

Part A

Report to: Council

Date of meeting: 16 October 2018

Report of: Director of Finance

Title: Business Rates Pilot for 2019/20

1 Summary

- 1.1 The Government has issued an invitation to apply to become a pilot for 75% Business Rates Retention in 2019-20. The pilot schemes are in advance of a proposed extension of the business rates retention scheme nationally from 50% to 75%. The deadline for applications was 25th September 2018. If successful, the pilot would begin 1st April 2018. The Mayor and Portfolio Holder for Resources and Customer Services have taken a delegated decision to enable Watford to be part of the pilot bid submission, but a Council decision will be required to formally enter the pilot should the bid be successful.
- 1.2 The pilot would need to include all Councils within Hertfordshire and current forecasts, based on last year's modelling, suggest that the County as a whole would gain by £8.4M by becoming a pilot. Agreement will need to be reached as to how to spend this additional money within the County as part of the pilot.
- 1.3 As part of the pilot scheme, local authorities agree to forego RSG grant in 2019-20, this does not impact on Watford Borough Council as it would not receive RSG in 2019-20 in any case. It is recommended that Watford Borough Council agrees to become a business rates pilot for 2019-20, as part of a Hertfordshire business rates pilot bid, subject to final confirmation that the business case shows a positive forecast outcome.
- 1.4 Should a pilot bid be unsuccessful Watford will be included in the business rates pool for 2019-20. This will also bring additional benefits to the Borough.

2 Risks

Nature of risk	Consequence	Suggested Control Measures	Response (treat, tolerate, terminate or transfer)	Risk Rating (combination of severity and likelihood)
Business Rates growth is lower than forecast	Resources would be lower than forecast, due to the way the system works this would hit 2020/21.	Monitor forecast.	Tolerate	4
Safety Net payments maybe higher than the business rates growth	Watford would lose safety net payments that would have otherwise been received.	Risk to be reviewed once Outline Business Case is produced. If the risk is too high then the pilot and/or pool will not progress.	Treat if OBC shows risk higher than expected.	3
Appeals may be higher than the provisions	Resources would be lower than forecast, due to the way the system works this would hit 2020/21.	Monitor forecast and actual appeals settled and received during the year.	Tolerate	4

- 2.1 Business Rate growth is forecast to be buoyant for 2019/20, especially with the Intu extension due to come on line and other known development occurring within the town. The Outline Business Case will set out in more detail the projected benefits and risks and risks will be reviewed at this stage.

3 Recommendations

- 3.1 That approval is given to enter the Business Rates Pilot, or if that bid is not successful the Hertfordshire Business Rates Pool for 2019/20
- 3.2 And that delegated authority is given to the Director of Finance in consultation with the Portfolio Holder for Resources and Customer Services to make the final decision on entering either the Pilot or Pool for 2019/20

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Report approved by: Joanne Wagstaffe, Director of Finance

4 Detailed proposal

- 4.1 On 1 April 2017 the government launched five initial 100% business rates retention pilots in devolution deal areas. These pilots were continued into 2018-/19. At the provisional Local Government Finance Settlement in December 2017, the government announced a further ten 100% business rates retention pilots for the duration of the 2018/19 financial year in local authority areas across England. On-going business rates retention pilots, set to operate for the duration of the 2018-19, will end on 31 March 2019. The Government is inviting these authorities, alongside other authorities in England, to bid to pilot 75% business rates retention in 2019/20.
- 4.2 75% Business Rate Retention is due to be introduced from 2020-21, the current proposals are that the pilot schemes would effectively go a year early and their experience will be used in the design of the final scheme. For two-tier areas, the Government expects the pool to comprise a county council and all of the associated district councils. Proposals will need to set out tier split arrangements of all precepting authorities, including Fire and Rescue authorities.
- 4.3 Experience of having operated a business rate pool in the county means that much of the existing risk mitigation and governance arrangements can be built upon as part of this submission.
- 4.4 Pilot authorities will retain half of the 50% income currently transferred to central government. They will no longer receive RSG and Rural Services grant: instead, this funding will be provided through the additional retained income. Tariffs and top ups will be recalculated to ensure the overall impact is cost neutral. For Watford the Council will not receive RSG for 2019-20 and the Council does not receive any Rural Services grant.
- 4.5 Pilot areas will be expected to operate under the arrangements which are currently in place for safety net payments for pools. However, the safety net threshold will be set at 95% of the baseline funding level instead of the current 92.5%. This is to reflect the additional risk of the proposal.
- 4.6 The benefit comes from the retention of income from growth above baseline – the 50% of growth paid directly to DCLG, and the 50% levy currently paid on districts' share of growth. This growth will all be retained locally.

