

CABINET

THURSDAY, 6TH SEPTEMBER 2018

REPORT OF THE PORTFOLIO HOLDER FOR ASSETS AND FINANCE

STAFFORDSHIRE PILOT FOR BUSINESS RATES RETENTION IN 2019/20

PURPOSE

- 1.1 To update members on the implications of the 75% Business Rates Retention pilots proposed for 2019/20.
- 1.2 To seek approval to submit an Expression of Interest to pilot 75% Business Rates Retention in 2019/20.

RECOMMENDATIONS

Cabinet are recommended to:

- 2.1 To note the changes to the criteria to be a pilot in 2019/20.
- 2.2 Delegate approval for the Executive Director Finance (Section 151 Officer), in consultation with the Leader of the Council and the Chief Executive, to agree, in conjunction with the other eleven authorities of the proposed pilot, the detail of the 2019/20 application.

EXECUTIVE SUMMARY

- 3.1 An invitation to pilot 75% Business Rates retention in 2019/20 was published on the 24 July 2018. The invitation applies to new pilot applications together with the ten pilots that were formed as part of the 2018/19 Local Government Finance Settlement. The 2019/20 pilots being governed by the 2019/20 Prospectus.
- 3.2 Cabinet at its meeting on the 19th October 2017 approved the submission of an Expression of Interest to be a pilot in 2018/19. The Expression of Interest related to all eleven of the authorities within Staffordshire notably the County; City; 8 Districts/Boroughs and the Fire and Rescue Service. The 2018/19 process involved 26 applications and although the Staffordshire and Stoke on Trent Application met all of the selection criteria the affordability envelope of Government limited the programme to only 10 pilots.
- 3.3 The principles and governance arrangements as agreed for the 2018/19 application have been replicated in determining and evaluating the 2019/20 prospectus. Two major changes arise in the 2019/20 prospectus notably that the government will retain 25% of business rates growth resulting in a 75% pilot scheme, rather than 100% as at present, and a "No Detriment Clause" will not be in place for 2019/20.

- 3.4 A 75% scheme is less rewarding than a 100% scheme however following clarification of the treatment of Business Rates Section 31 Grants the actual financial business case is as strong as that of the 2018/19 application considered for Staffordshire. **The potential “windfall” for Staffordshire for 2019/20, based upon the 75% prospectus, is estimated to be £13.265 million.**
- 3.5 The Local Government sector is currently subject to a claim in relation to mandatory business rates relief, backdated for 6 years, from NHS Foundation Trusts. This would appear to be the material issue in relation to the “No Detriment” clause not being available. However, it is now likely that if any potential liability arises it will be determined and more importantly accounted for in 2018/19 rather than the pilot year. Nevertheless representations will be made directly to the Ministry of Housing, Communities and Local Government (MHCLG) and via the Local Government Association that any such issues arising from changes in policy/legislation and legal interpretation are dealt with equitably between ongoing pilots and new pilots created in 2019/20 as well as the overall Local Government sector.
- 3.6 Subject to the considerations in paragraph 3.5, the experiences to date of the respective Business Rates Pools in Staffordshire, there being no apparent call on the “No Detriment” clause by other pilots, together with the £13.265 million loss / trigger point, it is considered the reward from a pilot greatly outweighs the risk of a “No Detriment” clause not applying.
- 3.7 The requirements to be a pilot and the proposed Governance arrangements of the Staffordshire and Stoke on Trent Business Rates Pool are in accordance with those approved by Cabinet in considering the 2018/19 application. The only change is amending the tier splits to reflect a 75% scheme rather than 100%.
- 3.8 District / Borough tier splits remain as at present with the additional allocation being passported to upper tier authorities. Each authority is guaranteed a minimum of £200,000 additional retention from the scheme whereas risks will be managed on a “No loss”, as compared to existing arrangements, at individual authority level.
- 3.9 “No loss” is determined to be that a Member will be no worse off:
- by being a Member of the Pool than they would have been if they had not been a Member of the Pool. Each Member will retain the income they would have received if they were not a member of the Pool.
 - No Member will be worse off as compared with previous pool arrangements for Staffordshire and Stoke on Trent Business rates Pool (2012) or Greater Birmingham and Solihull Business Rates Pool.
 - **No Member will be worse off as a result of the increased retained % arising from the Pilot Scheme.**

