BUSINESS RATES RETENTION AND POOLING PROPOSAL

Submitted by: **Head of Finance**

Portfolio: **Communications, Transformation and Partnerships; Finance and Budget Management**

Ward(s) affected: **All**

Purpose of the Report

To outline the new arrangements for business rates retention, which replace the current National Non domestic Rates (NNDR) grant element of formula grant, and a proposal to form a business rates pool for Staffordshire.

Recommendations

(a) That Members note the proposed new arrangements.

(b) That Cabinet determine whether Newcastle Borough Council is to participate in the Stoke on Trent and Staffordshire business rates pool.

(c) That, if participation in the pool is approved, the final version of the Memorandum of Understanding is agreed by the Council Leader and the Portfolio Holder for Finance and Budget Management in consultation with the Chief Executive and the Executive Director (Resources and Support Services).

Reasons

A decision is required as to whether to participate in a business rates pool.

1. Background

1.1 Currently business rates are collected by district and unitary councils from business ratepayers each year and this amount is paid to the government and held in a national business rates pool. The government redistributes the total amount of rates in the pool to every local authority in England (including districts, counties, unitary authorities, fire authorities and police authorities) in the form of NNDR Grant included in Formula Grant.

1.2 The Local Government Finance Bill, currently proceeding through Parliament, fundamentally changes the arrangements outlined above. It proposes a business rates retention scheme for local authorities, to commence from 1 April 2013. This will not, however, simply permit local authorities to retain all the money they collect. It will, in principle, allow authorities to retain a share of the amount of year on year growth in the business rates yield or bear part of the cost of a reduction in yield.

1.3 Some of the finer detail relating to the scheme has not yet been finalised or released, so in considering the best way forward your officers have had to make some assumptions based on data available, predictions of data applicable to future periods, emerging views and commentaries by interested parties such as the Local Government Association and financial modelling exercises.

1.4 It is important to understand that there will be no changes in the way that business rates are collected from taxpayers. They will see no difference at all in this regard. The new system relates solely to what happens to the money after it has been collected.

1.5 The new system involves district councils, county councils, unitary authorities and fire authorities. Police authorities are excluded and will have separate funding arrangements to replace the NNDR grant they previously received.

1.6 Appendix A sets out the principles of the business rates retention system showing how it will work in practice. The system which has been devised is a technically complex one, not easily understood or simple to operate. Members are advised to read Appendix A, which has been adapted from the Step by Step Guide to Business Rates Retention published by the Department for Communities and Local Government (DCLG), before considering the rest of this report. In addition, a “Glossary of Terms” in relation to business rates retention is provided at Appendix C for easy reference.

1.7 The proposals allow authorities to operate the scheme entirely on their own or to combine into business rates pools which aggregate the member authorities’ various key figures and calculations integral to the system, treating them as pool amounts. Depending on local circumstances, this could have a number of advantages, whereby the member authorities could be better off than if they acted alone. The rest of this report is concerned with considering whether Newcastle should join such a pool.

2. <u>Principles Relating to Business Rates Pools</u>

2.1 The option of pooling is available to authorities on a voluntary basis. Pools will consist of authorities within a defined geographical area such as within a county or a Local Enterprise Partnership (LEP) area. There must be a clear rationale for the geographic coverage and DCLG can refuse to allow a pool where this is absent. An authority can only be a member of one pool and must participate on a whole authority basis.

2.2 Where a pool is set up, all of the individual amounts, such as baseline funding levels and business rates baseline relating to each participating authority are combined to form a pool amount for those items. All money collected is paid into the pool and all payments to the government, such as for the tariff and the levy, are made out of the pool. Participating authorities receive the amounts due to them as retained business rates from the pool, either wholly or after setting aside a part (the pooled fund) to be used for the overall benefit of all members of the pool. Other payments (funded by the amount set aside) may be made from the pool to authorities, for example to compensate them where they would have received a safety net payment from the government, if not in the pool. The pool may also distribute surplus amounts in other ways, such as setting up funds to assist economic regeneration within the pool area or by directly giving participating authorities a share of any savings made. The precise details of how pools will be governed and operated are up to the participating authorities to decide, subject to operating within the overall framework laid down by the government. There will be legal agreements between the participants setting out how the pool is to operate.

