabrielle Henderson (Senior Office Clerk), Kerrie Hanley (Secretary) and Laura Kibby (Select Committee Media Officer).

Contacts

All correspondence should be addressed to the Clerk of the Communities and Local Government Committee, House of Commons, 7 Millbank, London SW1P 3JA. The telephone number for general enquiries is 020 7219 1353; the Committee's email address is clgcom@parliament.uk

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1 Our report

1. On 7 August last year we published our Report *Local Government Finance: Supplementary Business Rate*.¹ The Report followed the recognition in the Government’s Green Paper *The Governance of Britain* that “enabling communities to take decisions about how to use local funds can also help ensure that local priorities are being met”² and the proposal by Sir Michael Lyons to allow local authorities to make marginal changes to the national non-domestic rate.³

2. The Government had offered, in both the March 2007 Budget and the later *Sub-national review of economic development and regeneration*,⁴ an encouraging but general reaction to Sir Michael Lyons’s proposal, promising to give the matter further consideration and to make a more substantive response later in the year. We argued that that response should set in motion a process to enable local authorities, including upper and second-tier authorities in two-tier areas, to levy a supplementary business rate to increase or decrease the business rate paid by local businesses. We recommended a number of safeguards to ensure that local authorities secured the agreement of the local business community to introduce a supplementary business rate and on the purposes to which revenue could be applied; but we considered that, given those safeguards, a wide degree of local discretion was appropriate, including over the level of supplement, requirements for ballots of local business, and exemptions and discounts.

¹ Communities and Local Government Committee, Seventh Report of Session 2006–07, *Local Government Finance: Supplementary Business Rate*, HC 719.

² Ministry of Justice, *The Governance of Britain*, Cm 7170, July 2007, paras 176-7.

³ Sir Michael Lyons, The Lyons Inquiry, *Place-shaping: a shared ambition for the future of local government* (hereafter ‘Lyons report’), March 2007, Recommendation 8.2, p.296.

⁴ Budget 2007: *Building Britain’s long-term future: Prosperity and fairness for families*, para 3.138; *Sub-national review of economic development and regeneration*, July 2007, para 6.43.

2 The Government’s proposals

3. The Government’s proposals were published in a White Paper in October 2007.⁵ The White Paper accepts the case for introducing a power for local authorities and the Greater London Authority (GLA) to raise and retain local supplements on the national business rate.

4. The Government’s proposed model for business rate supplements involves four levels of protection for business:

- Revenue from supplements will only be available for spending on economic development, such as infrastructure. Plans will need to be clearly specified and committed in advance; and spending will be subject to a transparent accounting framework to ensure this.
- A national upper limit of 2p in the pound will be set on the level of supplements that can be levied.
- To protect smaller businesses from disproportionate burdens, properties liable for business rates with a rateable value of £50,000 or less will be exempted from paying supplements.
- Where the supplement will support more than a third of the total cost of the project there will additionally be a full ‘double-lock’ ballot of businesses affected.⁶

5. The White Paper continues:

Revenues from supplements will be locally raised and retained, with local decision-making on the duration of any supplement and the specific projects it should be spent on. The Government intends that that only the highest tier local authority in any area should be entitled to levy supplements. These authorities will be able to cooperate to raise supplements to fund joint projects, within the existing statutory framework. In London, the power will rest with the Greater London Authority. Shire counties will be required to consult their districts on any new supplement proposals.⁷

6. The Government supplemented the White Paper with a brief memorandum to us with “an explanation of why the Government decided to deviate from some of [the Committee’s] recommendations.” That memorandum is published as an Appendix to this Report.

⁵ HM Treasury and Communities and Local Government, *Business rate supplements: a White Paper*, Cm 7230, October 2007 (hereafter ‘White Paper’).

⁶ White Paper, Executive Summary.

⁷ *ibid.*

3 Our response

7. **We welcome the fact that the Government has made a commitment to give local authorities an opportunity to develop their role in place-shaping and identity-building, in partnership with local business.** In the introduction to our Report, we recalled the series of reviews of local government finance which have taken place over the last 30 years, and regretted that “there has under successive Governments been little change designed to create a funding system that supports and enables local authorities to fulfil their role as ‘strategic placeshapers’.”⁸ In proposing the introduction of a power to introduce a supplementary business rate, the Government has taken a first step towards reforming local government finance in a way which will begin to give local authorities the power needed to fulfil the role envisaged for them.