- 3.10 The Pilot governance arrangements will enable authorities to retain effective membership of other LEP'S via contributions to virtual Business Rate pools etc. The continuation of 100% Business Rates for Devolved areas will ensure that, for 2019/20 at least, membership of more than one pool will remain and hence the ability to stay in a pool whether the application is successful or not will remain in place. The application will, as in 2018/19, contain details of each authority's pooling requirements if the application is again unsuccessful.
- 3.11 The deadline for submission of an Expression of Interest is 25 September 2018. The process requires the Section 151 Officer of each member of the pool to confirm that "it fully supports the application and the proposed pooling arrangements".
- 3.12 MHCLG have indicated that the number of pilots may be less than in 2018/19 (such pilots having to re-apply to be a pilot under the 2019/20 prospectus conditions) since there are now fewer issues to test via pilots. The process is likely to be very competitive and combined with the tight deadline for applications delegated authority is requested to submit and agree the details of the application.

OPTIONS CONSIDERED

- 3.13 As outlined within the report.

RESOURCE IMPLICATIONS

- 3.14 The financial implications of a Business Rates Pilot have been discussed within the report.

In accordance with the locally agreed "No Detriment" Clause the Council will not only receive the same level of resources as determined by the current 50% Business Rates retention Regime but also additional resources of £373k are envisaged for 2019/20 reflecting this Council's share of the previous 25% growth passed to Central Government. It is proposed that this additional resource is initially treated as windfall income until decisions are made whether the pilot scheme is extended.

LEGAL/RISK IMPLICATIONS BACKGROUND

- 3.15 The Risk Management Implications of pooling arrangements for the proposed pilot have been referred to throughout the report but can be summarised as follows.

The pooling of Business Rates under pilot arrangements enables a greater proportion of Business Rates to be retained by Authorities by retaining the Government's share of growth achieved within the pooled area. An equivalent risk exists whereby the Council would be responsible for the Government's share if business rates contracted below the current level of business rates.

There are a large number of risks that already exist in relation to Business Rates Retention however the greatest risk is in relation to the level of appeals.

The proposed pool would potential be subject a material detriment dependent upon the outcome of the NHS Foundation claim to be treated as a Charity and claim mandatory relief for six years.

In the context of the Pilot Business Case any potential liability is likely to be determined and accounted for in 2018/19.

Further clarification in relation to how the pilot will test other aspects of the appeal system etc. are being sought from MHCLG.

SUSTAINABILITY IMPLICATIONS

3.16 None.

BACKGROUND

- 4.1 Cabinet at its meeting of 19th October 2017 approved the submission of an Expression of Interest to pilot 100% Business Rates Retention in 2018/19.
- 4.2 The Expression of Interest related to a new Staffordshire and Stoke on Trent Business Rates Pool consisting of the County Council; Stoke on Trent City Council, all 8 District /Borough Councils and the Staffordshire and Stoke on Trent Fire Service. The report highlighted the Financial Business Case for the Expression of Interest together with the proposed Governance arrangements (Memorandum of Understanding) for the proposed new business rates pool.
- 4.3 The outcome of the pilot application was announced in December 2017, as part of the 2018/19 Provisional Local Government Settlement, with 10 new pilots being selected. In total 26 applications had been submitted and although the Department for Communities and Local Government considered that all applications had met the criteria the key overriding factor in determining pilots was affordability and a programme was constructed that “covered a wide spread of geographical areas across England; focussed on rural authorities; and contained authorities with a variety of different rates bases” within the financial envelope available.
- 4.4 The 2018/19 announcement stated further pilots would be created in 2019/20 and a pilot prospectus (see **Appendix 1**) was issued on the 24 July entitled “Invitation to pilot 75% Business Rates Retention in 2019/20”.

2019/20 Business Rates Pilots

4.5 The Invitation contains two major changes in relation to Piloting Business Rates Retention in 2019/20, as compared to 2018/19, notably:

- Piloting a 75% scheme;
- No Detriment not applying.

