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XX September 2016

100% Retention of Business Rates

Dear Matthew

Thank you for the opportunity to respond to your consultation on the future of Business Rates and Fair Funding.

I attach a schedule setting out the council's responses to the individual questions within the consultations. Where the council felt there was some duplication in the consultation questions, it has clustered its responses to a group of questions.

I hope that you find our responses helpful in providing ministers with views that can assist in developing an effective outcome to these consultations and achieving the purpose of fiscal devolution. The council would be willing to take up any opportunities to work further with the Department to develop the ideas and comments in its response.

The council has also contributed actively to and endorses the responses by the Three Southern Counties (3SC) and the Society of County Treasurers. I would highlight 3SC's response as being particularly pertinent to questions concerning combined authorities.

In summary, the council would like to emphasise some important key principles (some of which are considered further within the specific consultation questions below).

- Unfunded pressures must be the first call on the quantum; this is particularly important given the pressure on social care budgets and the wider impact on the NHS. Similarly the quantum must also properly fund new burdens on a continuing basis.
- Local government must facilitate (and have the right responsibilities to facilitate) healthy local economies and drive business growth in order to reap the benefits of business rates retention.
- The new funding system must be focused on residents' needs; starting with a simple, fair and relevant per capita funding basis and taking all funding streams into account, including locally raised income.
- The local government sector must fully engage with the consultation and review process in order to create a system which can be tailored to local needs and opportunities.
- There must be transitional arrangements in place to enable a smooth shift to the new system and to assist planning.
- All areas should be enabled to maximise economic growth opportunities, this includes all having the ability to increase the business rates multiplier to fund essential infrastructure.

This specific letter sets out Surrey County Council's fuller response addressing the specifics of the consultation questions.

In several areas the council found it impossible to give a considered answer to the consultation question. This is mainly because, until devolution decisions are made and there is a firmer indication of what the new fair funding formula will look like, the council cannot yet assess the risk in the system nor say how other elements of the business rates retention model should be constructed. The council hopes the discussions started in the consultation continue and develop further at the steering and working groups and decisions made once the devolution and fair funding elements are fixed.

Yours sincerely

1. Which of these identified grants / responsibilities do you think are the best candidates to be funded from retained business rates?

Surrey County Council welcomes the proposal for councils to retain 100% of business rates raised locally. The council is keen to ensure it and other local authorities are well placed to fulfil the stated purpose of fiscal devolution, that is: *'to provide communities with the financial independence, stability and incentives to push for local growth and pioneer new models of public service delivery'*.

Working within arrangements that give the right balance of incentives for growth and support for service responsibilities, Surrey County Council believes it can help grow Surrey's economy even more and by doing so, increase Surrey's contribution to the UK economy. For the council and other local authorities to take full advantage of the potential benefits of the shift to 100% business rate retention, the council believes it is essential there is a clear link between local authorities' new responsibilities funded from retained business rates and economic growth, as suggested by the House of Commons Communities and Local Government Committee in its interim report on business rates. For example, the council believes responsibilities such as skills, transport and other infrastructure provide such a link, fitting the purpose of fiscal devolution and supporting the national priority of increasing economic growth.

Where the Government transfers responsibilities and funding, the council believes local authorities should have genuine discretion over how they provide those services and the ability to shape the services on offer in local areas to suit residents, businesses and the local economy. The council does not believe a simple transfer of funding for some services from specific grant to being funded from business rates will enable this growth aspiration.

The list of grants on pages 18 and 19 of the consultation document are all grants that local authorities already, or will receive. Transferring the funding of these grants from central government to locally retained business rates will result in local authorities having no more or less control over the services; but will transfer the funding risk as the stability and predictability of the funding will depend on the buoyancy of the local economy.

Examples such as the transfer of the Independent Living Find or the Attendance Allowance suggest a poor fit, where local government would merely be a local administrator of central government rules and policy with little or no input to reflect local need and instances and a cost base unrelated to the local business rate revenue. Equally, transfers of responsibilities should also remove ring fenced spending requirement, such as for Public Health. This mismatch could exacerbate the funding risk by placing an unavoidable, unrelated strain on resources and diverting funds away from the national priority of economic growth.

The council believes public services work best where there is collaboration. Therefore, in deciding which services and funding responsibilities to transfer, the council believes local and central government should consider the best place to manage the shared funding risk for local services and allocate funding and responsibilities accordingly to achieve local growth and effective public service delivery.

In summary, as outlined above, the council wants new responsibilities and discretions that:

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- link to the health of the local economy, its business rate base and the council's ability to facilitate their growth; and
- enable and facilitate effective delivery of public services, including through new models of delivery.

2. Are there other grants / responsibilities that you consider should be devolved instead of or alongside those identified above?

As offered in the Three Southern Counties' devolution deal proposal, the council would like to gain responsibility and control of services in the areas of: skills, education, economic growth and transport and digital infrastructure. The council believes these are responsibilities that local authorities can tailor and apply to local initiatives and responses to local needs, issues and plans which will facilitate more effective local economic growth and transform service delivery. Given the extent of the prize at stake and the fundamental long term change 100% business rates retention will bring, the council urges the Government to consider the principles involved and to arrive at the detail through discussion focused on defining the specific transfers to match the core objectives of fiscal devolution. As the success of 100% business rates retention grows, opportunities to transfer further responsibilities will also follow and working within a framework of principles will enable a continuing and focused dialogue to agree future transfers.