8. **However, the Government’s proposals, and its response to our Report, are a significant disappointment. They lack a convincing vision of the future. They are over-cautious and so circumscribed that they will fail to secure any real advance in autonomy for the majority of local authorities.** The Government’s proposals would result in an SBR with a significantly lesser degree of local discretion than that which we envisaged. Its response to our report is unconvincing in its arguments for the restrictions placed on the powers proposed and wholly lacking in any engagement with our broader conclusions on the need for further financial devolution to local authorities.

Differences between the Government’s proposals and our recommendations

9. The most significant differences between the Government’s proposals and those which we recommended are as follows:

- **Ballots.** We recommended, in line with Sir Michael Lyons’s conclusion, that there should be no requirement for a ballot on SBR proposals within the affected business community: local authorities should be free to hold a ballot “when local or specific circumstances warrant”.⁹ The Government proposes a requirement for a ballot where the contribution supported by the supplement exceeds a third of the total cost of the project.¹⁰
- **Level of authority empowered to levy an SBR.** We recommended that upper-tier authorities should be empowered to propose an SBR in co-operation with second-tier authorities in their area, and second-tier authorities should have the power to propose an SBR, either individually or jointly with neighbouring districts;¹¹ and that the Greater London Authority should have the power to initiate a London-wide supplementary business rate which could be blocked by a two-thirds majority of London local authorities, but individual London boroughs and the Corporation of London should

⁸ HC 719, para 16.

⁹ HC 719, para 35.

¹⁰ White Paper, paras 2.56ff.

¹¹ HC 719, para 42.

also be able to initiate a supplementary business rate.¹² The Government intends to empower only the highest tier local authority in an area (in London, the GLA) to levy an SBR;¹³ shire counties will be required to consult their districts on any new supplement proposals.¹⁴

- **Maximum level of SBR.** We recommended that there should be no cap on the SBR rate determined by local authorities.¹⁵ The Government proposes a limit of 2p in the pound.¹⁶ The Lyons report had recommended a 4p cap.
- **Exemptions and discounts.** We recommended that any decisions on exemptions or discounts should be determined at a local level.¹⁷ The Government proposes an exemption from SBR for hereditaments with a rateable value of £50,000 or less, with authorities able to provide for further exemptions or discounts.¹⁸

Maximum level of SBR

10. The Government’s proposal for a cap of 2p in the level of supplementary business rate which may be levied is the most disappointing aspect of the White Paper. Sir Michael Lyons envisaged a cap of up to twice that, 4p.¹⁹ Combined with the Government’s proposal to exempt all businesses with a rateable value of £50,000 or less, the proposed cap slashes the amount of money which could be raised through the levying of a supplementary business rate, by comparison with the Lyons proposals. Lyons suggested that a 4p SBR, levied uniformly across the country, could have raised some £1.6bn.²⁰ It has been calculated that the yield under the Government’s current proposals would be only some £600m.²¹ It has also been pointed out that, even if every local authority with the power were to levy the maximum permitted rate, the total raised would still not replace the £850m reduction in Local Authority Business Growth Incentive (LABGI) funding announced at the same time.²²

11. In its memorandum to us, the Government argues that a national upper limit on the level of supplements which can be levied by local authorities “will provide important security for businesses and will also serve to protect ratepayers from the impact of cost overruns.” It continues, “A maximum limit will ensure an appropriate level of protection of national economic and fiscal interests given the increased ability of local authorities to

¹² HC 719, para 52.

¹³ White Paper, paras 2.64ff.

¹⁴ White Paper, paras 2.71–2. In London, statutory arrangements already exist for the GLA to consult the boroughs as part of the budgeting process (para 2.71).

¹⁵ HC 719, para 53.

¹⁶ White Paper, paras 2.41–2.

¹⁷ HC 719, para 56.

¹⁸ White Paper, paras 2.51–4.

¹⁹ Lyons Report, para 8.48–50.

²⁰ Lyons Report, para 8.48.

²¹ Local Government Association press release, 10 October 2007, ‘CSR settlement is ‘worst in a decade’’, www.lga.gov.uk.