5 Pilot Proposal

- 5.1 Background to the 2019/20 application
- 5.2 Applications to form a Pilot face a competitive process and may not all be successful. They need to show how they will promote financial sustainability of

local services, and support economic growth. They should also show how they will help MHCLG explore the ways in which 75% retention could work in two tier areas; the impact of different tier splits; and how local authorities might share risk and reward under 75% retention. This reflects the position previously discussed by Cabinet at the same time last year. (The proposal submitted in 2017 for a pilot was not successful; there is therefore a pool currently in operation(Watford is not currently part of the Pool).)

- 5.3 Given the short timescales, the pilots do not include any additional devolution of duties or funding that would need agreement with other government departments. The Pilot is for 2019/20 only, as it is anticipated that the national scheme will be implemented from April 2020.
- 5.4 Under the pilot, authorities will no longer receive Revenue Support Grant (RSG) and Rural Services grant: instead, this funding will be provided through the additional retained income. Top Up and Tariffs (the means by which local rates are transferred to/from authorities to bring income in line with assessed need) will be recalculated to ensure the overall impact is cost neutral.
- 5.5 The Pilot's benefit comes from the local retention of income from growth above baseline, currently split:
- | | |
|-------------------------------|---|
| County Council | 10% |
| District Councils | 40% less half paid as levy to MHCLG = 20% |
| Subtotal – Herts share | 30% |
| MHCLG | 50% + 20% from District levy = 70% |
| Total | 100% |
- 5.6 In a pilot, MHCLG's 20% levy on District's share of growth, plus half of its 50% share of income growth, will be retained locally; in a Pool, a proportion of the 20% levy will be retained.

6 Analysis of business rates in Hertfordshire - current position

- 6.1 Table 1 below shows that, overall, Hertfordshire expects to receive £257.2m of business rates in 2019/20. The current funding mechanism for Councils dictates that tariffs and top-ups are applied. The net impact of this is a tariff of £96.7m – that is, the districts surrender £169.7m of the amounts collected to MHCLG, while £73.1m is received by HCC. The result is local receipts of £160.5m. This is compared with a level of assessed need, calculated as £147.9m. Receipts are therefore £12.6m above needs, and so a levy is applied amounting to £5.0m. Net business rates retained in Hertfordshire under the current 50% retention arrangements are therefore £155.5m. It can be seen that levels of growth vary between Districts.

Table 1: Forecast NNDR Income 2019/20

	NNDR Income £m	Tariff / Top Up £m	Net Income £m	Baseline Need £m	Variance to Baseline Need £m	Levy Due	Safety Net Due	Resulting income
Broxbourne	16.8	(13.4)	3.4	2.3	1.1	(0.550)	-	2.9
Dacorum	26.7	(22.5)	4.2	3.0	1.2	(0.604)	-	3.6
East Hertfordshire	18.6	(15.6)	3.0	2.7	0.3	(0.152)	-	2.8
Hertsmere	19.7	(15.4)	4.3	2.7	1.6	(0.800)	-	3.5
North Hertfordshire	16.5	(12.8)	3.7	2.7	1.0	(0.523)	-	3.2
St Albans	25.4	(23.0)	2.5	2.5	(0.0)	-	-	2.5
Stevenage	18.8	(15.2)	3.7	2.5	1.1	(0.561)	-	3.1
Three Rivers	11.4	(8.6)	2.9	2.0	0.9	(0.446)	-	2.4
Watford	27.8	(23.4)	4.4	2.8	1.638	(0.819)	-	3.6
Welwyn Hatfield	24.0	(20.0)	4.0	2.9	1.2	(0.584)	-	3.4
Hertfordshire	51.4	73.1	124.5	122.0	2.5	-	-	124.5
Total	257.2	(96.7)	160.5	147.9	12.6	(5.038)	-	155.5