The list of grants on pages 18 and 19 of the consultation document only includes one infrastructure grant and that benefits London only. Shire areas frequently miss out on support for investment in transport and infrastructure. If the country is to maximise the benefits of local economic opportunities, it is important all councils are able to access appropriate funding.

Local authorities are already investing, but need to see this commitment matched by government if areas are to reach their full potential. For example, infrastructure investment in Surrey repays handsomely in terms of GVA (Gross Value Added). If the Government wants to incentivise local authorities to invest to maximise economic growth and generate revenues which go beyond business rates income, it is important to enable appropriate funding.

Surrey County Council believes the responsibilities the Government is offering to areas piloting devolution deals include many of the services that can help to improve local growth and so maximise the country's economic wellbeing. The council strongly supports the offer to devolve a wider set of responsibilities to areas that do not have an elected mayor. The consultation paper implies governance may be a barrier to further devolution in some areas. The council would be keen to work with the Department to find ways to overcome this.

Surrey County Council believes whatever decisions the Government makes about which responsibilities to devolve, it is imperative that the first call on the business rates quantum is to ensure the new arrangement funds local authorities' current service responsibilities fully. Then, the transfer of funding from the remainder of the quantum for any existing or new responsibilities needs to be sufficient fully to recognise and accommodate known and foreseeable demand changes (e.g. population increases) and apply the new burdens doctrine to new responsibilities.,

The council recognises and supports the changing environments businesses operate in. Digital infrastructure and internet developments have seen a rise in the volume of small businesses that thrive without the need for a physical operations base and so do not contribute substantially to business rates revenue. Surrey County Council regards these businesses as a strong element of our future economy, both for the county of Surrey and the UK as a whole, and works to encourage and facilitate their growth and success. Given this position, the council urges the Government to develop a way to recognise this business trend and thereby to incentivise local authorities' role in its growth fairly and appropriately.

3. Do you have any views on the range of associated budgets that could be pooled at the Combined Authority level?

Surrey County Council believes individual combined authority areas will have their own views and should be left to agree their own arrangements about organising services and pooling budgets to make the best positive difference to their residents. In addition, the council firmly believes these new responsibilities must be truly new, appropriate to supporting fiscal devolution and not simply funding stream transfers.

The council endorses the collective view of the Three Southern Counties that decisions on pooling budgets should be left to the discretion of the individual areas developing their devolution proposals, as they are best placed to determine the most cost effective way of delivering local services, factoring in the different social and environment factors that impact of their area.

The council believes the responsibilities devolved through devolution deals should not affect the quantum available to the rest of local government, unless those responsibilities are devolved throughout local government and funded through the business rates retention distribution method. In other words, the appetite of combined authorities or those areas with an elected mayor should not result directly in less business rates funding for responsibilities devolved in other areas. An area's ability or suitability to adopt specific governance arrangements should not determine whether local authorities in an area have the opportunity to improve the services offered to their residents.

4. Do you have views on whether some or all of the commitments in existing and future deals could be funded through retained business rates?

Commitments in existing and future deals could be funded through retained business rates, provided those same responsibilities are devolved to all local authority areas. For example, some devolution deals include skills funding, Surrey County Council believes this should be devolved to all local authority areas to encourage and facilitate more local economic growth. In this scenario, that part of a devolution deal which includes responsibility and funding for skills could be funded from the quantum. Other features of specific devolution deals which are not available to all areas, should not be funded from business rates quantum.

5. Do you agree that we should continue with the new burdens doctrine post-2020?

Yes. Surrey County Council supports the continuation of the new burdens doctrine, which ensures newly transferred responsibilities between central and local government are fully funded and commends the increased transparency it brings. The council fully expects the move to 100% business rates retention to also include some element of grant funding. This could be an important element of flexibility in:

- managing service delivery funding risks at the most appropriate level (as outlined in the response to Question 1); as
- enabling devolution of responsibilities at the most appropriate time, rather than delaying transfers until a reset; and
- preventing the transfers of responsibilities becoming unsustainable through insufficient funding.

Depending on the decision made about the length of time between resets, the council would like to see the new burdens doctrine not only assessing the costs in the year of transfer but also projecting costs until the next reset, using reasonable, foreseeable cost and volume changes. It is undeniable many local authority services are likely to follow a demand pattern which is different to the pattern of economic growth and business rates revenues. As such, when a new transfer takes place, reasonable funding projections must be in place for future years to ensure service viability.

6. Do you agree that we should fix reset periods for the system?

The critical considerations here involve incentives, risk and reward.

- what is the risk that future retained business rates will not properly fund services; and
- what are the prospects of retaining the future proceeds of growth given the impact of the reset on the extent to which they will be retained?

If the proceeds of growth will be lost fairly frequently due to relatively short reset periods, there is low incentive for local authorities to invest in local economic growth. If economic growth and business rates revenues fail to keep up with service expenditure, for example due to faster demographic growth, then local authorities could need more frequent resets. The key is finding a balance. Enabling local authorities to retain a proportion of previously earned business rates growth would mean shorter reset periods would have a stronger incentive for local authorities to invest in economic growth and so become more palatable.