In addition the application process is likely to be more competitive than in 2018/19 with the new pilots established in 2018/19, excluding London, being terminated and the affordability envelope potentially reduced. Separate discussions are taking place with the London Pilot and the Pilots created in 2017/18 in relation to devolution areas.

4.6 The 2019/20 Invitation relates to piloting a 75% Business Rates scheme as compared to the 100% in 2018/19. The original intention of Business Rates reform was to enable Local Government to retain 100% Business Rates from 2019/20, however, following the last General Election the new Parliamentary timetable prevented the necessary legislation being in place. The Government although approving 100% Business Rates Pilots as part of the 2018/19 settlement announced that 2020/21 would see a 75% Business Rates Retention scheme being introduced combined with Fair Funding determined baselines and a the first Reset of the growth arising from the current Business Rates Retention scheme.

4.7 A 75% scheme by its nature means that a local authority or pilot, in this instance, would be able to retain 75% of future growth, as compared to the current 50%, together with a “windfall” representing the government share of underlying growth achieved at the date of creation of the pilot (in this case representing 25% of growth achieved by the 31 March 2019). The impact of a 75% scheme is discussed in more detail in Section 5 however it should be noted that the financial gain from a Pilot is still material.

4.8 The prospectus contains the majority of conditions as per previous pilots notably:

- To be accepted as a new pilot for 2019/20 all parties must be designated as a pool to share business rates income (paragraph 2.4 of the prospectus). **Authorities cannot be members of two pools** (paragraph 4.3);
- The 2018/19 pilot programme will last for one year only (Paragraph 7.4);
- No additional responsibilities are indicated within the prospectus with only Revenue Support Grant (RSG) and Rural Services Grant funding streams to be directly funded from Business Rates (paragraph 1.4).

4.9 However, new pilots will not be subject to a “No Detriment” policy. This was proposed as part of the 2018/19 prospectus but rescinded following representations from the Local Government Association.

The new prospectus states that “As the pilots are testing the pooled authorities” approach to risk, the government has agreed that a ‘no detriment’ clause will not be applied to the 2019/20 pilots. Instead, selected areas will test a 95% safety net to reflect increased risk in the proposed increased business rates retention system. Applying a “no detriment” clause to the pilots would not be reflective of the reformed business rates retention system that the government aims to introduce in 2020/21”.

- 4.10 The 2019/20 process is likely to be as competitive as in 2018/19 with the ten pilots created in 2018/19 being required to apply to become a 75% pilot governed by the 2019/20 Prospectus. In addition Government have indicated that the 2019/20 pilot programme may be smaller than in 2018/19 since there are fewer issues to test before 2020/21. However, this is slightly contradictory since (a) the 2018/19 Programme was curtailed due to affordability and a 75% scheme will double the affordability envelope; (b) a 75% scheme is now being tested and (c) a no detriment clause will not now apply, both now being tested for the first time.

Updated Business Case for a Pilot - Evaluation of Risks and Benefits

- 5.1 The evaluation of the risks and benefits of the Business Case for a pilot were contained in detail in the report to Cabinet in October 2017. The impact of the changes arising from the 2019/20 Invitation can be summarised as follows:

Financial Benefit

- 5.2 The potential “windfall” for Staffordshire for 2019/20, based upon the 75% scheme, is estimated to be £13.265 million and is in line with the Business Case approved by each authority in 2017.
- 5.3 In essence, the 75% scheme is less favourable than the 100% pilots, however, the potential loss has been more than offset by confirmation of the treatment of Section 31 Grants in relation to Small Business Rates Relief etc.

The Business Case in October 2017 at £12.635 million represented the worst case scenario, however, confirmation was received in advance of the final application that grants would be increased to reflect the 100% scheme. To set the Business Case in context a 100% pilot would have generated a windfall of £26.5 million.

- 5.4 The £13.265 million potential windfall of the 75% scheme is solely based upon the pool retaining the additional proportion of the Central Share (currently paid to Government) and Section 31 grants being paid in accordance with a 75% scheme. No account has been made at this stage for any new growth in 2019/20.

