Agenda Item No.

Southend-on-Sea Borough Council

Report of Corporate Director Support Services

to

Cabinet

on

6th November 2012

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Business Rates Retention Scheme

Economic and Environmental Scrutiny Committee
Executive Councillor: Councillor Nigel Holdcroft

A Part 1 Public Agenda Item

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1. Purpose of Report

To update Members on both:

- The proposed changes for Business Rates funding as part of the Government's review of funding for Local Government.
- The outcome of the recent Government consultation on business rates retention.

2. Recommendation

That Members note the details of the current position relating to the introduction of the business rates retention scheme and the implications this will have for Government Funding for the Council from April 2013.

3. Background

3.1 Councils currently receive their funding from three main sources:

- Grants from central government;
- Council tax;
- Other locally generated income (such as from fees and charges from chargeable services).

3.2 A core funding source of the 'formula grant' that councils receive from central government is redistributed business rates.

3.3 Currently, business rates are collected by local authorities from businesses in their areas and then paid into a national ‘pool’ for redistribution around the country, based on councils’ local service/ spending needs. Councils do not, therefore, currently receive the business rates receipts paid by businesses in their local area. Instead, business rates revenue is managed at the national level to equalise local council funding and the service needs of local communities. For 2011/12 in Southend we currently pay approx £42.4m into the NNDR (National Non-Domestic Rates) pool but received £48.9m back in redistributed NNDR.

4. Proposed changes from 2013/14

4.1 On 18 July 2011, Government published a consultation paper on proposals for business rates retention for Local Government. The consultation paper set out the intention to reform the local government finance system to give local authorities more control over their finances and an incentive to promote the growth and development of their area.

4.2 The Government response to the consultation was published on the 19 December 2011, followed by 5 technical papers on 17th May 2012.

- The central and local shares of business rates - A Statement of Intent;
- The safety net and levy;
- Renewable Energy Projects - A Statement of Intent;
- Pooling Prospectus;
- The economic benefits of local business rates retention;

4.3 The Government then issued a further 251 page technical consultation on 17th July 2012 for responses from Local Government by 24th September 2012. The Government has yet to respond back to Local Government on this latest technical consultation. The outcome of the various consultations on Business Rates Retention will now feature as part of the new financing arrangements for Local Government from April 2013, with the actual financial effect identified as part of the Local Government Finance settlement in December 2012.

4.4 The Government’s aims for reforming business rates are:

- To build into the local government finance system an incentive for local authorities to promote local growth over the long term.
- To reduce local authorities’ dependency upon central government, by producing as many self-sufficient authorities as possible.
- To maintain a degree of redistribution of resources to ensure that authorities with high need and low tax bases are still able to meet the needs of their areas.
- Protection for businesses and specifically, no increases in locally-imposed taxation without the agreement of local businesses.

<u>The proposals do not include any measures for local authorities to set the business rate levels in their areas – under these proposals, this would remain nationally-set, as at present</u>.

4.5 The Government will continue to set the business rate multiplier nationally.

4.6 The basis of the new Business Rate system is that the Council's spending level in year 1 (2013-14) will be calculated using the "baseline". This baseline will be initially set so that each authority's budget is equivalent to what it would have been under the current system. This baseline funding level will initially be financed by an individual authority business rate baseline, i.e. the amount of locally generated business rates that the authority is allowed to keep. Where Councils have a larger business rates base than the business rate baseline, the Government will take away some of this income as a tariff, and likewise if the business rate base is smaller than the business rate baseline the government will top up the income. The level of tariff and top up will be fixed (they will rise only in line with inflation) to ensure that any growth in business rates that a Council achieves is kept by them. In future years local funding would grow or reduce with future local Business Rate levels. The Government proposes a system of 'clawing back' disproportionate gains through a levy to provide a safety net to Councils whose business rates income falls.

4.7 There are options to enable councils to carry out Tax Increment Financing, which is basically a method of borrowing against the value of future anticipated growth in business rates, and is intended to work as a way of funding infrastructure investments to unlock local economic growth and regeneration.