Surrey County Council, like many other authorities, is keen to take on new responsibilities and work to improve our services and areas; it is also keenly aware that many of its statutory services enormously affect the quality of life for many of the most vulnerable residents. As mentioned above, the move to 100% business rates retention brings with it the potential for less stability in councils' funding streams. This will depend not only on the type and frequency of the reset, but also on the responsibilities devolved, confidence in the needs assessment, the expectation of demand and the protection provided by the new safety net arrangements.

The council suggests, as a viable alternative to fixed reset periods, using a trigger system based on reaching a critical disparity between funding and service demand. The council believes this option should be examined fully and is willing to support the Department to do so.

In summary, the answer to balancing this issue of incentives, risk and reward will depend not only on the type of reset, but also on the type of responsibilities devolved, confidence in the needs assessment, the expectation of demand and the protection provided by the safety net. As such the council believes a five yearly partial reset, with full resets if triggered by reaching a critical disparity between funding and service demand.

7. What is the right balance in the system between rewarding growth and redistributing to meet changing need?

As highlighted in the council's response to question 6, this will depend on many factors, none of which are known currently. Before being able to decide their position on this, local authorities will need to know the answer to several questions, including the following.

- What a reset looks like and how much, if any, previous growth can be retained?
- What new services will be devolved?
- What will the needs assessment and new burdens' assessment look like?
- What assurances do councils have about how funding and needs will be aligned in years two and onwards?
- Will the services that local authorities already provide and which are under increasing pressure be funded adequately in the future?
  (In other words, what confidence is there that the demand projections are manageable?)
- What protection will be offered by the safety net?
- How frequent will revaluations be after 2017?
- Will appeals continue to be a local issue, or can a national solution be found?

Once local authorities know all these, then it will be easier to come to a considered opinion on the frequency and nature of resets and the balance between rewarding growth and funding service demand.

8. Having regard to the balance between rewarding growth and protecting authorities with declining resources, how would you like to see a partial reset work?

The council believes if an area works to secure business rates growth, it is right it should be able to keep some of the benefits from it.

In its responses above, the council has emphasised the need for full and proper funding through the business rates retention system of local authorities' current responsibilities and any transferring responsibilities both at the time of transfer and for the reasonably foreseeable future.

The council is aware demand for some types of services grows more quickly than others and in some areas more than in others. It believes a partial business rates reset should also incorporate an element of needs assessment, specifically for demand led services such as adult and children's social care. This would offer more reliable funding for authorities with responsibilities where the pressures and demands do not correlate to economic growth. It would also continue the government's current approach of protecting, to some degree, authorities with social care responsibilities.

The timing of a partial reset could use a trigger system based on a set of indicators for demographic growth factors. The council believes this option should be examined fully and is willing to support the Department to do so.

9. Is the current system of tariffs and top-ups the right one for redistribution between local authorities?

The council believes the redistribution system should be relatively simple and transparent. In making the new needs assessment to determine the tariffs, top-ups and any redistribution mechanisms, it is important this should take account of not only demographic factors, but also include the effects of local differences in the costs of delivering services.

The council supports the Government's previous approach to protect authorities with social care responsibilities, in part achieved through the top-up / tariff system. That need for protection still exists and indeed, grows. The ability to raise funding through the adult social care precept is welcome and adds to the protection these services need. However, in Surrey it only covers about half of the annual growth in demand.

The council does not support the Government taking into account the ability of an authority to raise funds locally through council tax in determining the level of tariff or top-up (as has been done in the current four year offer).The council believes that this ability to raise council tax is already factored into a councils funding and to adjust for it a second time through top-up adjustment is unfairly detrimental to an area.

As the council's responses above state, the mix of responsibilities the Government devolves to local authorities and how they relate to the purposes of fiscal devolution will be important to the success of this significant change in local government finance. Providing the right opportunity for incentivisation of business rates growth and its risks and rewards, balanced against the reliability of other funding, specifically for demand led services such as adult and children's social care, should help mitigate service funding risks. Ideally the council would like to see local authorities exposed to risk (and therefore, reward) in proportion to the demand led pressure on their budgets as well as their potential influence over business rates growth.

Without knowing, even in broad principled terms, what new responsibilities different types of local authorities will take on, it would be futile to suggest a funding split between authorities in two tier areas. The council cautions against considering exact mechanics until there is more clarity over the new responsibilities, their distribution and the funding formula.

10. Should we continue to adjust retained incomes for individual local authorities to cancel out the effect of future revaluations?

Since the introduction of the current business rates retention scheme, local government has still not had a revaluation nor has it had a detailed explanation of what will happen at a revaluation. It is unclear how a revaluation will protect growth attributable to a local authority's actions. The consultation document implies it is possible to adjust the system at a given date to cancel out the effect of future revaluations.

In principle it makes sense to adjust tariffs and top-ups following a revaluation but until we have further clarity, the council cannot provide a definitive answer to this question.

11. Should Mayoral Combined Authority areas have the opportunity to be given additional powers and incentives, as set out above?

Surrey County Council believes for this national scheme of business rates retention, all areas should be treated equally and these powers and incentives should be available in all areas, irrespective of their framework for democratic accountability.

Any additional powers and incentives for Combined Authorities, with or without mayors, can be agreed when the devolution deal is made.

Given the issues facing the economy at this time, the council believes the scheme for fiscal devolution should maximise encouragement, enablement and incentivisation for all local authorities to do all they can to grow and sustain their local economies.

