

c/o Lee Burge
Room 3.12
Lyons Inquiry into Local Government
1 Horse Guards Road
London
SW1A 2HQ

24 March 2006

Lyons Inquiry Consultation

Dear Sir Michael,

The CBI welcomes the opportunity to respond to your consultation document, published in December. As you know the CBI has already been engaging in this debate both formally and informally via the Lyons Inquiry team and yourself. We have found this approach very useful and hope to continue this positive relationship with you during the remainder of the review.

The scope of the review is clearly extremely wide ranging, and we will not be able to respond to all of the consultation questions outlined in the December interim report. Instead we have identified a number of key areas which we will be developing further over the course of the year. In effect this will be our agenda for the Review.

Our ongoing work will involve members from different regions, sectors and sizes of business and also (hopefully) liaising with local government and others to develop some common objectives and solutions. We look forward to submitting more substantive views during the year. In the meantime, please treat this letter as the CBI's interim response – I apologise that it is slightly late.

CBI Lyons Review priorities

This review provides an important opportunity to develop and clarify the role of local government and also to enhance the relationship between business and local authorities. We need to ensure that local authorities can effectively promote economic competitiveness and really set a vision for their area that stakeholders – including business - can buy into and help deliver. But we are mindful that any debate on form and function cannot really be considered in isolation from funding – in terms of how necessary funding can be achieved and how that funding can best deliver improved local services and prosperity.

As we have already made clear through the Lyons Review consultation process (and during the previous balance of funding debate), a prime concern for the wider business community is the threat of re-localisation of business rates. We will not restate the well-rehearsed debates on this topic, but this sensitivity must be recognised as the review progresses. We would like to take

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this opportunity, however, to emphasise concern over some of the public debate around reform of business rates and urge you to help steer this in a more informed and constructive direction. Our concern is that re-localisation has been portrayed by some as a panacea for local government funding without any real regard to the question of equalisation. We noted the statement in the interim report that equalisation would remain an important part of the system and this has important implications for re-localisation. If there is to be a proper debate on this issue, the realities of equalisation must be openly and publicly articulated.

In addition to these specific concerns the CBI would like to stress the importance of the wider economic context, which makes this debate even more salient. The highly competitive and increasingly global environment in which UK business is operating has significant implications in terms of cost drivers, companies' internal structures and the need for responsiveness and innovation. These factors which are explained in more detail towards the end of our submission serve to heighten our sensitivity towards any proposals that would lead to business paying more at the local level.

The CBI also recognises the importance of addressing a number of other key questions, which were identified in the Lyons Review interim report. We will spend time debating these issues (and seeking to develop some answers) over the coming months. The key areas are:

1. What business wants to be delivered and at what level

Business has a key role to play:

- in helping set the strategic vision for an area and drive economic development and competitiveness
- in the shaping and provision of services
- as a user of services and important part of local communities
- as a funder of local government (not just through business rates but also Section 106, BIDs and a range of other partnerships)

Business views

Firstly it is worth noting that the CBI's recent Public Services survey highlighted a perception amongst businesses that they were not necessarily recognised as an important stakeholder. The table below shows that most businesses in the survey think that the Government only takes their needs into account 'to some extent' or 'to a minor extent'. By contrast businesses think that the Government take account of the views of the public, trade unions, public sector and voluntary sector to a greater extent. It will be important to address this issue during the inquiry:

To what extent do you think the UK government takes into account the needs of the following groups in its public service reforms?	avrg score	a great deal	to a large extent	to some extent	to a minor extent	no account at all	Don't know
Business as user	3.8	0	1	36	46	15	1
Business as funder	3.9	2	6	22	42	27	1
Business as supplier	3.2	2	12	53	22	4	7
Public as users	2.7	6	34	41	11	5	2
Public as funders	3.2	2	15	45	27	8	3
Trade unions	2.7	9	31	33	17	2	7
Frontline public sector	2.9	7	23	47	18	3	3
Public sector admin/mana	2.5	13	33	34	11	2	7
Voluntary sector	3.5	1	8	36	39	8	8

Business needs the right conditions for wealth creation, and local government has an important role to play in this. Key issues include:

- good transport links
- educated & skilled workforce
- quality built environment

- responsive planning service
- safe, clean environment

This was reiterated in the recent CBI Public Services survey. Transport, education and planning were cited as the most important to business competitiveness. But there is clearly much that needs to be done in terms of the quality (and perception of value for money) of such services. Transport and education were seen as the most important priorities for government action over the next five years. Local government will also need to continue to play an important role in terms of intervening where there are market failures or gaps and to help unlock solutions, for example in relation to land assembly.