4.8 There will be no changes to the current system of business rate reliefs, including eligibility. Government have proposed an allowance to cover the central government funding element of discretionary reliefs to ensure that local authorities have sufficient resources to continue to offer this service to current recipients. From 1st April 2012, Local Authorities have had greater scope to award discretionary relief but must meet the full cost themselves, if it is not for charities or non profit making organisations.

5. The Central and Local Shares Of Business Rates - A Statement of Intent

5.1 The statement of intent confirms that the local share will be set at 50 per cent of business rates revenue. The local share will form the baseline for each authority's baseline funding level and tariff and top up amounts. From April 2013, councils will keep all of the growth upon their share, subject to the levy on disproportionate benefit; that is the Council will retain 50% of any increase in its Business Rates revenue subject to an over-riding levy. The converse of this is that the Council will be exposed to any reductions in Business Rate revenue, sustaining 50% of any reduction in revenue, subject to a safety net arrangement.

5.2 The local share will remain fixed at 50 per cent until a reset of the system when the baseline funding levels for each local authority will be reviewed to take account of changes in relative need and resource. The Government does not intend to reset the system until 2020 at the earliest and in the long-term aspires to a 10-year reset period, although the length of the reset period and scope will not be set in regulation.

5.3 The statement also confirms that tariffs and top-ups will be adjusted at each five yearly revaluation so that an authority's retained rates income is not affected.

5.4 The Government has confirmed that, in addition to locally retained business rates, each authority within the scheme will also receive supplementary Revenue Support Grant (RSG) to impose councils' overall share of the spending review control total in any given year.

5.5 The following grants will be rolled into the rates retention system from 2013-14, although the Government has not stated if these will be paid out of the central or the local share:

- Bus Service Operators Grant – London buses element only
- 2011-12 Council Tax Freeze Grant
- Council Tax Support Grant (excluding the amount that will be paid to Local Policing Bodies directly)
- Early Intervention Grant (excluding funding for free early education for two year olds)
- GLA General Grant
- A proportion of GLA Transport grant
- Homelessness Prevention Grant
- A proportion of Lead Local Flood Authorities Grant
- Department of Health Learning Disability and Health Reform Grant
- A proportion of Sustainable Drainage Systems Maintenance Costs Grant

The amount of Revenue Support Grant for 2013-14 and 2014-15 will be set out in the 2013-14 Local Government Finance Report. It is not expected that this will be available until the week beginning 17 December 2012 at the earliest.

5.6 The Government will define in regulations what a billing authority's business rates income is for the purposes of determining the local and central shares. The Government intends that the definition is tied to the business rates payable to the authority, in respect of occupied and empty property, in that year and will take into account the effect of that amount on:

- Mandatory rate reliefs
- Discretionary relief
- Losses on collection
- Hardship relief
- Repayments of refunds in respect of previous years

The precise definition of income and treatment of related issues will be worked through with the Local Government Finance Group and has formed part of the summer consultation between Government and the Local Government Sector.

6. The Safety Net and Levy

6.1 The statement confirms that there will be a safety net to protect local authorities from significant negative shocks to their income, funded by a levy on authorities that experience disproportionate financial benefit from business rates growth.

6.2 The Government proposes to set a proportionate levy, with a 1:1 ratio, meaning that for every 1 per cent increase in business rates base, an authority would see no more than a corresponding 1 per cent increase in income as measured against its spending baseline.

6.3 The regulations will set out that the funds in the levy account cannot be used for any other purpose than to make safety net payments to local authorities, or in the event that the account is left with a surplus, for that surplus to be returned to local authorities.

6.4 The Government proposes to set the safety net threshold in the range of 7.5 per cent to 10 per cent below spending baseline. The final percentage is yet to be decided, but the following illustrates how the Government intends the safety net to work. A 10 per cent safety net threshold would mean that safety net payments would be made to take the authority's income up to 90 per cent of its spending baseline where income had dropped below that level. Final details of how this will work are still awaited from Government.

6.5 The regulations will set out the detailed calculations the Secretary of State will make to determine whether an authority is to make a levy payment or receive a safety net payment. The Government proposes to make these calculations after the end of each financial year on the basis of final outturn data

7. Business Rates Retention Scheme: Pooling Prospectus

7.1 The Government has also released a prospectus that sets out the process for formally designating pools of rate income across a number of councils.