12. What has your experience been of the tier splits under the current 50% rates retention scheme? What changes would you want to see under 100% rates retention system?

Surrey County Council agrees the issue of tier splits will need to be considered once the services to be devolved are decided upon and the balance between risk and reward will be an important consideration.

In its responses to other questions, the council has highlighted the need to protect funding for social care for adults and children. These services are demand led and activity levels and costs do not correlate to economic growth. Failings in these services can have a devastating impact individually, locally and nationally, so funding must continue to be protected.

The council has positive experience of pooling arrangements under the current system. Pooling provided many benefits and the council believes the following features could also work well in tier split areas and combined authorities:

- Enable the area to determine its own distribution arrangement for the additional resources arising from moving to 100% business rates retention, linked to both needs and economic development.
- Use the economy of scale the larger area brings to manage the valuation and appeal risks better.
- Provide a single voice to work more effectively with the Valuation Office to manage business rates within the area.
- Provide a single voice for engagement with the business community over investment.

13. Do you consider that fire funding should be removed from the business rates retention scheme and what might be the advantages and disadvantages of this approach?

With the recent initiative to improve links among blue light services, the council understands the rationale for a desire to move funding for fire from DCLG to the Home Office.

However, for fire authorities currently within a county structure, such as Surrey, any proposed transfer will be complicated, financially, administratively and organisationally challenging and it is difficult to see where the benefit would be, since the fire service is completely embedded within the operation of the council and subject to the same rigorous approach to continual efficiency imporvements.

The council would need assurance and a fuller explanation about how Surrey Fire and Rescue Service would be extricated before giving a full response about a transfer.

The consultation document proposes the Government would replicate published funding allocations for 2019/20 if it removed fire funding from the business rates retention scheme. Given Surrey County Council's proposed grant allocation for that year is -£17.3m, the council has concerns about how the Government would do this and what effect it could have on the fires service and the council's other services.

14. What are your views on how we could further incentivise growth under a 100% retention scheme? Are there additional incentives for growth that we should consider?

Surrey County Council firmly believes the business rates retention system needs fair and effective incentivisation arrangements to achieve the purpose of fiscal devolution. Please see the council's responses to other questions to attain wider points.

The council needs greater clarity on the *default* 100% business rates retention model before commenting conclusively on whether additional incentives are needed. However, as outlined in the council's response to question 2, given the changing nature of business and particularly the areas for strategic business growth in digital and high tech businesses that generate high GVA, but do not occupy a large business rates footprint, the council would like to see greater recognition of and incentivisation to encourage these enterprises through the new funding scheme for local government. Additionally, as one of the purposes of fiscal devolution is economic growth, the council would like the system to reward new business growth more favourably than transfers of essentially the same business between different areas, so the system rewards net new business growth to the country as a whole more strongly.

Shire areas tend to have a much greater share of their gross rates lost through mandatory reliefs. The council would like to sharpen the link between the income and the needs of the residents and allow local authorities more control over the eligibility criteria for mandatory reliefs.

15. Would it be helpful to move some of the 'riskier' hereditaments off local lists? If so, what type of hereditaments should be moved?

The council sees the merit of standardising and consolidating strategic national infrastructure assets such as power stations and airports for administration under a national list given their importance to the development of the whole nation's economy. However, in centralising the income, there should also be a centralisation of the associated risks, especially with the funding of any additional infrastructure that would arise from the expansion of those assets. For example, any strategic rail and road improvements arising from the expansion of either Heathrow or Gatwick airports should be funded by the Government, or through devolution deals by the relevant combined authority and not the individual surrounding local authorities.

Equally, there are also occasions where national government policy affects a business' viability, location or profitability. In such cases, the impact on business rates revenue should not be to the detriment of local residents.

Again, the council is not able to provide a comprehensive answer to this question until it has more information about the operation and protection of the safety net as well as greater clarity about the criteria for a hereditament to appear on the central list.

16. Would you support the idea of introducing area level lists in Combined Authority areas? If so, what type of properties could sit on these lists, and how should income be used? Could this approach work for other authorities?

The council would welcome the introduction of an area based list, as this would support the concept and management of an area based pooling arrangement. It believes the type of properties that feature on these lists is a decision for individual combined authority areas.

17. At what level should risk associated with successful business rates appeals be managed? Do you have a preference for local, area (including Combined Authority), or national level (across all local authorities) management as set out in the options above?

Under the current 50% rates retention scheme, individual local authorities make their own provisions for appeals. It is very likely under this arrangement, that the combined national amount set aside for appeals is greater than if provision was made centrally. This means less money is available for local services than there might otherwise have been and all the risks of appeals sits with local authorities. Under 100% business rates retention, the amount of these provisions could easily double.

In the near future, ahead of 100% business rates retention, local authorities may even need to increase their provisions as they receive increasing challenges from other public service bodies (e.g. NHS trusts).

Therefore the council believes that a national provision for business rates appeals would be preferable as this would ensure that overprovision is not made and funds are kept available for local services. It would also ensure that no authority is unfairly exposed to risk due to the composition of their local rating list. The provision would be funded from income from the central list and distributed to local authorities to reflect their actual losses on appeals.

