CABINET

5th September 2012

Report of the Portfolio Holder for Core Services & Assets

BUSINESS RATES POOLING

PURPOSE

In order to comply with the revised deadline of 10th September, 2012 set by the Department for Communities & Local Government (DCLG), Cabinet are required to make an executive decision in respect of the option to 'pool' Business Rates with other Local Authorities.

The revised deadline relates to those Local Authorities that have expressed an interest in more than one 'pool' (this includes Tamworth Borough Council) however; the original deadline of 19th October, 2012 as set out in the Statutory Consultation remains in respect of the final decision. All pooling arrangements will, if approved, be effective from 1st April, 2013.

RECOMMENDATIONS

Cabinet are recommended to:

1. Agree to engage in a Business Rates pooling arrangement to be effective from 1st April, 2013;

2. Indicate their preferred pooling arrangement i.e. Greater Birmingham & Solihull Local Enterprise Partnership OR Staffordshire & Stoke on Trent Local Enterprise Partnership; and

3. Indicate their preferred pooling option

EXECUTIVE SUMMARY

The Local Government Resource Review (LGRR) is considering ways to give councils greater financial autonomy and provide stronger incentives to support economic growth. The Government is committed to implementing the reforms suggested in the review by 2013/14. This inevitably requires major changes to the existing Government formula grant system.

Proposals are included in a draft Local Government Finance Bill, currently going through Parliament, for the retention of a proportion of the business rates revenue generated in a local area by the relevant local authorities.

Business rates retention is intended to provide incentives for local authorities to drive economic growth, as the authorities will be able to retain a share of the growth that is generated in business rates revenue in their areas, as opposed to the current system where all business rates revenues are held centrally.

A local business rates retention scheme will lead to various changes including;

- Authorities will be required to take the risk on any reductions in business rates income up to a predetermined level (7.5% to 10% below their baseline);
- Authorities will be able to share in any future increases in business rates income above a baseline and provide a real incentive to promote growth;
- The current formula grant system for funding local authorities will cease from 2013/14 onwards;
- A replacement resource distribution system with Authorities either receiving a “Top Up” to their business rates income or being required to pay over a “Tariff” from their business rates income to central Government.
- An Increase in the expectations of the Business Community which follow on from increased links between business rates income and the funding for Local Authority Services.

The Local Government Finance Bill also allows local authorities to form pools for the purposes of business rates retention. It is expected that pooling will offer local authorities an opportunity to retain more of the rates generated in their local areas and could allow them to use that additional revenue more effectively to drive future economic growth, which in turn should increase future business rates yield.

When authorities decide to enter into a pooling arrangement, a single funding baseline and single business rates baseline will be calculated for the whole pool, meaning that a combined tariff and levy is applied to the pool’s rates revenue as opposed to this being applied to each individual authority. This can deliver collective benefits for those involved in the pool. If a pool is dissolved then the member authorities would revert to their individual baselines, tariffs and levies.

There are a number of reasons why Local Authorities (LAs) could choose to pool. These include:

- cementing the working relationships / economic strategy;
- recognises the interdependence of the LAs;
- reduces the impact of the volatility of business rates income over a region by spreading the risk;
- potential tool to promote growth and job creation
- supports a holistic approach to investment / inward investment; and
- to gain a financial advantage – through retention of the levy element which otherwise would be paid to Central Government.

However, it should be noted that the safety net would not apply to authorities within a pooling arrangement – but the pool should provide funds to mitigate against such losses. In order to benefit from a safety net, the Council would have to experience a fall in business rates of between 7.5% - 10% of the funding baseline currently forecast at £2.4m (equating to £180k - £240k).

Members need to be mindful in coming to their preferred option of the following:

a) Financial impact & benefit to the authority;
b) Deliverability of growth estimates put forward & caveats outlined;
c) Impact of the decision on pooling on other potential decisions & future funding streams.

Should the Council elect to pool the retained business rates, there are currently two pooling options as outlined within options A and B below. External working groups relating to both pooling options were established and involved local authority Financial Directors discussing the various approaches, potential benefits and financial implications and modelling projections arising from the ability to pool business rates from 1st April 2013.

Option A - the Greater Birmingham & Solihull Local Enterprise Partnership Pool (GBSLEP)

A report produced by the GBSLEP Financial Directors is scheduled to be presented to the LEP Chief Executives on 30 August 2012. It identifies three options for distribution of the pooled resources:

1) No Loss – Share Proceeds of Reduced Levy Payments

Under the no loss approach each LA would retain the growth income that they would have received had no pool existed. The governance arrangements of the pool/political decisions would then prescribe how the additional business rates (levy) retained could be allocated across the pool. This would involve distributing windfall funding only.

