Manchester City Council
Report for Information

Report to: Resources and Governance Scrutiny Committee – 8 September 2016

Subject: Business Rates Retention

Report of: The City Treasurer

Summary

To provide Members with information on the Greater Manchester Pilot for 100% Business Rate Retention, the current government consultation and the impact on the Council's budget.

Recommendation

Members are asked to note the report.

Wards Affected: All

Financial consequences for the Revenue Budget

This report provides information on the the 100% business rates retention pilot and its impact on the budget.

Financial consequences for the Capital Budget:

There are no direct consequences for the Capital Budget.

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Background documents (available for public inspection):

The following documents disclose important facts on which the report is based and have been relied upon in preparing the report. Copies of the background documents are available up to 4 years after the date of the meeting. If you would like a copy please contact one of the contact officers above.

None

Introduction

1. Business rates are a form of tax charged to occupiers of most types of non-domestic property. Rates are payable on shops, offices, pubs, warehouses, factories, holiday rental homes and guest houses. The amount charged to occupiers of non-domestic premises is calculated by multiplying the Rateable Value (RV) of the property (determined by the Valuation Office Agency) by the multiplier (set by the Department for Communities and Local Government).

2. Broadly speaking, the RV of most non-domestic property is the same as the market rent at each premises in April 2008 (two years before the last revaluation). However, for public houses and other licensed premises their expected 'fair maintainable trade' is used to determine their rental value and in turn their RV. Fair maintainable trade is the annual level of trade (excluding VAT) that a public house can be expected to achieve assuming a reasonably efficient operator.

3. The multiplier is reset at each revaluation and typically changes each year in line with inflation (currently linked to RPI). At a revaluation the multiplier is reset to ensure that the overall national revenue from business rates only rises in line with inflation. In addition to the standard multiplier, in 2005/06 the small business multiplier was introduced, this is a slightly lower multiplier than the standard and is currently used to calculate the bill of premises with an RV of less than £18k (unless part of a wider group).

Background

4. Recent changes to the business rates regime are summarised below and detailed in the following paragraphs.

Pre-2013	All rates revenue sent to Whitehall
April 2013	50% rates revenue retained locally
April 2015	Pilot areas (inc GM and Cheshire East) retain 100% rates 'growth'
	Greater Manchester and Cheshire East Pool commenced
April 2017	Pilot areas (inc GM) retain 100% rates revenue
April 2020	National roll out of 100% retention

5. From 2013/14 the Local Government Resource Review (LGRR) introduced the partial re-localisation of business rates which brought a lot more volatility to the local government funding system. The risk of any reduction in local business rate yield due to the closure of businesses or appeals against rateable values previously lay with Central Government, and similarly they benefitted from any increase in local yield. From 1 April 2013 those risks and benefits were shared between Councils and Central Government. Councils

retain an element of the business rates collected, for districts like Manchester this is 49%.

6. The central share is redistributed to councils in the form of revenue support grant and other grants. The local share is kept by local government, but is partly redistributed between local authorities through a system of tariffs and top-ups. This redistribution is to ensure that areas do not lose out just because their local business rates are low compared to their assessed needs. Local authorities are either tariff authorities, who collect more than their assessed level of need, or top up authorities who collect less and receive a government top up grant to make up the difference. Tariff authorities pay their excess business rates back via a levy of to fund the top ups that other authorities receive.

7. Therefore Manchester City Council retains 49% of growth in business rate receipts arising from new or expanding businesses. Local authorities that pay tariffs are also liable to pay a levy of up to half of this type of growth. The money raised from this levy is then used to fund a safety net system. This system protects those councils which see their annual business rate income fall by more than 7.5% below their ‘baseline funding level’. The baseline funding level is that assessed by government based on levels of need and estimated business rates and council tax collectable.

Greater Manchester and Cheshire East Business Rates pool

8. Under the business rates pool regulations authorities can voluntarily come together to pool their business rates, providing them with the potential to generate additional growth and more importantly retain any levy payments rather than returning them to central government. This is possible because the Pool treats Authorities as a single entity for the purpose of calculating, top-up, tariffs, levies and safety net requirements. From April 2015 Councils from Greater Manchester and Cheshire East joined together as a Pool, seeking to maximise the amount of Business Rates retained within the area. Cheshire West and Chester joined the pool in April 2016.