²² *ibid.*

borrow for capital purposes that will result from the supplement.”²³ The White Paper adds, “Using a higher limit [than 2p] would increase the risk that spending grows faster than capacity to spend efficiently.”²⁴

12. It is in the failure to trust local authorities to take effective decisions, in partnership with local business, about the levying and use of local funds that the Government demonstrates its lack of vision. The proposal as it stands will allow significant sums to be raised in some areas, particularly London, and no doubt some worthwhile projects will come to fruition even outside London as a result. But the possibilities could have been much greater. We concluded in our Report that “it would be rare for a local authority to seek, and for the business community to accept, an SBR involving more than a marginal variation to the [national non-domestic rate]”, but where those circumstances did come together “we [saw] no reason why it should not be allowed.”²⁵ In our view, provided that adequate measures were put in place to ensure that an SBR was levied by consent, the precaution of a cap was “unnecessarily draconian.”²⁶ The Government has produced no evidence or arguments to change our view and **we are dismayed that the Government proposes to hobble local authorities’ ability to raise sums which would enable them, in partnership with local business, to make a meaningful contribution to the economic development of their area.**

Degree to which local authorities will benefit

13. Furthermore, the proposals which the Government has brought forward are likely to be of significant benefit only to a relatively small number of authorities. First, the Government is denying the power to levy an SBR, whether individually or in partnership with neighbouring authorities, to second-tier authorities, including London boroughs. We found the Government’s rationale for this decision, as set out in its memorandum to us, unconvincing. The Government says that this is “to avoid businesses in two-tier areas potentially paying two supplements, for the best fit with economic entities and to avoid complexity”.²⁷ Given the requirement to agree the levying of a supplement with local business, we consider this restriction unnecessary, either in London or elsewhere. As we noted in our original Report,

it seems perverse in the extreme to enable upper-tier authorities across the country—including Rutland with its population of 37,000 and capacity to raise a few hundred thousand pounds annually from a 1 pence levy—to initiate an SBR but to deny similar flexibility to London boroughs such as the City of Westminster, with its population approaching quarter of a million and the capacity to raise almost £25 million on the same terms.²⁸

²³ Appendix, response to recommendation 7.

²⁴ White Paper, para 2.42.

²⁵ HC 719, para 53.

²⁶ *ibid.*

²⁷ Appendix, response to recommendation 5.

²⁸ HC 719, para 51.

14. Secondly, even if all authorities were to have the power to levy SBR, this power alone would not give all local authorities the same opportunities to raise money. As our original report recognised, “the facility to levy a supplementary business rate is most attractive for unitary authorities covering urbanised metropolitan areas ... other areas, particularly less urbanised and rural parts of the country, would not be able to benefit or not to the same degree.” We have previously “encourage[d] Ministers to consider and bring forward alternative measures alongside a supplementary business rate to allow local authorities and local business communities seeking additional funds for local investment to choose a means which is suitable for their specific local circumstances.”²⁹ The Government’s decision to restrict the ability to levy an SBR to upper-tier authorities increases the importance of this recommendation. Thus far, however, there is no sign of any such measures, nor has the Government seen fit to make any formal response to our conclusion.

Further financial devolution to local authorities

15. Finally, we find it necessary to reiterate our conclusions regarding the longer-term consequences following from Sir Michael Lyons’s report and more recent Government policy pronouncements regarding the future role for local government. We argued in our original report that “the Government should consider implementation of Sir Michael’s recommendations on local government revenue not as the last word but the beginning of a development process of financial devolution”, recommending that “its response to the Lyons report should set out how and when the next steps might be taken.”³⁰ **Once again the Government has not seen fit to respond to our conclusions; and there is little sign as yet that the Government looking beyond SBR to any “next steps” in financial devolution to local authorities. As we noted in our original Report, more is needed if local authorities are to become the leaders of vibrant communities and the engines of local economic development. Is the supplementary business rate—with its 2p cap and its restriction to upper-tier authorities—the limit of the Government’s ambitions post-Lyons? Or will it have the courage and vision to go further? The Government’s rhetoric on the devolution of power to local authorities is good. Thus far, however, its actions have failed to live up to that rhetoric. We seek a clear indication from Government that it is prepared to match its words with significant action to empower all local authorities to become the ‘place-shapers’ of the future.**

²⁹ HC 719, para 39.

³⁰ HC 719, para 64.

Appendix

Letter from the Rt Hon Hazel Blears MP, Secretary of State for Communities and Local Government to Dr Phyllis Starkey MP, Chair, Communities and Local Government Select Committee

I wrote to you on 16 October about the Communities and Local Government Committee's Seventh Report of Session 2006–07 Local Government Finance: Supplementary Business Rate which was published 7 August.

I explained at the time that the Government had published as part of the CSR and PBR for 2007 *Business rate supplements: a White Paper* setting out how the Government intends to introduce powers for local authorities to raise business rate supplements and covering the Committee's 15 recommendations. This was in lieu of a specific command paper responding to your report.