18. What would help your local authority better manage risks associated with successful business rates appeals?

Greater information and intelligence sharing between the Valuation Office Agency (VOA) and local government would help assess the likelihood of successful appeals. An agreed mechanism of data sharing between VOA and local government would help to standardise the appeals provisions.

19. Would pooling risk, including a pool-area safety net, be attractive to local authorities?

The consultation paper does not give any detailed explanations of the relevant impacts of this proposal. As such the council cannot offer any specific observations, but in general it would support the establishment of an area based pooling arrangement. In saying this, the council also supports and recognises the importance of local discretion about whether a local authority wishes to join a pool or not.

20. What level of income protection should a system aim to provide? Should this be nationally set, or defined at area levels?

Similar to previous answers, the council does not feel it can make any specific observations on this question until more details are available on the responsibilities to be transferred, the associated funding arrangements and how 100% business rates retention generally will look.

21. What are your views on which authority should be able to reduce the multiplier and how the costs should be met?

In two tier areas where the decision will affect more than just the billing authority this decision **must** be made jointly, with the impact of it being borne collaboratively and proportionately.

Joint decision making is not the case for Council Tax Support Schemes, where the billing authority only needs to consult the precepting authorities. The council believes this is not equitable given the disproportionate impact on the upper tier authority.

22. What are your views on the interaction between the power to reduce the multiplier and the local discount powers?

Through the 3SC devolution deal the area is seeking to stimulate and increase economic activity and growth, with the growth in retained business rate income being a key element of gaining the funding needed to facilitate and deliver the economic growth. The council as part of the 3SC area would be interested, through this consultation exercise, to open discussion on securing additional freedoms and flexibilities over the following to help further facilitate growth.

- Control over setting the rate multiplier.
- Freedoms to set local levels of discounts for both mandatory and discretionary reliefs to improve their alignment with the actual needs of local businesses.
- Direct involvement in the timing and process for rate revaluations.

The council would prefer the freedom to change the eligibility for other reliefs and discounts and would argue that the application of discounts will be far easier and enable more specificity in targeting incentives and encouragement than a reduction in the multiplier.

23. What are your views on increasing the multiplier after a reduction?

Local authorities should be free to control it themselves without capping constraints.

24. Do you have views on the above issues or on any other aspects of the power to reduce the multiplier?

As with all other freedoms and responsibilities the council believes these should be granted to all local authorities, regardless of whether they are in a combined authority or have an elected mayor.

This also applies to the application of the power to increase the multiplier – this should be granted to all authorities, regardless of whether they are in a combined authority area or have an elected mayor. In addition as stated in the council's response to question 22, additional freedoms around setting reliefs and discounts could enable more targeted support to local businesses.

25. What are your views on what flexibility levying authorities should have to set a rateable value threshold for the levy?

The council believes this should be decided locally.

26. What are your views on how the infrastructure levy should interact with existing BRS powers?

The council has not used the existing business rates supplement and so does not have a seasoned opinion.

The business rates administration consultation hinted at a way to gather revenue from smaller, businesses that tend to trade on-line. The council would be interested in finding a way for these businesses to contribute fairly to their local area when their physical business rates footprint often means they are exempt from paying.

27. What are your views on the process for obtaining approval for a levy from the LEP?

The 3SC geographic area covers three different LEPs. Each LEP is a partner to the area's devolution deal and so would be involved directly in any discussion about implementing any levy. 3SC recognises the LEPs as the key channel to seeking the views of the business community so would be a seen as a key consultee in any proposal which impacted on the business community.

The council suggests the LEPs should be consultees to a local authority's budget decisions rather than approvers.

28. What are your views on arrangements for the duration and review of levies?

As the levy is a key financial element for delivering infrastructure improvements then the council and 3SC feel the duration of the levy should be left to the determination of the combined authority to match its financial requirement. As the improvement would be subject to development of an appropriate business case in accordance with the Treasury's Green Book, this would facilitate indication of the levy's duration in the initial prospectus as suggested by the Department.

29. What are your views on how infrastructure should be defined for the purposes of the levy?

The council welcomes the use of the CIL definition as a proxy for the definition of infrastructure and would also like to see digital related activity incorporated into the definition to reflect the current, growing and future strategic importance this has in the business community and UK economy in general.

30. What are your views on charging multiple levies, or using a single levy to fund multiple infrastructure projects?

The council believes this should be left to local discretion as to how best to align it with local development needs. The discretion should not be limited to combined authority areas only with mayors.

31. Do you have views on the above issues or on any other aspects of the power to introduce an infrastructure levy?

No.

32. Do you have any views on how to increase certainty and strengthen local accountability for councils in setting their budgets?

The consultation document hints at removing the legislation which requires government to make annual settlements to local authorities. The council is interested in local authorities gaining increased certainty through the use of multi-year settlements and would offer to join or assist full discussions with central government about how this might work and how many years a settlement would cover.

As mentioned earlier, the council still envisages some kind of grants arrangement remaining part of local government funding even after 100% business rates retention is achieved. The success of multi-year settlements will be determined by what local authorities do with the additional certainty and also by how well central government is at leaving the funding system untouched in the relevant years.

33. Do you have views on where the balance between national and local accountability should fall, and how best to minimise any overlaps in accountability?