2.3 There will be a “lead authority” which will administer the pool and account for its transactions.

2.4 All authorities will receive individual data from DCLG, whether they are in a pool or not. This, together with data they possess themselves, will enable pooling authorities to establish what their position would have been if they were not in a pool and so assess whether they are benefitting from membership.

2.5 Participating in a pool can be beneficial to authorities, as described below.

2.5.1 Taken individually all Staffordshire district councils will be tariff authorities and will be subject to a levy on the amount of growth in business rates. Staffordshire County Council, Stoke-on-Trent City Council and the Fire Authority will be top-up authorities and therefore will pay no levy. If some or all of the tariff authorities join with the top-up authorities in a pool, the levy formula (see 3.1.7 of Appendix A) will be based on the aggregate of all the authorities' baseline funding levels and business rates baselines, resulting in a lower levy rate. This rate will be applied to the aggregate growth of all the authorities in the pool to calculate the amount of levy payable, which will be a lower amount than the total of all the levy amounts otherwise payable by the districts if they had acted alone.

2.5.2 The benefits to top-up authorities are not so obvious as they would not have paid a levy as individuals so make no savings. However, they can benefit from any funds which may be set aside out of the overall savings and a pool also allows authorities to cooperate together for the overall benefit of the area covered by the pool, for example:

- by investing in measures to improve economic growth,
- allowing investment decisions to support shared priorities,
- contributing to the generation of increased business rates income.

2.6 However, because the eligibility for safety net payments is calculated at a pool wide level this means that participating districts will lose their eligibility for such payments or a much reduced amount would be paid to the pool. This is not a major consideration if districts anticipate or experience growth in the rates yield but would be of concern to a district which expected the income to fall by a significant and prolonged degree.

2.7 Pools must be approved by DCLG, who may attach conditions, if they consider them necessary. There will be an opportunity for proposals to be made each year, for pools to commence the following 1 April. Following receipt of a proposal to form a pool DCLG will consult with interested parties before giving approval by designating the pool. Pooling proposals to commence on 1 April 2013, signed by the Chief Executives and Section 151 Officers of all the participating councils, must be received by DCLG by 9 November 2012. Pools will be designated in November, following which there will be a "cooling-off" period during which any of the authorities can withdraw its intention to participate. If this happens, the whole pooling proposal collapses and no pool can be formed, until the next round of applications in a year's time.

3. <u>Proposed Business Rates Pool for Staffordshire</u>

3.1 Preliminary Work

3.1.1 The Staffordshire Chief Finance Officers Group (SCFOG) has set up a working group of finance officers, chaired by a Chief Finance Officer to report back to them, to consider the feasibility of forming a business rates pool for Staffordshire with all Staffordshire authorities, apart from the Police as members. Since the group was set up, four authorities (Cannock, East Staffs, Lichfield and Tamworth) have decided to participate in other pools, based on LEP areas, so have left the group and will not be part of this proposed pool. However, this does not affect the viability of the proposed pool.

3.1.2 DCLG required non-binding expressions of interest in forming a pool to be sent to them at the end of July and to be confirmed by 10 September. Accordingly a letter, signed by the Chief Executives and Section 151 Officers of all of the Staffordshire authorities which were at that time interested in joining a Staffordshire pool, was sent to DCLG expressing an interest in doing so and a further letter of confirmation was sent in September. This was in order to keep options open since any group of authorities which did not express their interest would be barred from consideration for pooling in 2013/14. The authorities are not in any way bound by this expression of interest, which was for the purposes of indicating the level of interest in pooling to the DCLG. It is understood that around 30 expressions of interest from around the country have been submitted.

3.1.3 The group has met frequently to deliberate upon the issues concerned and has concluded following examination of the principles and governance issues involved, data available and financial modelling that a pool would be a viable proposition. As a result a draft proposal for a “Stoke-on-Trent and Staffordshire Pool” has been developed.

