Leeds CITY COUNCIL

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**Report of Chief Officer Financial Services**

**Report to Scrutiny Board (Strategy and Resources)**

**Date: 12th November 2018**

**Subject: Update on Current Business Rates Issues**

| | | |
|---|---|---|
| Are specific electoral wards affected?<br>If relevant, name(s) of ward(s): | ☐ Yes | ☒ No |
| Are there implications for equality and diversity and cohesion and integration? | ☐ Yes | ☒ No |
| Is the decision eligible for call-In? | ☐ Yes | ☒ No |
| Does the report contain confidential or exempt information?<br>If relevant, access to information procedure rule number:<br>Appendix number: | ☐ Yes | ☒ No |

**Summary of main issues**

1. The purpose of this report is to provide a briefing on current business rates issues as requested by the Board at 18/06/18.

2. The report is intended to enable members to more fully understand the background of Business Rates Retention and the current position with regards to Business Rates Retention Pilots.

3. This report also looks at the continued volatility of Business Rates income.

**Recommendations**

4. Strategy and Resources Scrutiny Board are recommended to:

   - note the contents of the report.

## 1 Purpose of this report

1.1 Following Strategy and Resources Scrutiny Board in June a request was made to update the Board on:

- How Business Rates operates;
- The Council's current Business Rates Retention pilot and the application for a Business Rates Retention pilot in 2019/20; and
- The volatility of Business Rates including appeals.

1.2 Therefore, this report will cover:

- The background of Business Rates Retention at 50% and the move to 75% Business Rates Retention being implemented in 2020/21
- An update on the Leeds City Region Business Rates 100% Retention pilot in 2018/19
- The North and West Yorkshire application to pilot 75% Business Rates Retention in 2019/20
- Volatility of Business Rates including exposure to appeals risk

1.3 Additionally, this report will update the Board on Business Rates reform in the context of wider local government funding issues, recognising the positive impact Scrutiny has in advising on and influencing these issues.

## 2 Background Information

2.1 Since 2013/14, local authorities have been able to retain 50% of business rates growth above a Government determined baseline assessment. However tariff authorities such as Leeds are then subject to a levy which, in the absence of any pooling arrangement, is remitted back to government. In October 2015 the Government announced its intention to enable local government as a sector to retain 100% of business rates raised locally. A Local Government Finance Bill was introduced in Parliament in January 2017 to provide enabling legislation for the reforms. The Bill did not complete its legislative stages before the 2017 general election and was subsequently not reintroduced. MHCLG subsequently committed to the introduction of 75% business rate retention by 2020, alongside the implementation of its review of the needs and redistribution mechanism for local authority funding through the Fair Funding Review.

2.2 100% business retention pilots were agreed in 2017/18 as part of a number of devolution deals, in Greater Manchester, Liverpool City Region, the West Midlands, Cornwall and the West of England.

2.3 In September 2017, Government invited other authorities to bring forward applications to pilot 100% retention in 2018/19. This was an expansion of the 2017/18 100% pilot programme and was intended to help Government and the local government sector to explore options for the design of future increased business rate retention. Leeds, on behalf of the 7 authorities of the Leeds Region Business Rates Pool, submitted a successful application for 2018/19, together with Berkshire, Derbyshire, Devon, Gloucestershire, Kent, Lincolnshire, Solent, Suffolk, Surrey and Greater London. A piece of work by the Institute for Fiscal Studies has suggested that the gain to these pilot authorities in 2018/19 could be over £870m, almost half of which (£430m) would be gained by the London pilot authorities. By contrast we estimate the 2018/19 gain to Leeds City Region to be around £41m.

2.4 As a precursor to the introduction of 75% business rates retention nationally in 2020/21, the Government released its business rate pilot prospectus for 2019/20 on 24 July 2018 inviting authorities to submit applications to pilot 75% business rates retention. It was also announced that the 2018/19 pilots, including Leeds City Region, would not continue to pilot 100% retention but could participate in this bidding process. 2017/18 devolution pilots and the Greater London pilot will continue to pilot 100% business rates retention.

