

307/05

FR

East Midlands Chambers of Commerce

**THE BUSINESS SECTOR'S RESPONSE TO THE
LYONS INQUIRY INTO LOCAL GOVERNMENT FUNDING**

1. INTRODUCTION

As a major contributor (21%) to local authority funding through the National Non Domestic Rate (NNDR), the business community has serious concerns about the underlying funding difficulties affecting Local Authorities, and the inappropriateness of some of the proposed solutions to their funding problems.

East Midlands Chambers of Commerce (EMCC) thinks that there is an important distinction to be drawn, in that not all taxpayers are voters to whom Local Authorities and National Government are accountable. It is important that those taxpayers who lack a vote, notably businesses, are not exposed to any reforms that abuse or exploit this lack of direct accountability.

EMCC recognises that the funding of Local Authorities, under present arrangements, is under severe pressure and we have sought to look at this issue from a business perspective, seeking to suggest possible ways forward.

2. CURRENT PROBLEMS

Variations between adjoining local authorities - this often causes difficulties to businesses whose activities are not limited to a single local authority. This becomes apparent where businesses located either side of a local authority boundary (sometimes separated by a few yards), may experience markedly different levels and standards of service from their respective Local Authorities and, on occasion one business will pay substantially higher fees the same or reduced quality of service. The disparities of cost and quality between rural and urban authorities are also a frequent cause of complaint amongst businesses.

Collection - In general, it is the smallest authorities that act as the tax collector for the Treasury and for the other precepting authorities. This seems disproportionate to the level of services they provide and may not be the most cost-efficient way of running a collection service.

Help in deprived areas - The guidance for the new Local Authority Business Growth Incentive (LAGBI) does provide sufficient incentives to attract inward investment, but it seems excessively complex and doesn't seem to be genuinely helpful where both the local economy and the Local Authority are both struggling. Further powers to discount (and fund) NNDR to attract business investment into economically declining areas needs to be considered in order to help break the cycle of decline.

Help for Businesses in difficulty - despite recent legislative reforms, such as the Small Firm rebate, there is still too little Local Authority discretion to discount NNDR when businesses are in difficulty.

3. ALTERNATIVE SCHEMES

3.1 Property based taxation

3.1.1 Present System - NNDR

The role of the District Valuation Office is important to businesses, as that valuation provides an independent assessment, outside of political control.

Advantages

- Stability and predictability to the NNDR payer between revaluations.
- Protection against above-inflation increases. This is particularly important after revaluations.

Disadvantages

- Significant numbers of non-resident businesses also benefit without contributing – these include a mixture of buy-to-let owners, second homeowners that rent out and promoters of large public events.
- Revaluation based on notional rental is mainly a reflection of land value. This perpetuates the old basis for taxation based on rental income that once made sense before widespread homeownership, which has influenced all property prices. However this logic no longer holds, as the property does not generate income (rather it is a financial burden).
- Revaluations are often heavily geared by substantial changes in land values, This prompts high levels of valuation appeals, which have to be offset in the national recalculation of the NNDR poundage and the transitional arrangements.

3.1.2 An alternative basis for NNDR rateable value – cost of rebuilding

A problem businesses have with property-based taxation is the revaluation process, where booming property values outstrip business performance. The effect of the present system is to ratchet up the cost of occupying property, particularly in town centres, usually to the detriment of local non-chain retailers.

The runaway growth in property prices, both freehold and for rental is mainly a reflection of land value. As a basis for taxation based on rental income, this made some sense during more stable times, but the boom in housing and home-owning has driven up land values in all sectors, regardless of intrinsic value or cost to the landlord.

We suggest that an alternative model be studied, that looks at the less volatile cost of rebuilding as the foundation for a more stable NNDR tax base.

Advantages

- This could help to reduce the impact of volatile land prices and could be fairer to freeholders in particular.
- The valuation of the fabric of a building gives a better reflection of the services likely to be consumed.
- Building insurance information is a fundamental part of finance applications and lease agreements, so the insurance valuation could easily be used as the evidence for the tax base.
- This more stable basis for valuation could be better understood by NNDR payers and could help to reduce the erosion of the tax base due to the high level of appeals that the present system of revaluation provokes.
- This should be easy for District Valuation Offices to handle and administer.

Disadvantages

- An over-simplistic approach could be unfair, e.g. if the property is listed, the rebuilding cost would be disproportionately high.
- Under-occupied property would still present the same problems as the present NNDR
- There could be difficulties in valuing multiple-use property such as flats over shops, block of flats, bedsits and so forth.

Advantages

- Local income tax administration should be a fairly simple task for Revenue & Excise to implement, whose existing responsibilities in administering benefits and tax credits dovetail well with applying social and means based policies.
- Another potential advantage, of using a national agency in this way, is that apportionment of liabilities to national companies and other absent/transient users could be handled in a more co-ordinated way.
- The cost-benefits of handing responsibility for NNDR collection to Revenue & Excise could be investigated. We believe there may be an opportunity to rationalise the cost of collection, increase efficiency and to place revenue protection in effective hands.

Disadvantages

- If local authorities ceased holding and maintaining the NNDR register, they would lose a valuable information base for other statutory purposes. It could make Business Improvement District proposals harder to develop.