9. The Governance Agreement for the pool set out the arrangements for those authorities generating a levy payment to be retained by the pool. There will be an initial call on this levy in the following proportions: Cheshire East and Cheshire West and Chester retain 50%, Trafford and Stockport retain one-third with the remainder being pooled at GM level. The 2015/16 total saving is £2.3m of which £1.5m will be retained by the Combined Authority and utilised to the benefit of the region.

Greater Manchester and Cheshire East 100% Growth Retention Pilot

10. In the 2015 Budget the Chancellor of the Exchequer announced a pilot to retain 100% of additional business rate growth in Greater Manchester and Cheshire East. The scheme set a growth baseline above which named authorities would retain 100% of growth.

11. The scheme started on 1 April 2015, as a pilot and allows local authorities to retain 100% of "additional growth" in business rates. The formula remains under discussion with the Department of Communities and Local Government (DCLG) to identify the level of growth which removes the volatility of appeals.It has not been decided yet how any additional growth will be applied.

100% Business Rates Retention

12. The government has committed to delivering 100% Business Rates retention for local authorities in England by the end of this Parliament. They will pilot the approach from 1 April 2017 in a number of areas including Greater Manchester and Liverpool City Region.

13. By moving to 100% business rate retention local councils in England will have control of around an additional £12.5 billion of revenue from business rates. In order to ensure that the reforms are fiscally neutral, councils will gain new responsibilities, and some specific grants which are currently funded through the business rates central share will be funded through the local share instead.

14. The business rates baseline ('tariffs and top-ups') will be reworked to ensure that authorities that are more deprived or with less capacity to raise business rates do not suffer at the start of the new arrangements. The move to 100% retnetion does not represent additional funding for local government

15. Under 100% business rates retention all authorities will have a new power to reduce the business rates multiplier. Authorities with elected mayors will have the power to levy a 2p in the pound supplement on business rate bills to fund new infrastructure projects. The Levy will be removed but an element of safety net retained. The design of the new system will take account of the changing shape of local government, including the role of Combined Authorities.

16. The Government's intention is that policy should be developed with the sector, but decisions will lie with Ministers. The DCLG and Local Government Association (LGA) established a technical steering group and three sub-groups to provide information and expert advice. The groups remits are:

- Technical Working Group on Needs and Redistribution – looking at measuring local authorities' relative need and resource, reviewing the indicators that have previously been used in the relative needs formulae, distributing funding to geographies other than at the local authority level, the frequency of revisiting and approach to the needs assessment for authorities, whether, and if so how, to transition to a new distribution of funding and how, and what, incentives should be built in to an assessment of councils' need.
- Responsibilities Working Group - develop options for the devolution of responsibilities and funding, provide advice on a package or packages of responsibilities and funding that should be devolved to local government in implementing 100% rates retention.

- Systems Design Working Group – looking at interaction of the Central List and local lists, safety net under the new system, frequency of resets of the business rates retention system, power to introduce a levy on business rates to pay for infrastructure, flexibility of reliefs both from the point of view of administrative efficiency and from economic growth and employment, multiplier flexibilities - power to vary / reduce the multiplier.

17. The following principles provide the base for pilots to be developed:

- Give authorities an incentive to grow local tax bases by ensuring they see long-term rewards from growth;
- Maintain a predictable income stream against which authorities can take long term investment decisions; and
- Ensure that local authorities can continue to provide a full range of local services, whilst recognising that decisions about spending priorities should be made locally by locally-elected representatives accountable to local taxpayers.

18. There has been assurance that Authorities will be no worse off as a result of taking part in the pilot. For GM this will include covering the loss of any extra revenue generated from the current pilot (100% retention of additional business rates growth) and the business rates pool. The pilots will help to develop the mechanisms that will be needed to manage risk and reward. The approach will include financing new responsibilities and/or existing funding streams from additional business rates, including those that support economic growth at district or regional level.

19. The are four main areas of focus for the GM pilot

- Incentivising economic growth – in particular how growth can be incentivised and headroom for investment created

- Creating a stable funding stream – addressing issues such as how risk, particularly that associated with appeals is dealt with and how a new safety net arrangement to protect local authorities from the increased levels of volatility in their funding, should operate.

- Transfer of Functions – which functions will transfer to being funded from business rates income. It is given that Revenue Support Grant will cease and be funded via business rates income.

- System design - in particular how revaluations, resets and tariffs and top ups will operate.

20. GM are aiming to pilot 100% of business rates from 1 April 2017. Work is ongoing to ensure that the practical arrangements are in place. This includes agreeing how ‘no detriment’ will be calculated to ensure that the authority will be no worse off than under the current arrangements. Discussions are also ongoing with CLG on which functions should transfer during the pilot period with agreement expected in October.