The council believes this discussion should only take place in greater detail once the devolved responsibilities are decided. Local authorities' funding from other government departments frequently comes with its own rules and reporting requirements. If the Government is keen for local spending decisions to be scrutinised locally then local authorities need to be free to spend their funding in a way that suits their residents, who ultimately give their opinion through the ballot box.

As funding moves from central funding to local and possibly with different patterns across the country, it is important central government departments reflect on this within their own decision making processes. For example, a move to fund public health through retained business rates rather than specific grant will mean the Department of Health will not be able to state exactly what funds are to be spent in an area.

34. Do you have views on whether the requirement to prepare a Collection Fund Account should remain in the new system?

The council believes the requirement to prepare a collection fund account should remain. The collection fund helps the transparency of assumptions around estimates and actuals as well as providing a consistent benchmarking figure.

The council also feels there is potential scope for some technical clarification, for example when business rates income funds capital expenditure.

35. Do you have views on how the calculation of a balanced budget may be altered to be better aligned with the way local authorities run their business?

Surrey County Council supports the principle for local authorities to balance their budgets on an annual basis and welcomes improvements to financial reporting that increase transparency and result in reports better aligned to how local authorities are financed.

The sum outlined in the consultation seems appropriate. However, the council would be interested to see an alternative format.

36. Do you have views on how the Business Rates data collection activities may be altered to collect and record information in a more timely and transparent manner?

The council would prefer to consider this question once the design of the business rates retention model is closer to completion.

SURREY
COUNTY COUNCIL

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XX September 2016

Fair Funding Review

Dear Matthew,

Thank you for this opportunity to contribute to this call for evidence. The council is keen to contribute to the Department for Communities and Local Government (DCLG) and Local Government Association's (LGA) work to implement 100% business rate retention. The council has contributed to and endorses the Society of County Treasurers' (SCT) response to this consultation.

Before responding in detail to the specific questions posed by the call for evidence, the council would like to highlight some of the stark differences between Surrey County Council's funding, shire areas' funding and the rest of the country.

SCT member areas have an average core spending power figure per head of population which is 9% below the national average and 27% below residents in London Boroughs. Surrey's average core spending power per head of population is 12% below the national average and 29% below London Boroughs'. This means London receives an additional £259 worth of services for each resident than in shire areas and £387 for each Surrey resident. Once we take council tax out of this, Surrey residents receive only £165 core funding support each, which is £203 less than the national average and £387 less than London residents.

Furthermore, these differences are before the inclusion of the dedicated schools grant funding, which is well-documented to be significantly higher in London than shire areas.

The differences outlined above are for 2016/17 data. The changes to the 2016 Local Government Settlement mean Surrey local authorities lose core funding support losses much more steeply than the rest of the country, principally because these authorities are among the ones that have to raise the highest proportion of their funding from council tax. The disparity exhibited by the funding system in 2016/17 will be much more extreme if the Government persists with these funding arrangements through to 2019/20. As such Surrey

County Council is pleased the Government is looking afresh at needs in local government and urges it to commit to beginning the new system from a position that is fair and equitable to residents, businesses and taxpayers.

Q1: What is your view on the balance between simple and complex funding formulae?

The Four-Block Model was complex, opaque and extremely difficult to explain to elected members and taxpayers. Since the four block model's introduction it has been widely discredited – both independently and from within the sector. The council, does not believe complexity, in itself is a problem; local authorities deliver a wide range of services to a broad spectrum of people. However, when a funding model results in unexplainable results, unfair treatment of resources and heavy handed levers of ministerial control, then that becomes unacceptable.

Different local services will face needs and demands driven by differences in demographics, economic activities, local costs of delivering services and geographical landscape. Furthermore, these drivers are dynamic and are each changing at different paces across the country. The current reliance on regression analysis encourages statisticians to look for increasingly complex formulas in attempts to replicate the historic pattern of spending or activity. Basing future allocation on past spend cements the line between past and future funding, locks old funding inequalities into the system and increasingly misrepresents local authorities' developing service demands and the varying costs of delivering those services in different parts of the country.

The council believes a sensible approach would be for simplicity and transparency first to achieve a materially fair distribution that is also seen to be fair. The Department and the Local Government Association should then only add layers of complexity to the funding formula provided:

- each case has evidence to justify its argument;
- each additional layer adds value by materially improving the fairness of the system; and,
- the system retains its transparency and continues to be seen to be fair.

For example, start by funding services on an appropriate unit driver basis (for example, each elderly person, each driver mile for use and wear of roads) before hearing evidence about demand and incorporating other measures into the formula to address significant variances. One of the advantages of simplicity and transparency in a funding system that is materially fair is that it is reasonably predictable, enabling local authorities to plan around its outputs.

The council is pleased the Government is consulting on the needs assessment. However, it would be extremely disappointed if the Government attempted to replicate the crude, inequitable and flawed addition to the funding allocation method adopted for the first time in 2016. This late addition to the established method unfairly and repeatedly penalises councils who have to raise a greater proportion of their income through council tax through its direct impact on both Revenue Support Grant and Improved Better Care Fund allocations. The fact that this addition to the allocation method led to the Government having quickly to find

£300m to partially mitigate its unbalanced impact attests to its unsuitability for determining funding allocations across the whole of local government.

Q2: Are there particular services for which a more detailed formula approach is needed, and – if so – what are these services?