7 Estimated benefits of a pilot or pool

- 7.1 The advantage of the pilot is that the retention rate of any growth would increase from 50% to 75%, and the amount of levy taken by MHCLG under the current system (£5m) would be retained locally.
- 7.2 For a business rates pool, half of the levy due from Pool members is retained locally. The Pool mechanism means that optimal gains are made where the tariff paid by member districts matches the top up due to the County Council; this typically limits Hertfordshire Pool membership to 5 districts.
- 7.3 Based on estimated 2019/20 rates income, a Hertfordshire Pool would retain £2.9m of growth, while a business rates Pilot would retain an additional £8.4m, giving a total gain of £11.3m above a “do nothing” option, as shown below. If Hertfordshire do not apply to form a Pilot, or if this application is rejected, then this income will be paid to MHCLG.

Table 2: Estimated Gains from Pilot

		£m
Forecast Resources No Growth		149.9
Plus local Growth after levy	7.5	
Equals Forecast Resources - no Pool		157.4
Plus Forecast Pooling Gains	2.6	
Equals Forecast Resources from Pooling		160.0
Plus Forecast Pilot Gains	8.7	
Equals Forecast Resources		168.7

Shown differently, this can be presented as:

Estimated Gains compared to last year

	2019/20	2018/19
Net growth currently paid to MHCLG	£6.3m	£8.7m
Levies applied to districts	£5.0m	£3.5m
Total gain from the pilot	£11.3m	£12.2m
Less: gain from a pool	£2.9m	£2.8m
Total additional gain from a pilot	£8.4m	£9.4m

- 7.4 The total gain estimated in last year is higher than estimated for this year's application. This is due to a combination of underlying growth in the taxbase offset by the change from 100% to 75% retention.
- 7.5 Should a pilot bid not be unsuccessful, it is expected that the existing business rates pool will continue for 2019-20 and that Watford is will be eligible for the pool as a result of projected business rates growth.

8 Basis of Application

- 8.1 The application for a Hertfordshire pilot for 75% business rates retention has been prepared on very similar grounds to the bid submitted last year. While that bid was unsuccessful, no clear reasons for that have been provided by MHCLG. It is considered that the Hertfordshire bid was at least comparable to the successful bids, and the principals used in the proposed pilot and case made for Hertfordshire

are still valid. Independent advice is being taken on the preparation of the application, as it was in last year, and the advice received is that the application made in last year was a strong one and does not require fundamental change.

- 8.2 A copy of the bid document is included at appendix A in this report. The key points within it are discussed below.
- 8.3 An important element of the bid notes that the composition of the pilot and the pool in Hertfordshire is unusual. A 'normal' application would see the composition of the pilot being 100% of the councils affected in a 'functional economic area', with a large proportion (80%+) also being named as prospective pool members. However, because of the way that the Hertfordshire districts are all net 'tariff' authorities (which is to say, the level of business rates collected is materially higher than the calculated level of required funding for most districts in Hertfordshire), the proposed Hertfordshire pool only includes 50% of the districts.
- 8.4 The proposed bid will highlight this point, because it means that the purpose of the pilot (which is to prepare for the implementation of national policy which will lead to 75% rates retention across the whole country from April 2020) can only really be achieved if Hertfordshire is accepted to be a pilot. Conversely, the gain from being a pool is less both in terms of economic benefit and also in terms of promoting the level of county-wide collaboration that will be required under the new national funding process.
- 8.5 Other aspects of the bid remain largely the same as last year. The key points of the bid therefore focus on
- A commitment to sustaining and improving economic growth in Hertfordshire and use of the gains from either a pilot or a pool to further support this;
 - The strong level of cross-Hertfordshire co-operation already in place between the Hertfordshire councils, and the opportunity the pilot would give to develop that further;
 - A mechanism that provides for cross county investment and a balance between incentivising growth in individual districts and smoothing resource variations across the county; and
 - The fact that Hertfordshire is unusual in the relationship between the composition of a pilot and a pool and that a much greater economic and strategic benefit will arise from being made a pilot.