No Detriment - Pilot Area

- 5.5 All existing pilots have been created on a no detriment basis. The “no detriment” provision ensures that **collectively** the authorities in the pilot are no worse-off than if they had remained in the existing 50% scheme. In particular the agreement ensures that if new burdens arise or the assumptions in relation to the funding stream change, then the Pilot Area is protected.
- 5.6 No detriment will however not apply for the pilot or pool for 2019/20 although protection is provided at an authority level via the proposed internal governance arrangements for the Staffordshire and Stoke on Trent Pool.
- 5.7 In considering the “No Detriment” requirement a key factor is whether the reward of retaining 75% growth outweighs the risk. “No detriment” as applied to existing pilots would only apply if the proceeds from the scheme were less than the 50% scheme and if the cost of additional responsibilities were greater than the resource required. In accordance with the prospectus no additional responsibilities are to be transferred.
- 5.8 All authorities currently manage the risk in volatility of business rates by being a member of a Business Rates pool. The respective governance arrangements share the risk and reward on the basis that no authority will be worse off as compared to not being part of a pool. In accordance with the 2019/20 Prospectus 25% of the risk /reward will remain with Central Government and due to the scale of the windfall Business Rates would need to contract by in excess of £13million or 7% for a detriment issue to even apply.
- 5.9 As highlighted in the 2017 report two key risks exist in relation to pooling without a “No detriment” clause:
- A major Business Closes in the Area;
 - The level of Appeals exceeds Governments expectation / provision made by each authority.
- 5.10 The diverse nature of Businesses in Staffordshire combined with the operation of the scheme to date indicates that it is very unlikely that the closure of a business etc. will be a material factor in relation to the lack of a no detriment clause.
- 5.11 The greatest risk in relation to the non-existence of a “No Detriment” clause is the level of appeals. The initial business case in 2017 indicated that although the pool would be willing to accept the risk of volatility, due to changes in circumstances and its share of appeals, it is unwilling to become a pilot unless a “No detriment” clause applies for the loss of business rates income due to:
- The consolidation of hereditaments as a single assessment;
 - Transfer from the Local Rating List/Central Rating Lists;
 - Changes in Mandatory Relief Policy Charitable Status;

- Changes in the basis of determining the basis of Rateable Values;
- The backdated cost of new appeals post 1 April 2018.

- 5.12 A review of the proposals for the design of the new system to date indicates that the majority of such issues will be addressed in the new system and hence the pilot. Clarification will be sought from MHCLG to confirm that the pilot will operate / test such measures and hence it is the Mandatory Rate Relief for NHS Foundations issue that remains unresolved.
- 5.13 The impact of any such change in the determination of 80% relief for such organisations would undoubtedly create a situation which would completely negate the financial business case and hence on face value would be a caveat that would need to be included in any application. The claim for charitable status is being defended collectively via the LGA and following clear Counsel Advice has been refuted but nevertheless is being tested in the high Court arena. Nevertheless, and at the same time acknowledging that such a liability could not in any event be met by the Local Government Sector, the actual timeline for determination of the claim will be known this Autumn, and hence any potential liability would be accounted for in the current year as part of the current business rates regime.

The Proposal for a 2019/20 Staffordshire Pilot

- 6.1 In accordance with the principles agreed as part of the Financial Business Case for 2018/19 the additional resources generated via the windfall would be distributed on a 59/40/1 basis for the two tier structure (County/District /Fire) and 99/1 distribution for the Unitary/Fire authority arrangement. Each authority is, however, guaranteed a minimum £200,000 of the windfall allocation.
- 6.2 The tier splits which determine the distribution of new growth generated with effect from 1 April 2020 have been amended to reflect the change to a 75% scheme as follows:

Table A: Potential Tier Splits 75% Scheme			
Two Tier Authorities	(50% Scheme)	100% Scheme Windfall	75% Scheme
Central Government			25%
Staffordshire County Council	9%	59%	34%
Staffordshire Fire and Rescue Service	1%	1%	1%
District /Borough Councils	40%	40%	40%
Unitary Authority	(50% Scheme)	2018 Pool	2018 Pool
Central Government			25%
Stoke on Trent City Council	49%	99%	74%
Staffordshire Fire and Rescue Service	1%	1%	1%

6.3 The potential distribution of the windfall for 2019/20 based upon Business Rates estimates submitted to Government for the current year would be as follows:

Table B: 2018/19 Windfall as per 75% Pilot			
		75% pilot	
Authority		Revised Additional Growth Retained	Distribution
		£'000	£'000
Stoke on Trent		4,171	4,213
Cannock Chase		914	453
East Staffs		428	212
Lichfield		1,159	575
Newcastle under Lyme		488	242
South Staffordshire		878	435
Stafford		1,915	950
Staffordshire Moorlands		674	334
Tamworth		752	373
Staffordshire County Council		1,618	5,274
Staffs Fire and Rescue		265	200
		13,262	13,262

Governance Arrangements

- 7.1 The Draft Governance arrangements for the proposed pool are attached as **APPENDIX 2** in the form of a Memorandum of Understanding. The arrangements reflect the Governance arrangements as per the 2018/19 application and changes arising from a 75% scheme are annotated via “tracked changes”.
- 7.2 The Governance arrangements reflect the Membership of the Pool; Duration; Governance and Voting Rights; Amounts to be pooled and Distribution methodology; Safety Net; Accountable Body and Termination.
- 7.3 As stated with the 2018/19 application arrangements are in place to ensure that the Pool will be based upon a “No Loss” basis for each Member.

“No loss” is determined to be that a Member will be no worse off:

- by being a Member of the Pool than they would have been if they had not been a Member of the Pool. Each Member will retain the income they would have received if they were not a member of the Pool.

- No Member will be worse off as compared with previous pool arrangements for Staffordshire and Stoke on Trent Business rates Pool (2012) or Greater Birmingham and Solihull Business Rates Pool.
- **No Member will be worse off as a result of the increased retained % arising from the Pilot Scheme.**

7.4 Similarly the sovereignty and individual funding allocations for each authority will be maintained. The amount of core funding for each authority in any potential pilot will still be separately identified as part of the Local Government Settlement. Each authority will receive their allocated amount. There is no commitment as part of the pilot to share needs/resources and risk other than under the current 50% scheme. Business rates will still be collected and retained by each authority with only the additional resources arising from the 75% scheme being accounted for on a Staffordshire “Area” basis.

7.5 The Pilot governance arrangements will enable authorities to retain effective membership of their respective Local Enterprise Partnerships via contributions to virtual Business Rate pools etc. The continuation of 100% Business Rates for Devolved areas will ensure that for 2019/20 at least that membership of more than one pool will remain in place and hence the ability to stay in a pool whether the application is successful or not will remain in place. Similar to 2018/19 any changes in existing pooling arrangements will need to be notified to existing pools in advance of the submitting the application and details are required of pooling arrangements if the application was unsuccessful .

Process and Timetable

8.1 Applications for 2019/20 are to be submitted on the Template provided by MHCLG.

8.2 Section 4 of the Prospectus (see **APPENDIX 1**) outlines the requirements of the Application in terms of:

- Membership Details of Proposed Pilot;
- Bid Details;
- Additional supporting Information;
- Membership;
- Lead Authority;
- Pooling arrangements if pilot bid is unsuccessful;
- Other Information.

8.3 Subject to the approval to submit an Expression of Interest the application will be developed by Staffordshire Chief Finance Officers Group and nominated policy officers in further discussions with MHCLG.

- 8.4 The Deadline for Expressions of Interest is the 25th September 2018. In order to meet this deadline, subject to the approval to submit an expression of interest by each member, delegated authority is requested for the Section 151 Officer, in consultation with the Leader of the Council and the Chief Executive, to agree, in conjunction with the other eleven authorities of the proposed pilot, the detail of the 2019/20 application.
- 8.5 Successful applications will be determined and announced as part of the provisional 2019/20 Local Government Settlement in late November/Early December.

REPORT AUTHOR

If Members would like further information or clarification prior to the meeting please contact Stefan Garner, Executive Director Finance, tel. 709242.

LIST OF BACKGROUND PAPERS

Staffordshire Pilot for 100% Business Rates Retention in 2018/19, Cabinet 19th October 2017.

APPENDICES

Appendix 1 The Ministry of Housing, Communities and Local Government (MHCLG) - Invitation to Local Authorities in England to pilot 75% Business Rates Retention in 2019/20, July 2018

Appendix 2 Draft Memorandum of Understanding

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