7.2 Local authorities in a pool will be treated as a single body, for the purposes of calculating tariffs, top-ups, levy and safety net payments.

7.3 Pooling arrangements will be voluntary and it would be for pools themselves to decide how to distribute aggregate revenues within the pool. If a pool is dissolved, members of a pool would return to their individual tariff, top-up and levy amounts.

7.4 It will be for local authorities to determine the geographic coverage of a pool, subject to the following requirements:

- There should be a clear rationale for the coverage that is proposed
- Pools should operate on a whole local authority basis, and an authority cannot be a member of more than one pool.
- Authorities will have to nominate one member to act as a lead

7.5 Although discussions have taken place across all of Essex, there is a consensus that the benefit of pooling across authority boundaries is unknown and uncertain. This has arisen due to the late notifications from Government on pooling arrangements and that no final decisions have yet to be made by Government. This has led to an all wide Essex position of not creating a pool for 2013/14.

8. Business Rates Retention Scheme: The Economic Benefits of Local Business Rates Retention

8.1 The government has carried out an exercise, based on results from economic literature, to gauge the likely economic impact of the partial retention of business rates growth

8.2 Across a range of models, the middle-case scenario predicts that, given the 50 per cent local share and seven year reset period, an additional £10.1bn of GDP (Growth Domestic Product) could be created. GDP is the total value of all goods and services produced within a country in a year, minus foreign investments.

8.3 In the lowest-case scenario £1.7bn of GDP is created over 7 years, and in the best-case scenario £19.9bn of GDP is created.

8.4 The government states that the size of the incentive is affected by the size of the local share of business rates, the levy on disproportionate gain, the length of time until the next reset and the tier-split.

8.5 The basis for these estimates is a calculation of the size of the incentive for each billing authority to expand its commercial floor space. Authorities are then grouped into behaviour groups and an appropriately increased growth rate for commercial floor space assumed for each group. A national projection of increased business floor space is then combined with data on the ratio of commercial floor space to GDP to arrive at estimates of the increase in GDP from the incentives provided by business rates retention.

8.6 These government projections of course are just that. There is no certainty that business rate income will grow as predicted; that is dependent upon prevailing economic conditions. However the localisation of business rates does undoubtedly tie the Council's financial future closer to that of the local economy.

9. Business Rates Retention Scheme: Renewable Energy Projects

9.1 The statement confirms the list of qualifying technologies that will be included in the definition of renewable energy projects:

- Onshore wind power
- Offshore wind power
- Hydroelectric power
- Biomass
- Biomass conversion
- Energy from waste combustion
- Anaerobic digestions, landfill and sewage gas
- advanced thermal conversion technologies – gasification and pyrolysis
- Geothermal heat and power
- Photovoltaic's

9.2 Billing Authorities will be responsible for determining which properties should qualify as a renewable energy project – e.g. where it is a new build, or has been converted or expanded and meets the renewable energy definition, or where renewable technologies have been installed with a separate identifiable impact on rateable value.

9.3 In two tier areas, all business rates income will be retained by the local planning authority that is the decision maker for the renewable energy project, whether at county or district level (with certain exceptions or allowances for National Park Authorities and London authorities).

9.4 The regulations will provide that business rates income from such renewable energy projects will be retained in full by the Billing Authority and as such the income will be disregarded from calculations in the rates retention scheme on the central/local share, levy, and re-set of tariff and top-up amounts. The total amount of business rates income resulting from a new renewable energy project will be disregarded.

9.5 The Local Government Finance Bill, currently before Parliament, will provide for the Secretary of State to make regulations to designate classes of hereditaments and for business rates income from those hereditaments to be disregarded from levy calculations in the rates retention scheme. This will provide a mechanism for the Secretary of State to define a renewable energy project, in line with the Government's policy intention

10. Conclusion

10.1 There are a number of factors to consider that pose a risk to the Council. As the local authority will have no say in setting tax rates, and there are no plans for changes to valuation or exemptions and reliefs, the level of control will be very limited. Therefore although the proposals are to encourage growth, the incentives to do so do not adequately encourage this. There is still a high degree of central control, such as setting of parameters for levy mechanism

The proposals are also, even by experienced rating practitioners, seen as very complex.