The latest update proposes the use of 25% of the avoided levy payments to be set aside as a contingency fund – the first call on this will be to fund safety net payments. The remaining 75% will be allocated by the Executive Body.

From the modelling work undertaken with the lead authority, Birmingham City Council, the recently released CLG business rates pooling model has been populated with our estimates of growth. This suggests that the total retained levy could be:

Year (Option 1)	Retained Levy (Most likely) £m	Retained Levy (Worse case) £m
2013/14	1.1	0.3
2014/15	3.2	0.7
2015/16	6.2	1.1
2016/17	8.6	1.4
2017/18	10.1	1.4
2018/19	11.8	1.8
2019/20	13.7	2.1

2) No Loss – Shared Benefit of Growth

Under a shared benefit of growth approach each LA would, in the first year (2013/14), be allocated the funding that would it would have received had no pool existed. Any levy payments avoided would then be invested by the pool to facilitate growth. The proceeds of growth and retained levy could, in subsequent years, either be distributed across the pool or, be specifically allocated to facilitate further growth. This would involve distributing a combination of windfall funding and core funding.

From the modelling work undertaken the total funding under this option could be:

Year (Option 2)	Retained Levy (Most likely) £m	Retained Levy (Worse case) £m
2013/14	5.4	0.4
2014/15	13.9	1.5
2015/16	25.3	2.7
2016/17	34.3	4.5
2017/18	41.8	3.6
2018/19	49.7	4.7
2019/20	58.3	5.9

These figures include growth above inflation together with the levy savings.

3) Fixed Percentage Distribution

Under a fixed percentage distribution approach, in 2013/14 each LA would retain the income from business rates that they would have received in 2013/14 had no pool existed. Future years funding allocations could then be allocated according to this baseline ratio of funding. This would involve distributing a combination of windfall funding and core funding as included within the above forecasts.

Commentary on the options:

The consensus from the Finance Directors represented is that option 1 would be preferred – subject to confirmation of the distribution mechanism for the levy savings. The benefit being that any growth generated locally will be retained locally – so authorities will be no worse off in times of austerity & funding constraints.

It is anticipated that the Chief Executives at their meeting on 30th August will be asked to decide upon which option to progress – including confirmation of the distribution mechanism.

Option B - the Staffordshire and Stoke on Trent Business Rates Pool (SSBRP)

The tables below show the prospective growth rates assuming a 'most likely' and best/worse case scenario as provided by each District authority followed by the potential financial consequences of pooling. The results have been based on a Society of County Treasurers (SCT) model which is comparative with alternative models.

Growth scenario	2013/14 average	2014/15 average	2015/16 average	2016/17 average
"Best case"	1.53%	1.61%	2.60%	2.49%
"Worst case"	-0.44%	-0.81%	-1.50%	-0.28%
"Most likely"	1.39%	1.41%	0.55%	1.68%

Growth scenario	Predicted Total Benefit / Loss from the Pool			
	2013/14 £m	2014/15 £m	2015/16 £m	2016/17 £m
	SCT Model Results			
"Best case"	1.397	2.395	4.603	7.151
"Worst case"	-0.334	-0.939	-1.820	-1.926
"Most likely"	1.014	1.960	3.016	4.615

The exact details of the scheme are still awaited from DCLG and consequently, all Local Authorities are in a similar position in terms of understanding the precise benefits of pooling.

The SSBRP have stated that the proposed financial principles underpinning a pooling arrangement should have three component parts to manage the levy savings;

- A **contingency** to provide a safety net to mirror the Government's arrangements so that no one is 'worse off' being in the pool compared to being outside the pool – 20%.
- A **local incentive** (so that Districts keep a share of their own 'levy' savings) – 40%;
- Retention of a **central investment fund** to support future economic growth – 40%;

Furthermore, they have also recommended that as a starting point the split between the three component parts are 20%:40%:40%. Authorities will be able to influence the distribution of the central investment fund and contingency through representation / votes at the Staffordshire Economic Consortium.

The proportions are recommended so that after setting aside a contingency sum, there is an equal split between the amount retained locally in each billing area and that which is earmarked to central investment fund to support key projects across the whole county. In practice the pool would need to initially decide how much was required to be placed into the contingency and so the local incentive/fund shares may be higher or lower but they would be split equally.

Commentary on Both Pooling Options:

From the financial estimates detailed above, the GBSLEP projects levy savings of c.£19m over 4 years compared to c.£11m from the SSBRP.

Year (Option 1)	GBSLEP Option 1 (preferred) (Most likely) £m	SSBRP (Most likely) £m
2013/14	1.1	1.0
2014/15	3.2	2.0
2015/16	6.2	3.0
2016/17	8.6	4.6
2017/18	10.1	n/a
2018/19	11.8	n/a
2019/20	13.7	n/a

A key issue is around the expectation / delivery of Growth and whether there is more chance of growth potential with one pool over the other – especially as there may be a viability issue where some Authorities will have to decide to pool with one pool over another.