3.1.4 A draft Memorandum of Understanding setting out the main provisions of the proposed pool agreement has been drawn up. The Draft Memorandum of Understanding is reproduced at Appendix B and is discussed in the following three sections together with any issues arising.

3.2 <u>Financial Provisions of Proposed Pool</u>

3.2.1 A basic principle of the pool will be that no authority will be worse off by being a member than if they were outside the pool. Authorities will retain the income they would have received, if no pool existed. The Pooled Fund will, therefore, consist of the levy payments that would have been paid to the government, i.e. the levy savings.

3.2.2 The Pooled Fund will be distributed on the following basis:

- 40% to the billing authorities as a local incentive payment based on relative growth performance to maintain an incentive to participate in the pool.
- 40% to be placed in a central investment pot to be used to deliver key projects which will regenerate the local economy within Staffordshire
- 20% to be placed in a contingency reserve to enable the pool to offer a protection mechanism to authorities that would have otherwise received a safety net payment from the government

3.2.3 The protection mechanism will operate as follows:

- If an authority’s business rate income drops by more than the government determined safety net trigger (which will be between 7.5% and 10.5% of its baseline funding level - the final percentage is still to be determined), then the authority will be entitled to receive a safety net payment from the contingency fund.
- All the participants in the fund will agree and approve the amount of a safety net payment. However, the payment will match any safety net payment that would otherwise be made if they were outside the pool.

3.2.4 If in a financial year there are insufficient funds in the contingency reserve to pay the safety net payments, then Staffordshire County Council and Stoke-on-Trent City Council will make a top-up payment to the contingency reserve sufficient to enable safety net payments to be made in full. They will be repaid the top-up amounts the following year. If the top-up requirement continues for two or more consecutive years, they may notify the other authorities that a variation or termination of the pooling agreement is needed. Staffordshire County Council has provisionally agreed to underwrite the fund in this way.

3.2.5 The contingency reserve is to be reviewed annually and if there are excess funds in it these can be distributed to the participating authorities as additional local incentive payments (50%) and paid into the central investment pot (50%), subject to the approval of the pool board.

3.2.6 Surplus pool monies will be invested to earn interest for the benefit of the pool. Some or all of this interest will be added to the central investment pot.

3.3 Governance Arrangements

3.3.1 A Pool Board consisting of the Leaders of each participating authority or their nominee will be responsible for governing the pool. The Board will operate on the principle of one member, one vote, all members being equal, with a quorum of 50% of members. Board meetings are likely to be held quarterly and rotated around authorities, the chair being taken by the host authority. Exact details will be decided at the first meeting at which the Board's terms of reference will be agreed.

3.3.2 The Board will be responsible for determining how the central investment pot will be spent.

3.3.3 Other matters to be dealt with by the Board include:

- Nomination of the lead authority
- Receiving and considering an annual and other reports from the Lead Authority
- Approving the investment strategy
- Reviewing the contingency fund
- Issues relating to members desiring to leave the pool

3.3.4 There will be a Lead Authority, accountable to the Board, which will administer the pool and account for its transactions. The consensus view of the SCFOG group is that this should be either Stoke-on-Trent City Council or Staffordshire County Council, as they have greater capacity to act in this regard. It is probable that the County Council will be the Lead Authority as they have indicated their willingness and already have a relationship with the districts and have already taken the lead in some areas of the preparatory work. It has yet to be determined whether the costs of the Lead Authority incurred on behalf of the pool will be reimbursed from the pool.

3.4 Termination Provisions

3.4.1 Membership of the pool is on a voluntary basis and all members of the pool will be able to leave the pool if they choose to.

3.4.2 It is intended that the pool agreement will remain in place until 2020 (which is the earliest date that DCLG is likely to reset the rates retention system) with membership being looked on as a long term commitment. However, it may be necessary to review membership on an annual basis if a material contraction in business rates is envisaged to ensure no member should be worse off as compared to whether they had pooled or not.

3.4.3 If any of the members leave the pool it will be necessary to apply to DCLG for redesignation of the pool, with a reduced membership. The agreement will, therefore, contain provisions relating to the period of notice which must be given by authorities wishing to leave in order to allow time to make application for the pool to continue the following year.