10.2 There is also potential for significant financial risks to local authorities, especially where growth potential is limited and as the Council has no control over the Valuation Office (VO). Large Rateable Value (RV) amendments can occur that would seriously affect the rates collected. Valuation appeals are currently, and will continue to be, dealt with the Valuation Office (VO). The Local Authority has no way of identifying within the appeals being dealt with or outstanding what are likely to result in a revaluation. There are at any one time several hundred appeals outstanding. For Southend there are currently over 800. Under the new scheme excessive RV decreases could have a serious impact on the Councils income, and this is out of our control. However the Government has recently announced its intention to postpone the next business rates revaluation in England to 2017. Primary legislation will be brought forward through the growth and infrastructure Bill which was laid before Parliament on 18th October 2012.

10.3 The Local Government Association (LGA) is of the opinion that the proposed safety net threshold could leave local authorities exposed to levels of volatility in their income that could have an adverse impact on local services and local residents.

10.4 Although pooling is allowed whereby Authorities can come together to form a pool with scope to generate additional growth in reality there may be a reluctance to enter into an area where the risks are currently unknown.

10.5 As collection of NNDR is proving more difficult with collection rates tending to decline rather than increase in the financial downturn, the risk of non collection to the council’s financial stability under the new scheme will be far higher than under the existing scheme of pooling, and this cannot be fully predicted.

10.6 Finally, as Government proposes to keep a top slice of 50 per cent of business rates for the Treasury, taking taxes paid by local businesses for local services and using them for local services based on national priorities instead this may affect the incentive for growth altogether.

11. Other Options

None as this is the only Government proposed option.

12. Reasons for Recommendations

To apprise members of significant changes to local government financing from 2013/14 and the relative financial risk of these proposals to the Council.

13. Corporate Implications

13.1 Contribution to Council's Vision & Corporate Priorities

To ensure that the full implications of the changes are addressed to assist with the Council's forward financial planning and regeneration plans.

13.2 Financial Implications

The financial implications of these changes should be limited in the first year of operation, given the proposals for top-ups and tariffs to restore base funding to what it would have been prior to the changes. 2013/14 depends far more on the overall financial settlement for local government. This will start to become clear following the Chancellor's Autumn Statement on 5 December 2012, and will be known with greater certainty for individual authorities from the week beginning 17 December 2012.

However under these proposals, the Council will be exposed to volatility in the local business rate environment, both in terms of the growth and decline of the business rates base, and also our ability to collect. This will need to be closely monitored as part of our monthly budget monitoring to help inform the Council's in year financial position to assist planning future years' budgets.

13.3 Legal Implications

The regulations will be within the soon to be enacted Local Government Finance Act 2012

13.4 People Implications

None applicable for the proposals in this report

13.5 Property Implications

See main body of report

13.6 Consultation

There is no statutory requirement for consultation although the Council has been fully involved in consultation with the Government over the proposals.

13.7 Equalities and Diversity Implications

None in relation to the proposals.

13.8 Risk Assessment

Under these proposals, the Council will be exposed to the risk of volatility in the local business rate environment, both in terms of the growth and decline of the business rates base, and also our ability to collect. Growth will represent a financial opportunity, whereas decline will represent a real constraint on the

Council's ability to finance its services. Although the Council has limited levers to secure local economic growth, given that the national and international economy can easily outweigh local conditions, it will be imperative that the Council maximises its intelligence around the local economy so that we get some forewarning of the financial impacts, and subject to other priorities, seeks to maximise business growth within our boundaries where possible.

13.9 Value for Money

There are no specific implications as a result of this report

13.10 Community Safety Implications

There are no specific implications as a result of this report

13.11 Environmental Impact

See body of report, in particular section 9, Renewable Energy Projects.

14. Background Papers

Local Government Finance Business Rates Retention

www.local.odpm.gov.uk/finance/brr/sumcon/index.htm

www.communities.gov.uk/publications/localgovernment/businessratesstepguide

15. Appendices

None