Indications are that should Lichfield and Tamworth not join the SSBRP pool, the impact may result in reduced benefits from the levy savings, so in sharing the levy savings according to proposed splits (40/40/20) the overall impact is that the central investment fund and contingency may receive no contribution.

Governance issues still need to be resolved / formalised – especially around termination arrangements.

The key impact for members' consideration is which pool shows greater reward / opportunity and of course greater opportunity re Business Growth. The following table summarises a weighted assessment of the potential benefits based on current information on which Pooling arrangement best delivers in line with the evaluation criteria, as detailed at **Appendix B**:

Evaluation Criteria	Financial impact & benefit to the authority	Deliverability of growth estimates put forward & caveats outlined	Impact of the decision on pooling on other potential decisions & future funding streams
Cementing the working relationships / economic strategy;	GBSLEP	GBSLEP	GBSLEP
Recognises the interdependence of the LAs;	GBSLEP	GBSLEP	GBSLEP/SSBRP
Reduces the impact of the volatility of business rates income over a region by spreading the risk;	GBSLEP	GBSLEP	
Potential tool to promote growth and job creation supports a holistic approach to investment / inward investment;	GBSLEP	GBSLEP	GBSLEP
To gain a financial advantage – through retention of the levy element which otherwise would be paid to Central Government.	GBSLEP	GBSLEP	

It should be reiterated that the proposals focus on the distribution of business tax revenues, rather than changes to the system of taxation. Businesses will see **no change** in the way they pay business rates or the way the tax is set. Rate setting powers will remain under the control of central government and the process for revaluations will be unchanged.

RESOURCE IMPLICATIONS

The Local Government Resource Review including the retention of business rates will have potentially significant implications for the Council. The system will incorporate the savings required as part of the Comprehensive Spending Review but will also provide a financial incentive to councils generating business growth.

As part of this arrangement it is expected that many of the financial risks associated with collection of business rates will also be transferred to councils, although a safety net is to be put in place to deal with significant shocks (for Authorities which decide not to pool).

The DCLG letter to the Lead Pool Authorities requests that certain information is provided by September 10th 2012, including that those authorities who have expressed an interest in more than one Pool are required to decide which Pool they will chose.

The October deadline presented us with some challenges, given that we will still be making a decision using significant assumptions on many of the variables involved. The September deadline effectively pulls this deadline forward by one month, because the decision on which pool to commit to has to be based on the financial implications and prospects for each authority and each Pool. So not only is this a complex decision for each Council, but the decision by each potential Pool member can effect the financial position of the Pool as a whole.

Requesting that a decision be made by September 10th 2012 fails to recognise the complexity of the financial equation involved.

LEGAL & RISK IMPLICATIONS

As the proposals focus on the distribution of business tax revenues, rather than changes to the system of taxation it is not perceived that there will be any direct legal implications.

Risks associated with the business rates retention scheme include;

a) The risk associated with the collection of business rates is clearly passing to the Authority although the new system has a ‘safety net’ component so that authorities are compensated if their rates income falls below 7.5% or 10% (the government has yet to decide the specific figure of their baseline spending) - if real terms business rates income across the Authorities fall, a pool has no advantage and indeed individual Districts could lose out on ‘safety net’ payments;

b) The key driver of whether a pool is advantageous is whether there will be sustained positive real growth in business rates across the Authorities included;

c) There is also a risk in relation to the uncertainty over inbuilt changes to the new system. For example it is understood the system is due to be ‘reset’ after a period of time e.g. 5 -7 years and there is no clear idea of how the benefit of the additional rates income generated in intervening time would be dealt with. There is a risk that any interim benefit will be lost after the reset although equally authorities might benefit from a ‘needs’ reset;

d) Financial information included within the report is based on the best estimates / interpretation of the proposals available, as provided through discussions with the GBSLEP & Staffordshire Consortium;

e) Uncertainties over financial decision making as the baseline is still unknown with a lack of time for more meaningful modelling following further consultation released during July 2012;

f) Financial information based on modelling data under current interpretation of proposals which could change before the scheme is finalised;

g) Impact on potential growth modelling will be impacted by the baseline figures – critical for forecasting the level of growth / levy shares;

h) Forecasts are based on predicted growth but any levy surplus will be subject to actual growth achieved (given current economic conditions);

i) Political considerations & impact of decisions on pooling for partners, stakeholders and other Local Authorities;

j) The Draft Bill is still progressing through Parliament & subject to change;

k) The proposed apportionment of levy for distribution will mean 60% will be out of the Councils' control in line with voting rights for districts & therefore a potential likelihood is that this could favour others as there is no commitment as to where it will go.