5. BUSINESS IMPROVEMENT DISTRICTS

This concept has become an institution in the US and Canada, and Chambers of Commerce through our national body, BCC, pushed for their implementation in the UK. The pilot schemes are beginning to demonstrate that business communities see the advantages, to the extent that the first referendum in Kingston on Thames was passed with a substantial majority on a proposition to levy an additional 1 penny in the pound on rateable value to be collected with the NNDR

Advantages

- The scheme is voluntary
- The funds raised are truly additional to statutory Local Authority Services
- The ability of other agencies and local government to buy into a BID project offers a win-win public-private partnership

Disadvantages

- Without good preparation of the BID proposal, this process is vulnerable to accusations of proposing a stealth tax.
- Local Authorities are not yet well equipped to produce and present the information needed from the Business Rates Registers to enable good BID proposals to be generated.
- The level of levy that could be justified and raised in deprived communities with a low NNDR tax base may be too small to be worth setting up a BID proposal.
- The start-up costs for the first BID project in a new area seem high, although experience may show how to bring this down.

6. CONCLUSIONS

In the EMCC's view, it is important that everyone who consumes local authority services makes a fair contribution to the costs. The geography of work and life has grown beyond the tight communities that created our Local Authorities, once reflected in the linkage between consuming local services and voting/paying tax, but this has been diluted over time. This matters to business in so far that differing local tax burdens distort the employment relationship and the disparity in delivery between different Local Authorities adds to businesses' feelings of resentment.

Since the full cost of Local Authority services cannot be met from what local people and businesses can afford, the role of redistribution by government will and should remain the foundation of local government funding. This is particularly important, as it protects the contribution of those tax payers that have no vote from exploitation or abuse. Suggestions that

3.2 Local Income Tax

The potential of progressive local taxation to stabilise Local Authority funding would be worth considering and could help to engender greater confidence. This proposal would be of direct relevance to the Self Employed, and of indirect interest to the rest of businesses, assuming that this would be handled through PAYE, and provided there is no extra Red Tape.

Advantages

- Income Tax is more likely to be fair and is clearly based on ability to pay.
- A simple administration process that allowed employers to show the local tax as an extra line on pay slips could prove popular.
- Rather than create an additional local income tax service in each Local Authority, handing over collection to Revenue & Excise could reduce costs.

Disadvantages

- Employers would be unhappy if they had to handle more red tape as a result of a secondary PAYE system.
- Intrusion and loss of privacy. A local income tax inspectorate with powers comparable to Revenue & Excise could cause deep public resentment and costly litigation.

3.3 Local Indirect Taxes

As this form of taxation is consumption driven, it is a "pay as you go" form of funding.

Advantages

- Introducing a local purchase tax, possibly as a form of VAT precept could provide the means for the non-resident service users to contribute.
- By being consumption driven, the wealth redistribution aspect could be seen as more just.
- As a burden on the most disadvantaged, it causes the least pain, as it is "pay as you go".
- This form of taxation has the advantage of capturing revenue from non-resident users of local authority services and increases the stake of local government in local economic activity.

Disadvantages

- The administrative set up and running costs could be prohibitive
- Supplementary local excise duties or duty precepts are probably not a good idea as, in our crowded island, "smuggling" would be almost impossible to prevent.
- Risks becoming a "stealth tax" on business (or for that matter, local government)

4. ALTERNATIVE COLLECTION OF LOCAL TAXATION

EMCC felt that there is some efficiency to be uncovered from investigating whether cost of setting up new collection procedures in 600-plus District Councils would undermine the intrinsic advantages of an alternative local taxation measure through excessive cost. Given that the Local Income Tax and Local Indirect Tax suggestions are modelled on existing national taxation systems, could giving responsibility for collection to Revenue & Excise speed up implementation and contain costs, whilst maintaining the Local Authority role of providing and maintaining the relevant tax registers?

employees in some way exercise the demand for democratic accountability for their employer are often baseless, since their place of work may not be in the same electoral ward or even the same authority.

EMCC believes that maintaining the present NNDR arrangement allocates accountability where business trust is best placed. However, NNDR payers still do not enjoy "consumer" protection for the services provided by Local Authorities of the kind that we would expect from private service contracts.

Measures to address the ways to protect local economies through NNDR relief for struggling companies represent risks. EMCC would urge that a more supportive policy could help, at very little additional risk. The LAGBI proposals are well intended, but the complex measures to prevent "inefficient" authorities from being granted these freedoms may kill the incentive to attract inward investors to where they are most needed. Failing local economies need every incentive to redress their plight, without being punished for their desperation.

EMCC believes that the Revenue & Excise could be a more efficient alternative collector of NNDR and any new local taxes, and would urge that this option should be explored further in this Inquiry.

7. RECOMMENDATIONS

1. Leave the NNDR in place, and retain the setting of the poundage and transitional arrangements under national control.
2. Keep the role of the District Valuation Office.
3. Legislate to enable the Local Authority to give discounts on the NNDR to businesses experiencing financial difficulties and in economically deprived communities, as an incentive to attract new business to invest.
4. Business Improvement Districts – retain this new legislation and further refine and develop the regulations to enable these schemes to proliferate across the country.
5. Review the collection mechanism and utilise the considerable abilities and infrastructure of the newly integrated Revenue & Excise to collect local taxation where this can be shown to be simpler and more cost efficient.

Max Boden
8 December 2004