Business Rates Retention Consultation

21. There are currently three consultations:

- *Fairer Funding* – This consultation seeks to review how relative need is measured and what the needs assessment formula should be in a system where local government is funded by local resources not central grant. Government aims to have this in place for 2020/21, when the 100% business rates retention is rolled out nationally.
- *Appeals* - In October 2015 Government published the 'Check, Challenge, Appeal' consultation document which sought views on a new three stage approach to business rates appeals. This second consultation seeks to consult on draft Regulations to enable primary legislation via the Enterprise Act.
- *Business Rates* - This consultation seeks views on the implementation of the Government's commitment to allow local government to retain 100% of the business rates that they raise locally.

22. This report foucses on the Business Rates consultation which was issued on 5 July and will run for 12 weeks until 26 September. It is seeking views on the implementation of the 100% retention scheme and specifically seeking to identify some of the issues that need to be addressed when designing the reforms.

23. The consultation includes 36 questions which are split over four catagories and listed in Appendix 1 for information. A summary of the areas for consultation and initial comments are set out below.

Devolution of Responsibilities

24. To ensure that the proposal for 100% business rates retention is fiscally neutral, local government will need to take on new responsibilities to match the increased income, and existing central government grants will need to be phased out. If the value of new responsibilities exceeds the increased retained rates receipts, Government would continue to make grant payments to fund the difference, although the government's expectation would be any grant payments would not replicate the current Revenue Support Grant which will be phased out.

25. There is a danger that the functions which transfer are driven purely by the headroom within the business rates system rather than those which are most appropriate to transfer, will provide the right incentives to promote growth and reform as originally intended with business rates retention and best fit the capacity of the local area to take on different responsibilities.

26. Some underpinning considerations include:

    - functions must be relevant to supporting productivity and growth in a way that is fiscally neutral to HMT and GM

- their should be an abiltiy to create an investment capacity through growth in business rates income
- there should not be a one size fits all approach - different local authorities and city regions / CAs should be able to have different arrangements
- should avoid the transfer of demand led budgets that transfer a future funding /cost risk to local authorities
- the pilot should support the testing of more innovative ideas in a 'safe environment' to inform the proposals for full devolution
- the transfer of functions should be tested at both CA and individual local authority level
- functions transferred should not have any ring-fencing constraints and there needs to be the ability to shape / influence / redesign those functions at a local level
- The new burdens principle should apply – ie where further responsibilities are transferred to local government the funding should follow.

27. The consultation document has identified current grant funding streams which Government see as a "fit" for transfer but Authorities need to consider and respond as to whether these are appropriate. These are listed below:

- Revenue Sport Grant
- Rural Services Delivery Grant – Not applicable for MCC or GM
- Greater London Authority Transport Grant – Not applicable for MCC or GM
- Public Health Grant – This would need to be accompanies by the removal of the ringfence
- Improved Better Care Fund – ie the additional social care funding for councils
- Independent Living Fund - Discretionary payments to disabled people
- Early Years- Funding for 15 hour entitlement for 3 and 4 year olds and disadvantaged 2.year olds.
- Youth Justice - for the operation of the youth justice system and the provision of non-custodial youth justice services. There are risks with this as it is a demand led function where funding is reducing.
- Local Council Tax Support Administration Subsidy and Housing Benefit Pensioner Administration Subsidy, no value in transferring this DWP funding into the Business Rates Retention system.
- Attendance Allowance – A benefit for those with disabilities over the age of 65. The transfer of this responsibility is not supported.

28. GM are looking for other areas to be considered which could include 16-18 vocational skills and transport capital funding.

Rewarding growth and sharing risk

29. The consultation raises questions in relation to rewarding growth and distribution including the timing of resets of the system and tarrif and top ups, additional powers for elected mayors, local versus central list and appeals.

30. Resets: A system reset will allow Government to reconsider relative need and recalculate the redistributable amounts by reassessing how much an authority can raise through business rates and recalculating the top up and tariff amounts.

31. A five year partial reset is supported as this provides an incentive for authorities to grow and retain that growth. A full reset would remove all business rates growth every five years, thus removing any incentive to grow the business rates base. A partial reset would ensure that some authorities with a large business rates base do not grow their funding disproportionately, provides an incentive through retaining some local growth and ensuring that authorities who are unable to grow their business rates income are protected and able to continue to fund services at their assessed level of need. Underpinning this is the associated work on reviewing the local government funding formula which will define what a fair level of funding for each authority is. This is subject to a separate consulation process.