I understand that the Committee has asked for an explanation of why the Government decided to deviate from some of their recommendations. This is enclosed.

Hazel Blears

26 November 2007

COMMUNITIES AND LOCAL GOVERNMENT COMMITTEE

LOCAL GOVERNMENT FINANCE: SUPPLEMENTARY BUSINESS RATE

Government response to individual recommendations

The Government's conclusions were different from the Committee's in some respects, but overall we are confident we have achieved the right balance, including between the interests of business, of local authorities, and of the wider community.

Recommendation 3. Local businesses' acceptance of levy proposals and spending plans, secured through a ballot or demonstrated through consensus-building consultation, should be achieved before any SBR is imposed. Sir Michael Lyons' recommendation was that there should be no requirement for a ballot on SBR proposals within the affected business community. We agree. Local Authorities should, however, remain free to hold a ballot when local or specific circumstances warrant.

The Government has specified the circumstances in which accountability to business and transparency should be based on a consultation and when it should be based on a ballot. The reason for this is to best align the incentives with the accountability arrangements.

Where the private sector will be meeting most of the costs of a project, there is less of an incentive on the local authority to focus on value for money and to ensure that spending is effectively targeted. With less of its money 'at risk', there is a greater chance that the authority will commit to less productive expenditure. In these circumstances, a ballot can provide a better alignment of incentives. Businesses can effectively weigh up the balance of costs and benefits. There is no incentive for business to attempt to 'call the bluff' of the authority in the belief that they can benefit from the investment without contributing to a supplement.

For larger projects where revenue from the supplement is only one small part of a number of funding streams that need to be lined up, the uncertainty of a vote could make it extremely hard to reach agreement. There is also the risk that business would vote against, in the belief that the project would go ahead anyway. In those cases, transparency and accountability will be provided through statutory consultation. Businesses and other stakeholders can clearly see the costs and benefits associated with a project, and can assess the proposal fairly. They will have the assurance that the local authority will stick to its stated plans.

We will therefore require a ballot of businesses where the contribution supported by the supplement exceeds a third of the total cost of a project.

Recommendation 5. We recognise the additional difficulties and complexities that may be involved in securing agreement to levy a county-wide SBR in two-tier areas. We recommend that upper-tier authorities should be empowered to propose an SBR in co-operation with second-tier authorities in their area. We also recommend that second-tier authorities have the power to propose an SBR, either individually or jointly with neighbouring districts; and that specific arrangements should be determined by the local authorities involved in conjunction with the local business community, case by case.

The Government intends that only the highest tier authority in any area should be entitled to levy supplements to avoid businesses in two-tier areas potentially paying two supplements, for the best fit with economic entities and to avoid complexity. Districts have a key role in establishing partnership, gathering information and developing policies to improve economic well-being in the towns, cities and localities they represent. Shire counties will be required to consult their districts on any new supplement proposals. Authorities with supplement powers will be able to work jointly within the existing statutory framework.

Recommendation 6. We agree with Sir Michael Lyons that special arrangements for London are justified on the grounds of its unique governance arrangements and economic circumstances. We do not agree that powers to levy an SBR should rest with the Greater London Authority only. We recommend that the Greater London Authority should have the power to initiate a London-wide supplementary business rate which could only be blocked by a two-thirds majority of London local authorities. In addition individual London boroughs and the Corporation of London should be able to initiate a supplementary business rate either individually or in co-operation with other boroughs.

In London, there is a clear case for the single supplement that business should be required to pay being set by the GLA. It is a democratic city-wide authority whose role is to take strategic decisions on the economic development issues that a business rate supplement is for. In this context there is no case for the London Boroughs to be able to block a GLA decision to set a supplement.

Recommendation 7. We recommend that the SBR rate should not be capped by central government but determined locally and that where SBR proposals contemplate a local variation, upwards or downwards, of more than 10 per cent, a ballot of the business community should be the norm.

A national upper limit on the level of supplements that can be levied by local authorities will provide important security for businesses and will also serve to protect ratepayers from the impact of cost overruns. A maximum limit will ensure an appropriate level of protection of national economic and fiscal interests given the increased ability of local authorities to borrow for capital purposes that will result from the supplement.

Recommendation 8. Local authorities should not be able to exempt or discount the liability of public sector buildings for a supplementary business rate.

Recommendation 9. We recommend that any decisions on exemptions and discounts, other than in relation to the public sector's liability, are made at local rather than national level.