3.4.4 If an authority leaves the pool this could result in some cost being incurred by the pool or lead to the levy savings being reduced, thereby affecting the remaining members. Accordingly, the agreement may contain disincentives to leave the pool, related to the cost to the remaining members, for example requiring repayment of all or part of the local incentive payments made in the final year of membership.

3.4.5 In some cases it may be advantageous, both to a particular member authority and to the pool as a whole if that authority was to leave the pool. This might occur where the authority appeared likely to suffer a period of contraction in its business rates income. There will, therefore, be a "friendly leavers" clause in the agreement to permit authorities to leave in these circumstances, without penalty, which would allow it to take advantage of the safety net payments from the government, whilst not reducing the levy savings made by the pool, to the benefit of the remaining members.

3.5 Other Issues

3.5.1 Currently each authority will have different policies in relation to discretionary rate relief. In order to be fair to all members of the pool, it will be necessary to "iron out" these differences, either by harmonising the relief policies across the membership or by devising a mechanism to compensate for the variations.

3.6 Further Actions

3.6.1 An application to form a pool has to be made to DCLG by 9 November. Once the identities of all the members of the pool have been established, an application will be made. DCLG designation of the pool is then awaited, which should be received in November.

3.6.2 All of the authorities that are potential participants in the pool need to decide that they will participate before 9 November. Whilst to date most of the deliberations have taken place at officer level, the decision to participate must be taken by members, after they have considered the financial case and any other relevant factors. Accordingly each authority is taking action to obtain approval to membership hence the compilation of this report for your consideration.

3.6.3 Authorities will be able to withdraw their interest in participating in the pool during a cooling off period (probably December to January). The finance settlement figures should be received from the government during this period which might influence some authorities to reconsider their earlier decision to participate. If an authority does withdraw, the whole pooling proposal collapses and no pool can be formed, until the next round of applications in a year's time. It is important therefore that the decisions to participate are based on a firm commitment to do so. If there is any doubt about participation it would be better if the authority concerned decided not to participate at this stage so as to avoid potential collapse of the pooling proposal if they later withdrew.

3.6.4 A formal agreement will be drawn up and agreed and signed by all of the pooling authorities. The pool will then be able to commence operation on 1 April 2013.

4. Proposal

4.1 That the Council participate in the Stoke-on-Trent and Staffordshire Business Rates Pool.

5. Reasons for Preferred Solution

5.1 The Council is likely to benefit from membership of the pool, as outlined elsewhere in this report.

6. Legal and Statutory Implications

6.1 Powers to form business rates pools will be contained in the Local Government Finance Act once it has been enacted.

7. Financial and Resource Implications

7.1 The pool is intended to operate on a "no loss" basis so that no authority is worse off than if it stayed out of the pool. If this proves to be the case (and the pool agreement is designed so that this happens) then there will be no detrimental effect upon the Borough Council. If the Council experienced exceptional growth in its business rates income this would have to be shared with the other members of the pool, via the levy savings but such a scenario seems unlikely at the present time.

7.2 The likely amount of the benefit to be gained from pool membership cannot be reliably quantified at present owing to insufficient data being available and full details of the rates retention system still to be decided by the government. Some financial modelling has been carried out, particularly using a Society of County Councils model but this still suffers from these data deficiencies and lack of final system detail. However, it would be reasonable to envisage that savings will arise in the pool as a whole in the first year, which will increase in subsequent years, provided growth is experienced across the pool area. 40% of this would be shared amongst the pool members as incentive payments, 40% paid into the investment pot and 20% paid into the pool contingency reserve.

8. Major Risks

8.1 The pool has been designed, particularly through the "no loss" principle to minimise the risk to its members. Most of the "risk" is that members might not be as well off in the pool as outside it rather than that they suffer as a result of membership.

8.2 There is a risk that the Council might incur costs, if it decided to leave the pool. A firm commitment to membership would mitigate this.

9. List of Appendices

Appendix A - Outline of the new arrangements for business rates retention
Appendix B - Draft Memorandum of Understanding
Appendix C - Glossary of Terms

10. Background Papers

Various technical consultation and explanatory documents published by DCLG in relation to business rates retention