9 Proposed allocation of gains

- 9.1 Chief Finance Officers from the ten Hertfordshire Districts and the County Council have considered the invitation to Pilot, and have agreed that an application could benefit all authorities within Hertfordshire. All eleven authorities are therefore

seeking formal approval through their relevant governance processes to confirm that each authority is supportive of an application for Hertfordshire.

- 9.2 Whilst there are any number of potential methods to apportion any gains from a pilot, the proposal that has emerged from engagement with CFOs comprises the following three steps, which are unchanged from the application made 12 months ago (at that time the principles underlying these three steps were discussed in detail by Chief Executives and Chief Finance Officers):

Step 1

- 9.3 To use gains to meet any safety net liability, and to bring all authorities to the position they would have been had they been acting individually, or in a Business Rates Pool;
- 9.4 Under step 1, gains will be allocated in the following order:
- Pay any safety net that would be met by MHCLG if outside the Pool (not applicable in the current year application)
 - Pay all districts with business rates growth the levy they would have retained had they been in a Pool (based on the 16/17 Pool mechanism, as used in last year's bid)
 - Pay the County Council the levy gain they would have received if districts were pooled
 - Bring any districts with negative growth up to baseline, to provide financial stability.

- 9.5 This leaves £7m to be allocated in steps 2 and 3.

Step 2

- 9.6 A proportion of the central gains to be allocated to a central Investment Fund for One Public Estate (OPE) or similar purposes. It is proposed that one third of central gains be held in this fund.

Step 3

- 9.7 The balance would then be allocated across all members. It is proposed that this is allocated based on a combination of baseline funding (as a measure of each authority's need) and growth (to retain an incentive to promote growth) The table below shows the results of an allocation based on 30% baseline funding and 70% growth.

Table 3: Allocation of Pilot and Pool Gains

	Forecast Resources - no Pool	Gains - 5 District Pool	Bring all to optimum pool	Allocate Balance	Total Income with Pilot
Broxbourne	2.9	0.4		0.4	3.7
Dacorum	3.6	-	0.5	0.5	4.5
East Hertfordshire	2.8	-	0.1	0.2	3.2
Hertsmere	3.5	0.6		0.5	4.6
North Hertfordshire	3.2	0.4		0.4	4.0
St Albans	2.5	-	0.0	0.1	2.6
Stevenage	3.1	0.4		0.4	3.9
Three Rivers	2.4	0.3		0.3	3.1
Watford	3.6	-	0.6	0.6	4.8
Welwyn Hatfield	3.4	-	0.4	0.4	4.3
Hertfordshire	126.4	0.5		0.8	127.7
Growth Fund	-	-		2.3	2.3
Total	157.4	2.6	1.6	7.0	168.7

10 Proposed use of gains

- 10.1 All Hertfordshire authorities will be able to bid for gains held in the Growth Fund. It is proposed that this be based on the criteria used by the Hertfordshire Property Partnership, and may include bids received under One Public Estate for which there has been insufficient funding to take forward. These may provide examples of potential schemes, to be included in the business case; but it is not proposed to commit to specific schemes in our application.
- 10.2 It is proposed that second tranche gains allocated to individual authorities be used at local discretion, for projects that economic growth or financial sustainability (bearing in mind that this will be one off funding). Our application will need to include examples of potential projects: District suggestions include provision for homelessness and town centre regeneration, and invest to save projects.

11 Allocation of Losses

- 11.1 The governance arrangements will also need to provide a mechanism for the allocation of any loss. It is anticipated that this be shared pro rata to the resources each authority would have received had it been acting individually ie in proportion to baseline funding (assessed need) plus any growth/ loss of income. However, as set out above, it is considered that the risk of this scenario occurring is low. Further, by being part of a pilot, the 'safety net' threshold is increased (which means that the total loss required before the safety net mechanism is activated to prevent available funding falling below that level), reducing the overall risk to the members of the pilot.

12 Risks

- 12.1 The figures in section 4.3 are estimates based on recent financial modelling and latest information from Hertfordshire Districts. The financial modelling predicts receipts due for the period April 2019 – March 2020, and benefits may be higher or lower. The main risk is from a significant drop in income for one or more

authorities, which could be caused by business relocations away from Hertfordshire, unanticipated increases in the number of appeals by businesses against their rates determinations, or a significant increase in the number of such appeals that are successful.