Excluding Education, the largest service area in terms of expenditure is Adult Social Care. It is therefore of paramount importance that the increasing demands of this service are captured now and for the period until the next reset. The consultation running alongside this call for evidence suggests partial resets may also incorporate some measure of need reset for demand led services such as social care for adults and children. Given the potential widespread impacts of failures in these services the council would be wholly supportive of demands and funding in these areas being reviewed more frequently than for other service groups.

A key element of this work will be through engagement with the Department of Health and its work since the last formula update on developing social care formulas. This includes the Advisory Committee on Resource Allocation's (ACRA) work to review and recommend changes to the public health formula to calculate the 2016/17 allocation. The council also understands that in anticipation of the Care Act the Department commissioned work from LG Futures on updating the adult social care relative need formula (RNF).

At the time of writing local authorities are also expecting the Improved Better Care Fund formula consultation. The council believes this developmental work will provide a strong platform for the work of the Formula Funding Review in getting the considerable adult social care needs element materially right. The council strongly opposes the current approach to allocating funding through the Improved Better Care Fund as it unfairly penalises councils who have to raise a greater proportion of their income through council tax. The fact that the Local Government Settlement allocates only £1.5m in total to Surrey County Council in 2019/20 (a mere 0.1% of the £1.5bn national total) makes a mockery of Surrey County Council's placing at eighth out of 152 social care authorities and 1.66% share of the national relative needs assessment (which would equate to £25m).

However, the council's earlier comments still remain: future funding allocations cannot be based upon past spend or activity. An area that fares relatively well from the funding system will be able to choose to do more and spend more than an area which is does not. The council strongly urges the Department to speak with directors of adult social care to understand the growing and developing patterns and location specific costs of demand pressures and ensure these are funded adequately rather than relying on regression analysis to lock in past funding.

Many other services provided by the council are coming under intensifying pressure. For example school transport costs are increasing with the rise in the number of maintained schools converting to academies (who are responsible for the qualifying criteria). Historical pressure on concessionary fares budgets has meant, in some areas, the difficult decision to offer reduced bus services is masking the true unfairness of the current funding. The council believes that an approach to funding local services based more on actual service demand drivers will address many of these current issues.

The council also urges the Department not to be constrained by the current allocations. If a new formula is constructed and consulted upon rigorously, but offers a different pattern of funding then, transitional arrangements aside, it should be implemented.

Q3: Should expenditure based regression continue to be used to assess councils' funding needs?

The council believes that a system whereby future funding allocations are calculated on the basis on past spending decisions is not one that supports future funding needs. Instead it simply embeds past funding decisions (whether these were by the local authority itself, or the government) in determining local authorities' funding needs and damping levels.

It is of paramount importance service needs are captured for services now and for the lifetime over which the formula is expected to apply. This is vital for a needs assessment that is expected to be frozen for a number of years under the business rates retention scheme, during which time population increases are expected to cause significant service pressures for demand led services such as Adult Social Care.

The council is excited by the possibility of designing a distribution system from a blank sheet of paper. At the July Needs and Redistribution Working Group the SCT highlighted research by Plymouth University, commissioned by the Police and Crime Commissioners Treasurers' Society in relation to the Home Office's review of the Police Funding Formula. This research proposed an approach which brings together representatives in each service area to agree the key cost drivers in providing each service, to derive a unit cost basis for each service. As you may be aware, the 2015 police formula review failed to agree a formula, primarily due to the way in which the Home Office engaged with the sector. The council believes this more normative approach is worth further investigation.

The council advocates using the same approach for local authority funding, adding a modification to reflect fairly different areas' material differences in service delivery costs. Housing, for example, is a significant element of the cost of living and indicates some of the differences. Average house prices in Surrey in 2016 are 90% higher than the England average, 5% higher than Outer London and 40% higher than the South East. Only the Inner London and all London averages are higher. London tends to receive a weighting to its funding for this, Surrey, to date, has not. The council believes this modified approach will also fairly provide the incentive effect the Government is keen to incorporate.

The July working group meeting agreed ALATS members would form a group to consider putting forward a funding proposal based on this concept whereby local need is driven by a common basket of place based indicators that give a fair reflection of local need, considering primary cost drivers for all local areas. This approach focuses on existing and emerging service need rather than historical spend. It provides a mechanism to establish a funding formula that is relevant today and has future proofing as well.

Q4: What other measures besides councils' spending on services should we consider as a measure of their need to spend?

See Q3. the council considers that a local authority's spending on a service is a very poor measure of need, as it will be dependent on whether it was funded adequately in the past. As stated above, the development of key cost drivers reflecting relative activity levels and different areas' differences in service delivery costs would seem a more fair and equitable measure to assess need. This should also be set against the reset period, so the system assesses need across the medium term, not just the present or recent past.

Q5: What other statistical techniques besides those mentioned above should be considered for arriving at the formulae for distributing funding?

See Q3. The council does not have an issue with the regression technique, in itself. However, for the reasons outlined above it cannot support a method based only on historic spending or activity.

Q6: What other considerations should we keep in mind when measuring the relative need of authorities?

See Q3. The new funding formula must be capable of reflecting future demands for services. For example, the introduction of the Care Act will change the pattern of demand for adult social care from being driven by derivation to being more associated with an ageing population.

Q7: What is your view on how we should take into account the growth in local taxes since 13-14?

The council recognises that local capacity to raise all income (including and not limited to council tax) will need to be considered as part of this review.