A standard exemption for hereditaments with a rateable value of £50,000 or less will provide consistency for businesses and protection for smaller businesses which the economic evidence suggests can be disproportionately affected by changes in business rates. The legislation we will be introducing will also enable authorities to provide more generous safeguards for local businesses, including whether to introduce a taper above the £50,000 threshold.

Recommendation 10. We recommend that where a supplementary business rate is introduced in an area which includes an existing business improvement district there should be an off-set for BID contributors against their supplementary business rate liability.

The Government supports BIDs and shares the Committee's view that they should not be undermined or discouraged by the introduction of BRS. We agree with the Committee that provision should be made for an offset for BID contributors against their BRS liability and the legislation we will be introducing will cater for this. However, we consider that the decision whether to have an offset is a matter that should be determined locally on a case by case basis rather than being imposed centrally. In many cases, those businesses paying a BID levy will not be liable to pay a BRS due to the £50,000 rateable value exemption we have announced. In other cases, it should be left to local authorities developing proposals for BRS to consider whether there should be an offset for those ratepayers contributing to a BID. In doing so, authorities will need to consider the benefits that those particular businesses are likely to derive through the BRS as well as from contributing to the BID.

Recommendation 13. We recommend that the Government monitor the long-term impact of supplementary business rates on the rateable values of business properties.

As part of the process of consultation or voting, local authorities will be required to make an assessment of the impact of a supplement on local business and to show how this relates to the benefits that will be delivered from projects supported by the supplement. In addition, rateable values are regularly updated by the Valuation Office Agency.

Recommendation 14. We recommend that local authorities and local businesses should be free to determine jointly their own investment priorities.

We agree with the Committee's recommendation, subject to the safeguard that supplements should only be used to finance additional investment in economic development. We announced in the White Paper that we will consult on how best to deliver the additionality requirement.

Recommendation 15. We recommend that SBR proposals include a clear timetable pegged to project milestones rather than absolute time periods where this is more appropriate. The timetable should include safeguards for both ratepayers and council tax payers against project overruns and, in the case of council tax payers, against any long-term financing costs arising from SBR projects.

As the Committee acknowledges, infrastructure projects of the type that might in future be financed in whole or in part through BRS can extend over many years and overrun their original estimated deadline for completion. In view of this, we consider that setting a national maximum limit on the duration of supplements could put projects at risk. At the same time, we agree with the Committee that certainty and predictability are key factors in ensuring the success of BRS. We consider this can best be achieved by local authorities setting out their plans for expenditure, including timescales and how the supplement is intended to operate, as part of the statutory consultation with local businesses and other stakeholders. This will ensure that those affected by a supplement have a good foundation for assessing the merits of particular projects.

Formal Minutes

Tuesday 8 January 2008

Members present:

Dr Phyllis Starkey, in the Chair

Mr Clive Betts

Bill Olnier

Jim Dobbin

Dr John Pugh

Andrew George

Local Government Finance—Supplementary Business Rate: Government Response

Draft Report (Local Government Finance—Supplementary Business Rate: Government Response to the Committee's Seventh Report of Session 2006-07), proposed by the Chairman, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 15 read and agreed to.

A Paper was appended to the Report as Appendix 1.

Resolved, That the Report be the Third Report of the Committee to the House.

Ordered, That the Chairman make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

[Adjourned till Monday 14 January at 4.20 pm]

Reports from the Committee during the current and previous Sessions

The reference number of the Government’s response to each Report is printed in brackets after the HC printing number.

Session 2007–08

First Report	Coastal Towns: the Government’s Second Response	HC 70
Second Report	DCLG Annual Report 2007	HC 170
Third Report	Local Government Finance—Supplementary Business Rate: the Government’s Response	HC 210

Session 2006–07

First Report	The Work of the Committee 2005-06	HC 198
Second Report	Coastal Towns	HC 351 (<i>Cm 7126</i>)
Third Report	DCLG Annual Report 2006	HC 106 (<i>Cm 7125</i>)
Fourth Report	Is there a Future for Regional Government?	HC 352-I (<i>Cm 7119</i>)
Fifth Report	Refuse Collection	HC 536-I
Sixth Report	Equality	HC 468 (<i>Cm 7246</i>)
Seventh Report	Local Government Finance—Supplementary Business Rate	HC 719
Eighth Report	Local Government Finance—Council Tax Benefit	HC 718
First Special Report	Local Government Finance—Council Tax Benefit: Government’s Response to the Committee’s Eighth Report of Session 2006-07	HC 1037
Second Special Report	Refuse Collection: Government’s Response to the Committee’s Fifth Report of Session 2006-07	HC 1095