- 12.2 The government currently provides some protection via “safety net”. With a Pilot or Pool, safety net payments have to be made by the other members, reducing or removing any gains. As set out in section 4.7, any safety net would initially be offset against the forecast £8.4m gains, but above this it would be met from the growth currently retained. Forecasts show that individual districts’ income would need to fall by between 1% and 10% to trigger a safety net payment. However a significant fall would be required for this safety net to completely offset the £8.4m gain: for example, St Albans, the district closes to safety net, would need to experience a 33% loss of income.
- 12.3 MHCLG provides pilots with a safety net that guarantees that total income will not fall by more than 5% of baseline funding. For Hertfordshire, this gives a minimum income of £142.4m compared with the £168.7m expected on current estimates, and the £157.4m projected if authorities acted individually. It must be noted that our position against these estimates would worsen with or without a Pilot, should income fall.
- 12.4 Current Pilots have a “no detriment” clause – a guarantee that authorities will not be in a worse position than if they were operating as a Pool, or individually. For this round of applications, this guarantee is not being offered. (Initially this was not offered last year, but the provision was re-introduced by MHCLG late in the process.) This absence of a ‘no detriment’ provision does make the agreement of a pilot potentially more risky, and MHCLG have therefore set the ‘safety net’ threshold higher (95% rather than the normal 92.5%).
- 12.5 Members should be aware that the estimates set out in this report have been reviewed several times to achieve a prudent position with a fairly cautious estimate of gains. However the forecasts do include some element of estimated growth, so there is potential for actual receipts to be lower as well as higher. However, whichever application is successful, the estimates indicate a significant net benefit to Hertfordshire and to HCC compared to not being part of either a pilot or a pool.

13 Business Rates Pool

- 13.1 In the event that a Pilot application is unsuccessful, MHCLG have invited authorities to submit applications to form Business Rates Pools at the same time as applying for a Pilot. Under the MHCLG mechanism, the optimum number of pool members is limited, as levy becomes payable by the pool where the total district tariff exceeds the ‘top up’ amount payable to the County Council. Using the previous methodology to determine membership that retains greatest growth in the county, the optimal Pool comprises HCC and the following five districts:

Broxbourne, Hertsmere, North Herts, Three Rivers and Watford. As in the current Pool, 15% of the Pool gains will be set aside in a Growth Fund available for allocation across all Hertfordshire districts.

- 13.2 Hertfordshire is unusual in this respect, that the members of the proposed pilot and those of the proposed pool are quite different (in other areas there is more consistency between these groups). As noted above, this is used as a supporting reason for our pilot application in the bid, as the experience of the pilot will help Hertfordshire councils prepare for the national rates retention scheme ahead of time, while the pool would deny us that opportunity.

14 Implications

14.1 Financial

- 14.1.1 The Shared Director of Finance comments that Medium Term Financial Plan 2018-2021 currently includes income in relation to Business Rates. The Plan only includes the base income for Business Rates, no growth is currently included. Any changes to these figures will be included in the 2019-2022 Medium Term Financial Plan.

14.2 Legal Issues (Monitoring Officer)

- 14.2.1 The Head of Democracy and Governance comments that the legal implications are contained within the body of the report.

14.3 Equalities, Human Rights and Data Protection

- 14.3.1 Having had regard to the council's obligations under s149, it is considered that there are no equalities or human rights implications.
- 14.3.2 Having had regard to the council's obligations under the General Data Protection Regulation (GDPR) 2018, it is considered that officers are not required to undertake a Data Processing Impact Assessment (DPIA) for this report.

14.4 Staffing

- 14.4.1 There are no staffing implications.

14.5 Accommodation

- 14.5.1 There are no accommodation implications

14.6 Community Safety/Crime and Disorder

- 14.6.1 There are no community safety/crime and disorder implications.

14.7 Sustainability

- 14.7.1 There are no sustainability implications.

Appendices

- Business Rates Pilot Submission.

Background papers

- No papers were used in the preparation of this report.