Another question we asked business focused on the balance between central and local government in setting the framework for delivery. Clearly local authorities are seen as having an important role across many areas, with greater flexibility from central government seen as important in some areas. In particular business identified the environmental and recreational services as being appropriate for greater local discretion and transport as an area requiring greater central government control. On education, planning, public housing and social services the majority favoured significant local government discretion within a broad national framework set by central government.

For the following services, which level of government should be predominant in deciding what needs to be done and how to deliver it? (please tick once for each service)						
	Avg score	No role for local authorities	Central government should play the main role with minimum discretion for local authorities	Local government should have significant discretion within a broad national framework	Complete discretion for local authorities	Don't know
Education	2.6	4	37	52	4	4
Environmental	3.3	1	3	54	38	3
Transport	2.4	5	53	38	2	3
Planning	2.8	2	23	63	9	3
Public housing	3.0	1	13	61	17	8
Recreational	3.5	0	3	43	50	3
Social services	2.7	2	31	53	8	6

Even when Whitehall succeeds in devolving formal responsibility for decision-making down from central government, it still often finds difficulty in letting go and allowing real autonomy at a local level. Business finds Whitehall micro-management in many areas both confusing and counter-productive. There needs to be genuine discretion in areas that are best tackled at a local or sub-regional level.

Clarification of remits

The review should seek to clarify remits of different levels of government and across different organisations. Currently the perception is of many overlapping responsibilities which undermine accountability and can hamper delivery. The inquiry therefore should develop with stakeholders and the Government a shared understanding about what local government and other bodies should do. Ultimately clearer remits should be underpinned by decision-making arrangements that facilitate effective action, appropriate accountability and genuine scrutiny by stakeholders.

Place-shaping

Many businesses are attracted to the idea of local authorities as place shapers, with a more strategic focus on setting a vision for their area (and also looking beyond their boundaries). In the Public Services survey, the majority of business believed that local government setting a clear vision and strategy for the development of the area was the most important aspect in terms of promoting economic growth and competitiveness. We will be seeking to develop clearer views as to what this entails in practice and how different areas can interact more effectively, taking into account wider economic drivers beyond Local Authority boundaries. It will be vital that places

are shaped not just in relation to issues within local authorities but also in relation to other areas and wider economic drivers.

Business is clearly not a monolith - companies face different drivers, have a range of priorities and interact in different ways with local authorities and other public sector agencies. They also have different perceptions about the importance of place. But a key issue for business is the need for greater co-operation and co-ordination across local authority boundaries. As competition becomes more and more international in nature it is increasingly important that areas and regions co-operate effectively. In order to assist this a key priority should be to build up a more complete understanding of each area, incorporating the full range of public and private sector activity, along with an evaluation of the performance and capacity of public service providers.

Role of local government

Local government will clearly need to continue to play a role in delivering efficient and effective public services. Public expectations of local services are rising even as the challenges of delivery become more complex. Both local government and business will need to re-think their role in the years ahead in order to deliver better services and find new ways of working together.

The role of local government in this respect is to lead the community, to understand user needs and to specify and commission services designed to meet those needs. Local people need real and direct power over services. This could come in a range of forms: direct user payment, neighbourhood budgets or more advanced user consultation in the commissioning process. Councils should play a more active and innovative role as commissioners of services. Commissioning should be based on the principle of competitive neutrality – a level playing field – between the public, private and social enterprise/voluntary sectors. Local authorities will also need to build up commissioning capacity and capability.

Some key issues we will be considering further include:

- whether certain services could be delivered at different spatial levels more effectively;
- which aspects of local services require a democratic element ie to be overseen by local councillors and whether some services or parts of services can be effectively delegated / delivered by others;
- how reforms could help deliver services more effectively and more in tune with the local community (business as well as the electorate)
- exploring the role of local authorities in economic development and helping business to grow the economic competitiveness of local areas, with a particular interest in the concept of 'place-shaping'.

2. Developing the relationship between business and local authorities

All of this has implications for the relationship between business and local authorities. This review offers real opportunities for new and improved relationships but there are some challenges to address for all parties if this is to be achieved - and we need clear shared objectives and dialogue.