An update report may be required as a result of ongoing discussions between the parties involved.

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Background Papers:

Local Government Resource Review – Proposals for Business Rates Retention

Appendices

Appendix A – Copy of DCLG Letter dated 13 August 2012
Appendix B – Benefit Weighted Evaluation Assessment

Appendix A

Department for Communities and Local Government

Lead Pool Authorities
Via email

Our Ref:
Your Ref:

13 August 2012

Dear Lead Authority,

Pooling: Expression of Interest

Thank you for submitting an Expression of Interest for pooling business rates. I have had conversations with a number of you already and I will be contacting all of you shortly to discuss progress towards the October deadline. In advance of those discussions I wanted to set out our expectations in terms of handling the key activities over this period of development.

As the Pooling Prospectus makes clear, the Government's view is that rather than trying to impose a uniform model from the centre, it is for the members of the pool to determine how best a pool might work. This will allow pools to develop which reflect both the unique characteristics of the area and will best serve the local authorities' aspirations. Having lodged an Expression of Interest, the task is now for you to develop the detailed proposal which can be signed off by relevant Chief Executives and section 151 Officers and submitted to us by 19 October.

There is a lot of detail to be worked through in order for this deadline to be achieved. Our presumption is therefore that there is a serious intent behind the Expressions of Interest and that work is already underway on establishing the operational details which will underpin the final proposal. For this to be the case, we would expect local authorities to have undertaken some modelling of the potential financial impacts of pooling and that discussions have started on the governance arrangements, including dissolution of the pool, and the allocation of resources between pool members. Again, we are not seeking to be prescriptive here; the onus is on the members of the pool to create a model which is appropriate for them. However, it is critical that pool members satisfy themselves that they are content with the governance structure, how benefits and risk will be shared, the decision making arrangements and the dissolution process.

As you will be aware, before a designation of a pool of authorities can be made, the Department must consult such other parties as are likely to be affected by a designation

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(for example, neighbouring authorities) on your pooling proposals in September, to provide them with an opportunity to highlight any perceived benefits or disadvantages to them, before final decisions on designation of your pool are taken. We envisage that this consultation will take the form of a letter sent to all of the relevant parties, which would set out the proposed membership of the pool and your consideration of the potential impacts it may have on other bodies, and invite them to send views on the proposal to the Department.

We will therefore need the following information from you as soon as possible and **by no later than 10 September,** to include in the consultation:

- a firm list of the pool members. The only restrictions we have set in terms of the membership of the pool are that the pool must cover the whole of the local authority area and that a local authority can only be a member of one pool. Some local authorities have been identified in more that one pool. Where this is the case the relevant local authorities must quickly decide which pool they wish to be part of.

- your consideration of the impacts the pool may have on other parties, including neighbouring authorities (and, where this has identified potential adverse impacts, any steps you have taken or will take to mitigate them). For the consultation to be effective this must provide sufficient detail for those consulted to reach an informed view on the proposal. This need not be full details of your governance arrangements – since issues such as the distribution of the resources within the pool will not impact on non-members – it should set out clearly all aspects of your proposal that may affect other bodies.

We shall then be seeking responses to the consultation no later than 28 September.

Whilst full details of your governance arrangements need not be included in the consultation, you will understand that before consulting, the Department will need to satisfy itself that you are on track to deliver a fully signed off proposal by all members of the pool by 19 October. To provide us with this reassurance, we would therefore also welcome sight of your emerging governance arrangements and the process for securing signatures from each of the councils as soon as possible and by no later than **10 September**. I will of course be more than happy to discuss draft governance arrangements as you work them up over the coming weeks.

Yours sincerely,

Elizabeth Cowie

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Appendix B

Benefit Weighted Evaluation Assessment

Evaluation Criteria	Financial impact & benefit to the authority		Deliverability of growth estimates put forward & caveats outlined		Impact of the decision on pooling on other potential decisions & future funding streams	
Pool	**GBSLEP**	**SSBRP**	**GBSLEP**	**SSBRP**	**GBSLEP**	**SSBRP**
Cementing the working relationships / economic strategy;	**High**	**Medium**	**Medium**	**Low**	**High**	**Medium**
Recognises the interdependence of the LAs;	**Medium**	**Low**	**Medium**	**Low**	**Medium**	**Medium**
Reduces the impact of the volatility of business rates income over a region by spreading the risk;	**High**	**Medium**	**Medium**	**Low**		
Potential tool to promote growth and job creation supports a holistic approach to investment / inward investment;	**High**	**Medium**	**Medium**	**Low**	**High**	**Medium**
To gain a financial advantage – through retention of the levy element which otherwise would be paid to Central Government.	**High**	**Medium**	**Medium**	**Low**		

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