2.5 **Appendix 1** describes Business Rates as a tax and the Business Rates Retention Scheme.

## 3 Main issues

### 3.1 2018/19 Leeds City Region Business Rates Retention Pilot

3.1.1 Since 2013/14 Leeds has been a member of the Leeds City Region Business Rates Pool along with the other four West Yorkshire Authorities, Harrogate and York which has been able to utilise the levies of the 3 tariff authorities within the Pool, about £3m to £4m each year.

3.1.2 In December 2017, Government notified the Council that the Leeds City Region Business Rates Pool bid to pilot 100% Business Rates Retention in 2018/19 had been successful. The key objectives of the Leeds City Region pilot are to support regional economic growth and the financial stability of member authorities. This pilot scheme allows the Leeds City Region Pool to retain all additional growth in business rates above business rate baselines determined by Government and associated Section 31 grants, whereas currently 50% of that growth is remitted to Government.

3.1.3 For the Leeds City Region Pilot this additional income is estimated to be in the region of £41m, with the Pool retaining 50% (£20.7m) to continue to support and enable regional economic growth. The other 50% (£20.7m) will be allocated to the member authorities themselves to improve financial stability within their authorities. Of this 50% allocated to member authorities, half will be based on each authority's actual additional growth and half will be redistributed by population. At Quarter 1 the overall expected benefit for Leeds, including all revenue streams affected by 100% retention, is around £12m.

3.1.4 Attached at **Appendix 2** is a summary of the benefits, both locally and regionally which are being delivered by the 100% pool.

### 3.2 2019/20 North and West Yorkshire Business Rates Retention Pilot Application

3.2.1 Whilst the change from 100% retention pilots in 2018/19 to 75% pilots in 2019/20 is disappointing, the opportunity to bid for pilot status in 2019/20 still presents the potential for significant additional funding for authorities in comparison to reverting to the standard 50% retention scheme.

3.2.2 Following discussion with members of the existing Leeds City Region Pool and with North Yorkshire County and Districts, a joint 2019/20 pilot has been submitted. The proposed North and West Yorkshire Business Rates Pool offers the opportunity to test 75% retention in a region made up of both unitary and two tier authorities, a total of 14 different organisations. This will enable Pool members and Government to test how to resolve the issues inherent in such an arrangement.

3.2.3 The proposed Pool area has a population of 3.1 million people and an annual economic output of £70.3 billion with 1.4 million jobs and 137,000 businesses. At almost 4,000 sq. miles it covers 8% of England, including the major cities of Leeds, York, Bradford and Wakefield, complemented by diverse and distinctive towns and extensive rural and coastal areas (including three national parks).

3.2.4 It is hoped that a successful bid will demonstrate to Government that local government can work together to share the risks and rewards of increased business rates retention across such a diverse region.

3.2.5 The estimated additional funds available to the North and West Yorkshire region for redistribution are estimated to be around £19m, of which one third would be retained by the new North and West Yorkshire Pool to support regional economic growth by providing support to and working in collaboration with regional partners and two thirds would be allocated to member authorities to support their financial stability, both at an individual and a regional level. In addition tariff authorities, including Leeds, will retain levy amounts that would otherwise be payable to Government. As a consequence the total gain to the North and West Yorkshire region is estimated to be £22.6m. If the pilot bid is successful, the total gain to Leeds could be around £7m.

3.2.6 Leeds, as the lead authority for the proposed pilot, submitted the application on the 25th September 2018 and we expect to hear the outcome of 2019/20 pilot bids alongside the Provisional Local Government Settlement in December 2018. Should the bid not be successful, the authorities of the current Leeds City Region Pool have agreed to continue with a pool, but this would only have access to the levies of the three tariff authorities within the pool, including Leeds.

3.2.7 The application to pilot 75% retention in a North and West Yorkshire pool is for one year only.

**3.3 Continuing Volatility of Business Rates Income**

3.3.1 A key difference between business rates income and grant income is its uncertainty. Although Leeds has experienced growth above the baseline in every year since the beginning of the retention scheme except in 2014/15, from year to year income has been very volatile. This volatility has presented a significant challenge for medium-term financial planning.