There are many challenges for different businesses in terms of playing a more active role. Many find it difficult to engage and there is a range of reasons for this, for example the lack of resources, lack of understanding about local government and the type of engagement opportunities. For some businesses the local level is perceived as less relevant as they compete on an international basis and have international supply chains. Others operate at a national level, for example, major retailers which have multiple sites and so a range of contacts with local government. Other companies are primarily local and have significant interactions at this level. There need to be different ways of engaging different players – but above all business must see relevance and genuine opportunities for influence.

Business input into decision-making should be encouraged and improved by creating a climate where business actively wants to get involved. The Public Management Foundation's report *In the Public Interest?* provided some insights as to how to create a climate where business can best contribute to policy. It explains gaps in attitudes between business people and the public sector, and suggests how to design processes that maximise the value of collaboration. Priorities include effective chairmanship, strong teamworking and excellent secretarial support. We also need to be more innovative in developing channels for input. There are a number of key issues:

- need for broader recognition that it is important for business and local authorities to work more closely together
- how to tackle the wider context of increasing understanding and developing shared goals and dialogue
- opportunities to build on good practice and innovative partnership working – the need to identify more examples of good relationships and develop different models and best practice for partnership working. While there will not be a one size fits all, there will be some common factors eg BIDs, although small in scale, offer lessons about what could work more widely
- how to develop different and more appealing mechanisms for business involvement and innovation in relation to how to engage with different types of businesses. We will look at what levels and types of business engagement might be appropriate / possible and also seek to define business experience to date of different forums / models
- local authority can be a key driver in bringing different parties together, developing a clear vision, co-ordinating strategies and generating wider buy-in – Local Area Agreements could be an important basis on which to build.

3. Incentives to motivate local authorities to help develop the local economy and grow the business base

We need to develop clearer and more meaningful incentives and drivers for local authorities to promote economic development. While we strongly support the aims of initiatives such as BIDS and LABGI, there are key issues that need to be tackled in terms of their complexity and effectiveness, particularly in relation to LABGI. Over the coming months we will be working with our members (and more widely) to discuss ways in which such schemes could be more conducive to business involvement and simpler to administer. This will also involve discussing the most appropriate spatial scale at which to operate incentive-based schemes. A key issue is the importance of clear alignment of objectives and drivers – questions that we will be addressing include:

- what positive drivers currently influence behaviour / aims – are drivers sending different / conflicting signals?
- how do objectives align between different levels of government but also within councils and across local authority areas?
- are the drivers sufficient to promote economic growth and achieve wider objectives – and if not what other mechanisms may help improve incentives for local authorities and others to promote economic development?
- are structural changes needed or can the objectives be achieved in other ways?

4. Developing clearer responsibilities and a more influential role for local authorities

There are two key areas:

- to develop the local authority role as "first among equals" within their area (ie horizontal relationships with other public sector bodies)
- to develop clarity in responsibilities between different levels of government – nationally, regionally, sub-regionally, locally and at the neighbourhood level (ie vertical relationships)

Developing the relationship between local authorities and other public sector bodies (both horizontally and vertically) will be important to maximise the effectiveness of local government and also the input and involvement of business. The business community is aware, as a funder, provider and user that services do not start and end with the local authority. Alongside a debate around the most appropriate spatial level for particular services we will be looking at how this impacts on a range of local service providers which fall outside the remit of local authorities.

We are particularly interested in the concept of local authorities as ‘first among equals’ in terms of bringing together different agencies, funding streams and co-ordinating them within a wider strategic framework and vision. The integration of funding streams, service commissioning and other issues could also help to engage business more effectively. The ability to bring different parties together to support economic growth should be central to local government activity. Local Area Agreements are an important building block and we need to understand how real co-operation and pooling can be developed in order to maximise leverage and ensure genuine flexibility within spending.

More broadly, there also needs to be more effective co-ordination across local authority boundaries eg developing transport solutions relating to travel to work areas. Clear mechanisms to develop effective solutions will be key.