32. Tariff and Top Ups –Such a system needs to remain in order to ensure that all local authorities receive an appropriate level of funding to meet their needs and the value of any functions that have transferred. This is the mechanism by which ‘excess growth’ from some local authorities will be redistributed to ensure that all local authorities receive sufficient funding to meet their assessed needs.

33. The consultation asks if it would be helpful to move some of the ‘riskier’ hereditaments off local lists and to the central list. For businesses on the local list the business rates income is retained locally, for the Central it is retained by central government. The Central List was established to hold a (small) number of properties for Business Rates purposes. These are mostly property holdings of former nationalised industries, including utilities, long distance pipelines, telecommunications and British Waterways. If Government is to pursue the National List, we suggest hereditaments are transferred by local request rather than by mandate. It is preferable that properties such as the airport and stations are on the local list so the local authority sees a return on its investment into those assets.

34. The consultation seeks views at which level the risks associated with successful business rates appeals should be managed. An approach to try and move this to regional or Combined Authority level would not be supported. It is suggested the risk for appeals driven by errors made by the VOA and from the impact of the revaluation system should be funded nationally from income from the central business rates list although it is not known whether this suggestion will be taken up. It is accepted that the risk of appeals driven by local action and policy decisions should be managed locally.

35. It is also being stressed that the above will need to be accompanied by a tighter safety net arrangement which provides more protection than the current 92.5% of the baseline funding level. At the moment this will protect Manchester if business rates income drops by £12.3m more then than assumed in the baseline funding level.

Local Tax Flexibilities

36. There are several questions around the design and operation of the new tax flexibilities that authorities will have , the range of options for powers to reduce business rates and the ability to raise an infrastructure levy. Initial thoughts are set out below.

37. Power to reduce the multiplier could be welcomed as it gives local Authorities more control over Local Taxes and gives the option of a universal discount offering, as opposed to discretionary relief which is more targeted. However it is important that this is not used to promote inter authority competetion to attract businesses.

38. The consultation asks how the proposed infrastructure levy should interact with existing Business Rates Supplement (BRS) Powers. Under the current scheme a Business improvement Disrtrict (BID) enables 2% to be applied to RV in a predetermined area where the additional funds raised are used for the for the betterment of those contributing. For example Manchester has the ‘Heart of Manchester’ BID set up around the Arndale Shopping Mall. These additional funds are used to promote the area and attract and create retail opportunities. A BID can only be implemented following a successful referendum.

39. The proposed Mayoral Levy (or Infrastructure Levy) allows a 2p in the pound supplement on business rates bills in Combined Authority Areas, with all additional revenue being used for cross boundary infrastructure projects. The approval of the majority of the business members of the Local Enterprise Partnership (LEP) board will be required for a levy to be raised. For simplicity it is suggested the Mayoral Levy supersedes all existing BRS schemes in Combined Authorities and City Regions. Another option is to continue successful BID schemes and remove them from the infrastructure levy.

40. There are also Enterprise Zones to attract commercial growth and investment within a specified area by offering business rates relief. Manchester currently has three live Enterprise Zones which have attracted significant investment including Amazon and DHL.

41. Consideration is being given to how all these ‘incentives’ should operate under the new system.

Accountability and Accounting

42. The final questions in the consultation consider the consequences of the reforms on accountability, potential changes to the way the scheme is accounted for and changes to data collection. These technical considerations are being worked through. It is likely that the response will advocate:

43. As local services will increasingly be funded from locally raised resources it is important to ensure councils are accountable for funding decisions. To

facilitate this the removal of all ringfencing is sought and councils require greater assurance over future policy decisions. Certainty could be increased by:

- The removal of ringfencing constraints
- Improving the business rates appeals process (again subject to a separate consultation) and improving the quality of data from the VoA
- Simplifying the Collection Fund accounting treatment
- Retaining the Collection Fund Account which provides transparency over how much of the local taxes the billing authority forecast it would collect and how it has been distributed.

Impact on Budget

44. Under the 100% retention pilot there has been assurance from the Government that pilot areas will not be financially worse off than if they had not participated. This includes covering the loss of any extra revenue generated from the current pilot (100% retention of additional business rates growth) and the business rates pool. Therefore two monitoring systems will be in place one measuring the new system of 100% retention and one measuring the current 50% system.

45. There is the added uncertainty of the impact of the business rates revaluation. Whilst the authority will not lose out on the level of funding received (any reduction in business rates income will be offset by the top up arrangement) the associated increase in appeals pose an additional risk.