The proportion of a local authority's budget which is funded by council tax varies hugely across the country. There can, of course be many reasons for these differences. The council believes a significant one is that past local government settlements have frequently included an element of resource equalisation, whose impact has fallen heaviest in areas with large tax bases.

When council tax was introduced it was based on property values as a reasonable proxy for wealth. Since then the housing market has changed drastically and despite buoyant wage growth in Surrey, the resulting comparison between residents' income and council tax makes for interesting reading.

- Residents in Surrey earn, on average, 16% more than the national average. However, they tend to pay over 40% more in council tax.
- When compared to London boroughs, Surrey residents earn 5% more. However, Surrey residents pay over 40% more for their local authority services.
- Residents in Surrey earn, on average, 45% more than residents of metropolitan areas. However, Surrey residents pay around 75% more for their local authority services.

Clearly using 1991 house prices as a proxy for wealth in 2016 is no longer valid. In the interests of fairness and transparency the council firmly believes this issue needs to be discussed openly and addressed as part of the fair funding review. Leaving the current arrangements in place is unacceptable and risks undermining any work to create a fair funding formula.

On the subject of locally raised taxes the council would also like to see a review of the current council tax support scheme, specifically the protected demographics in shire areas. In a similar way that the SCT is calling for freedoms in relation to funding through business rates the council would also support having the freedom to vary the eligibility criteria for current discounts and support.

Q8: Should we allow step-changes in local authorities' funding following the new needs assessment?

The council believes local authorities need to manage service provision to their local populations as effectively as possible throughout the Formula Funding Review process. The council agrees transitional arrangements are important in ensuring this is maintained if any new needs assessment results in a significantly different distribution pattern by allowing local authorities the time to plan financially for them.

The council believes there is a balance between moving to the new distribution as quickly as possible and a safe transition period that takes account of the scale of funding changes local authorities can manage adequately. The council believes specifying where this balance should be set without knowing the magnitude of changes caused by any new needs assessment would be misinformation at this point in time, and so recommends revisiting it once implications of the new scheme design are clearer.

For the devolution of new responsibilities as part of 100% business rate retention the council agrees that, where possible, existing distributions should be continued for a transitional period and consistent with principles set out for future models.

Q9: If not, what are your views on how we should transition to the new distribution of funding?

See Q8

Q10: What are your views on a local government finance system that assessed need and distributed funding at a larger geographical area than the current system – for example, at the Combined Authority level?

The council expects the move to 100% business rate retention and the Fair Funding Review to lead to significant changes for local government funding. The council believes changes to the current local authority geography system will proceed dynamically at least over the remainder of this Parliament. Distributing funding to these developing and evolving groupings could add further complexity to the system. The council believes local authorities are best placed to consider and decide upon what is appropriate in their local area, be that combined authorities, pooling of budgets or a different form of collaboration determined locally. So, while the council believes the component parts of the needs assessment and funding distribution should remain at individual local authority level, it is for individual councils to decide and agree how they should combine and manage their funding.

Q11: How should we decide the composition of these areas if we were to introduce such a system?

See Q10. The council believes this is something that should be decided on an authority-by-authority or region-by-region basis. A truly fair and transparent funding formula where the assessment of need and distribution of funding are seen to be fair will help to facilitate this.

Q12: What other considerations would we need to keep in mind if we were to introduce such a system?

One of the advantages of collaboration and combination is better management of risk. Allowing and encouraging greater collaboration and combination, while dealing with needs at individual local authority level will provide an incentive for authorities to combine in ways that manage their different risks best.**Q13: What behaviours should the reformed local government finance system incentivise?**

Q14: How can we build these incentives in to the assessment of councils' funding needs?

The approach for reaching a fair funding formula the council outlines above would produce a weighted cost driver approach for each local authority area (or region). The council believes fair funding puts local authorities on a fair footing, should increase the relevance of current and foreseeable needs to funding of services and mean that service portfolio holders and directors can get on with running the best services they can knowing their funding allocation does not put them at a disadvantage. The council does not believe any further incentivisation is needed in the formula.

The council calls on the Government to publish a more detailed, practical implementation timetable, giving local authorities an achievable implementation date for central and local government to plan and work to. For example, providing illustrative distribution figures in July 2018 would be too late for local authorities to plan effectively as local authorities will by then be working on budgets for 2019/20. Furthermore, to deal with any funding shocks such as that experienced by Surrey County Council in the Local Government Settlement 2016, the Government would need to make sufficient transitional funding available.

It is also important decisions are made regarding devolution of services as soon as practicable to enable discussions in other areas to continue. Recent political developments such as the EU referendum, a new Prime Minister as well as new Secretaries of State mean local authorities are operating in a time of unprecedented uncertainty. The council strongly believes local government has shown enormous capacity and competence to change and deal with uncertainty. It is also in an excellent position to work locally with partners, businesses and other stakeholders to stimulate and sustain economic growth. It is important the sector as a whole is enabled and encouraged to deliver this agenda and the council makes a plea to ensure no unnecessary blockages are put in place of any part of the sector.

The council looks forward to continuing to engage in the development of the needs assessment and the implementation of 100% business rates retention and awaits the Government's response to this consultation and the 100% Retention of Business Rates' consultation.

Yours sincerely

Sheila Little
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Surrey County Council

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