5. Issues that need to be tackled to enable local authorities to fulfil role

To deliver this agenda, there is a range of issues that need to be tackled. Business has long made the case for a focus on skills at the local authority level and would emphasise the importance of this in achieving the wider objectives. It is important to recognise that there will not - and should not - always be institutional or structural solutions. Leadership is absolutely critical. But effective leaders will only be attracted to organisations that have clear remits and the ability to get things done

Central government therefore should address a number of areas, including:

- greater flexibility for local authorities over spending / funding streams
- clear boundaries between roles at different levels
- openness where national decisions have implications at the local level
- the interaction between the efficiency and devolution agendas and potential tensions

There must also be a focus on developing project management capabilities and other key skills to support the changing role of local government. With a greater focus on coralling resources and setting a strategic vision and framework, different types of skills are likely to be important. Given the aim to shape and influence the priorities of others, rather than necessarily to administer spending programmes directly, it is imperative that there are strong influencing skills across organisations. These centre on having a clear vision, an inclusive approach, the ability to negotiate effectively and prioritise workloads and objectives. In order to support economic growth and competitiveness in a rapidly changing world, local government and other organisations must also be more responsive and “fleet of foot”.

The (often conflictual) approach within local party politics is perceived as a real ‘turn-off’ by business and can undermine engagement. It is also seen as undermining the willingness of local leaders to take tough decisions. This is clearly an extremely difficult issue to address but the review needs to look, for example, at the role of councillors and how to improve decision-making and encourage a longer-term perspective.

There should also be a look at drivers to promote change rather than just “business as usual”. The emphasis on continuous improvement is important but currently there may be too many or conflicting targets. Some targets are necessary – but we need to look at whether they are the right targets, promoting the right behaviours and whether the interaction between targets is

effective. Local government must have an adequate toolkit to deliver key outputs. We are keen to establish the levers, skills and incentives that are currently in place and assess whether these are sufficient.

6. The overall coherence of the system

As identified in the Lyons Review interim report a perceived weakness of local government is the lack of accountability and transparency. We would therefore welcome, as an outcome of the Lyons Review, having much greater clarification on where public responsibility lies at different levels and in different organisations so that different elements add up to form a coherent and workable system. Key issues include:

- the interaction between different levels of government and between different organisations
- the need for solution to work within the wider context of economic growth and international competition
- the need for honesty in the debate about equalisation – otherwise there will be unrealistic expectations about re-localisation and a likely “fudge” in the outcome
- whether certain projects eg Olympics, City of Culture, urban redevelopment succeed in spite of rather than because of the system
- the need to look more fundamentally at the most effective and efficient mechanisms and distribution of roles rather than defending current responsibilities and simply overlaying new responsibilities or structures
- the need to understand how potential Lyons Review recommendations fit in with the city-region agenda and existing regional arrangements eg RDAs as well the need for a clear strategy for areas that fall outside “city regions”
- the need to understand different drivers, potential interactions and to accept greater diversity of outcomes though there are likely to be limits to the degree of diversity of systems and inputs that business could accommodate without increased confusion and complexity
- the need to drive competitiveness but move away from zero-sum game competition within / between regions. Place shaping needs to take account of wider context and linkages between areas.

7. Importance of wider context

Many businesses are increasingly operating in global and highly competitive markets – and this has significant implications, for cost drivers, companies’ internal structures and the need for responsiveness and innovation. This will also affect their approach to the Lyons Review and increase sensitivity to any proposals that would lead to business paying more at the local level.

For many companies, paying more is simply not acceptable – and for others a minimum prerequisite for any proposals would be clear and additional benefits for business to ensure it is not just a further tax or cost increase. For example, in the case of road pricing many companies are sensitive to the prospect of paying more directly for their road use, but there are potential quid pro quos in terms of congestion reduction and improved transport alternatives. However, there is much work yet to be done to ensure these outcomes actually materialise.

Overall, Budget decisions since 1997 will have added an extra £8bn to the tax bills of business and its investors in the fiscal year about to end – bringing the cumulative additional bill since 1997 to £50bn. As the table below shows, business and its investors have borne a disproportionate share of the tax rise due to post-1997 policy action, even if the impact of above-inflation council tax increases is taken into account.