46. For prudence the council budget will be set on the basis of the forecast receivable under the old system. Due to the risks associated with appeals it is unlikely that any growth in business rates income will be included.

Conclusion and Next Steps

47. This report provides an overview of the business rates system, the pilots that are in place for Greater Manchester and the issues that are covered in the consultation document.

48. There is an opportunity with the business rates pilot to influence the arrangements that will be in place under the new system, the functions that will transfer to being funded by retained business rates and to work with CLG to create some additional headroom capacity. However there is unlikely to be any immediate impact on the council's budget.

49. The final response to the consultation will be agreed with the Executive Member for Finance and Human Resources.

Business Rates Retention Consultation Summary of Questions

Devolution of Responsibilities

Question 1: Which of these identified grants / responsibilities do you think are the best candidates to be funded from retained business rates?

Question 2: Are there other grants / responsibilities that you consider should be devolved instead of or alongside those identified above?

Question 3: Do you have any views on the range of associated budgets that could be pooled at the Combined Authority level?

Question 4: Do you have views on whether some or all of the commitments in existing and future deals could be funded through retained business rates?

Question 5: Do you agree that we should continue with the new burdens doctrine post- 2020?

Rewarding growth and sharing risk

Question 6: Do you agree that we should fix reset periods for the system?

Question 7: What is the right balance in the system between rewarding growth and redistributing to meet changing need?

Question 8: Having regard to the balance between rewarding growth and protecting authorities with declining resources, how would you like to see a partial reset work?

Question 9: Is the current system of tariffs and top-ups the right one for redistribution between local authorities?

Question 10: Should we continue to adjust retained incomes for individual local authorities to cancel out the effect of future revaluations?

Question 11: Should Mayoral Combined Authority areas have the opportunity to be given additional powers and incentives, as set out above?

Question 12: What has your experience been of the tier splits under the current 50% rates retention scheme? What changes would you want to see under 100% rates retention system?

Question 13: Do you consider that fire funding should be removed from the business rates retention scheme and what might be the advantages and disadvantages of this approach?

Question 14: What are your views on how we could further incentivise growth under a 100% retention scheme? Are there additional incentives for growth that we should consider?

Question 15: Would it be helpful to move some of the ‘riskier’ hereditaments off local lists? If so, what type of hereditaments should be moved?

Question 16: Would you support the idea of introducing area level lists in Combined Authority areas? If so, what type of properties could sit on these lists, and how should income be used? Could this approach work for other authorities?

Question 17: At what level should risk associated with successful business rates appeals be managed? Do you have a preference for local, area (including Combined Authority), or national level (across all local authorities) management as set out in the options above?

Question 18: What would help your local authority better manage risks associated with successful business rates appeals?

Question 19: Would pooling risk, including a pool-area safety net, be attractive to local authorities?

Question 20: What level of income protection should a system aim to provide? Should this be nationally set, or defined at area levels?

Local Tax Flexibilities

Question 21: What are your views on which authority should be able to reduce the multiplier and how the costs should be met?

Question 22: What are your views on the interaction between the power to reduce the multiplier and the local discount powers?

Question 23: What are your views on increasing the multiplier after a reduction?

Question 24: Do you have views on the above issues or on any other aspects of the power to reduce the multiplier?

Question 25: What are your views on what flexibility levying authorities should have to set a rateable value threshold for the levy?

Question 26: What are your views on how the infrastructure levy should interact with existing BRS powers?

Question 27: What are your views on the process for obtaining approval for a levy from the LEP?

Question 28: What are your views on arrangements for the duration and review of levies?

Question 29: What are your views on how infrastructure should be defined for the purposes of the levy?

Question 30: What are your views on charging multiple levies, or using a single levy to fund multiple infrastructure projects?

Question 31: Do you have views on the above issues or on any other aspects of the power to introduce an infrastructure levy?

Accountability and Accounting

Question 32: Do you have views on how to increase certainty and strengthen local accountability for councils in setting their budgets?

Question 33: Do you have views on where the balance between national and local accountability should fall, and how best to minimise any overlaps in accountability?

Question 34: Do you have views on whether the requirement to prepare a Collection Fund Account should remain in the new system?

Question 35: Do you have views on how the calculation of a balanced budget may be altered to be better aligned with the way local authorities run their business?

Question 36: Do you have views on how the Business Rates data collection activities may be altered to collect and record information in a more timely and transparent manner?