Approximate change in annual tax take, 2005/06 versus 1996/97

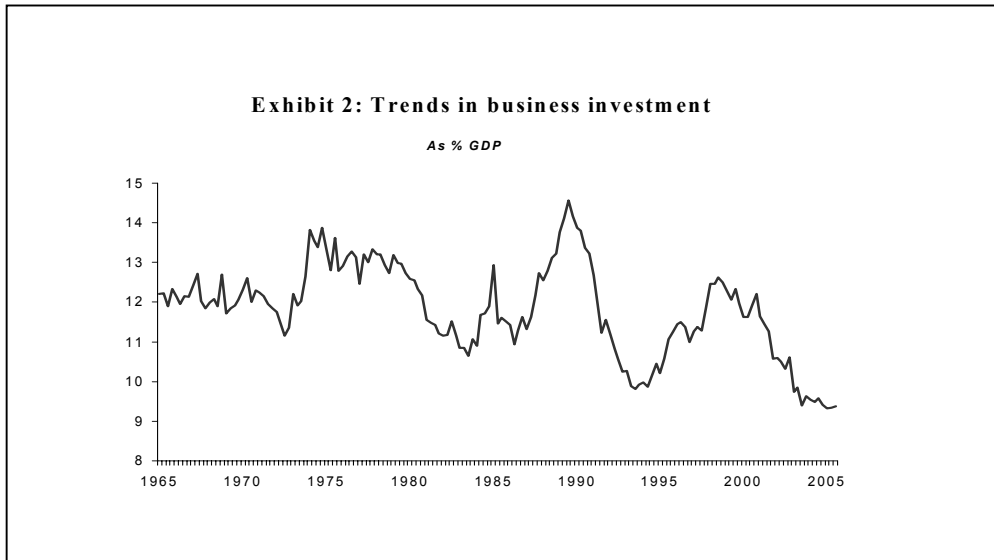
Budget: employer & corporate taxes	+ £3bn	} + £8bn tax rise affecting the } population via business
Budget: tax position of investment funds	+ £5bn	
Budget: all other tax policy decisions	- £4bn	} + £4bn tax rise affecting the } population in all other capacities
Council tax: above-inflation rises	+ £8bn	
Impact of post-1997 policy decisions	+ £12bn	
Tax 'escalators' put in train prior to 1997	+ £5bn	} Additional 'automatic' above- } GDP rise not 'given back'
Residual rise (due to 'fiscal drag', etc)	+ £15bn ¹	
Total rise in tax burden	+ £32bn^{1,2}	
¹ Comparison is with constant share of GDP. ² Of which: £6bn deficit reduction, £3bn to offset lower non-tax revenues, £23bn above-GDP rise in spending. Source: CBI calculations based on successive Treasury Budget Reports		

As a result the tax burden in the year just ending will be £32bn higher than it would have been, had it grown in line with GDP since 1996/97 – £458bn (37.4% of GDP) rather than £426bn (34.8%). Looking to 2006/07, a further rise in the tax-to-GDP ratio is planned to 38.2% of GDP – if achieved, this would be the highest since 1984/85.

The problem is that these fiscal policy impacts have come on top of other pressures making it more difficult for businesses to grow profits, compared with a decade ago. At present, this includes the impact of the economic slowdown. But while the economic cycle will turn upwards in due course, other – 'structural' – pressures have also emerged:

- intense international competition thanks to globalisation and the rise of China as a major world trading power. This has helped to push prices down in product markets, but up in commodity markets, thereby squeezing margins. Imported goods prices (excluding oil) are 17% lower than a decade ago, and export prices are down by 14% on the same basis. By contrast, manufacturers' raw material and fuel costs have risen by 26% in just three years.
- the increase in employer-funded pension scheme deficits, which are having to be reduced through additional business contributions. Employer contributions to funded occupational and personal schemes amounted to £36bn in 2004, having more than doubled from £17bn in 1998. Increased longevity, low long-term interest rates and – until recently – poor global stock market returns have all contributed to this situation, alongside the tax changes.
- Government policies outside of the fiscal policy field, in particular labour market and other regulations that have added to business costs.

In turn, corporate profits recently peaked as a share of GDP, at a clearly lower level than the peaks achieved in the mid-1980s and mid-1990s, and even a little lower than the peak achieved in the late 1970s. Related to this, business investment has been depressed, reaching an all-time low as a share of GDP early last year (exhibit 2). Meanwhile over the past nine years, London share prices have under-performed key European and North American counterparts, reinforcing the pensions 'crisis' which threatens the financial wellbeing of millions of UK residents.



We recognise that local authorities are facing significant pressures - from users of services, from targets and performance systems and in some cases from central government in terms of funding commitments made nationally. And there are responsibilities on all players – local authorities, national government, business and local people to make sure there is a more coherent system with realistic – and fundable – expectations. Business is keen to continue to be part of this debate – but the development of potential solutions must be seen within this wider context.

We hope this letter is helpful as an initial response to your consultation questions and we will work over the coming months to submit a more substantive response along the lines we have identified above. We will be interested to see the papers that are due for publication in April and look forward to a continuing positive dialogue with the Lyons Inquiry team.

Yours sincerely,

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