3.3.2 The volatility of business rates income is a result of a range of factors that are largely outside the control of local authorities. This also impacts on forecasting the level of provisions required. Each of these factors are dealt with in more detail in **Appendix 3**.

3.3.3 On the 1st April 2018, there were 2,628 appeals outstanding against the 2010 ratings list. During the first six months of the year 851 appeals have been settled, of which 628 have not resulted in changes to rateable values. 29 new appeals and 37 late notified appeals were received in the same time period. At 30th September there are 1,843 outstanding appeals in Leeds, with 18.2% of the city's total rateable value in the 2010 list currently subject to at least one appeal. No appeals have been received to date against the 2017 list, with only 2.5% of the city's total rateable value in the 2017 list currently subject to either a 'check' or a 'challenge', the pre-appeal stages of the new appeals process introduced in 2017.

## 3.4 The Future of Business Rates: 2020 and beyond

**Fair Funding Review**

3.4.1 The Fair Funding Review will set new funding baselines for every authority alongside the introduction of 75% business rate retention in 2020/21.

3.4.2 It will design a new needs assessment methodology for local government, replacing the current redistribution formulae which were designed over 10 years ago and have not been updated since 2013 and the introduction of the 50% Business Rates Retention scheme, since when there have been considerable demographic and other changes.

3.4.3 The Fair Funding Review will address three inter-related strands: Relative Need; Relative Resources; and Transitional Arrangements. Specifically it will consider how the relative needs and resources of local authorities should be assessed at a time when local government funding is increasingly reliant on local resources, rather than central grant, and will consider in detail the factors that drive local authorities' costs to develop a new redistribution methodology. Transitional arrangements will be needed to manage the impact on the funding allocations to individual authorities.

**Business Rates System Reset**

3.4.4 The funding redistribution mechanism designed by the Fair Funding Review and 75% Business Rates Retention are expected to be implemented in England in 2020/21. As local authorities will retain additional business rates income, Revenue Support Grant, Rural Services Delivery Grant, GLA Transport Grant and Public Health Grant will be 'rolled in' to Business Rates Retention and funded from this additional business rates income.

3.4.5 The business rates system itself will be "re-set" for 2020/21. The re-set will reflect new baseline funding levels and business rates baselines for each local authority.

3.4.6 Baseline funding levels will be based on the spending control totals for 2020/21. The business rates baseline established for each authority represents a "starting point" against which the authority can grow its business rates income.

3.4.1 It is anticipated that current equalization arrangements through tariffs and top-ups will continue, as will some sort of safety-net arrangement to protect authorities from severe losses of income from year to year. However, safety nets may no longer be partially funded from levies on growth in tariff authorities, as levies may be abolished.

3.4.2 However, much of the design of the new system is yet to be agreed. A joint MHCLG/LGA steering group has been established to ensure that government and the sector work together. Indeed, local government representatives have recently presented an alternative business rates model for consideration. We await consultations regarding 75% retention and the Fair Funding Review, together these may give further indication as to the direction of travel.

3.4.3 A number of fundamental issues remain to be decided, these include:

- The quantum of funding available;
- The outcome of the Fair Funding Review  and the approach to establishing needs and resources;

- How and how often the system should be reset in future to address divergence from the needs and resources starting position;

- Design issues such as how safety net arrangements should work and how they should be funded, e.g. by levy or by top slice;

- Ways of addressing local authority exposure to appeals risk and volatility; and

- How the new system will engage with the devolution agenda.

**3.5 Influence of Scrutiny Board**

3.5.1 Given the role of Scrutiny to analyse, inspect and advise on the direction of travel of financial matters, we continue to welcome your views. We have responded to consultations from MHCLG and contributed to discussions around the future of local government funding. We have previously passed information to the Board during a period of consultation and will, where possible, continue to seek the Board's thoughts on these key consultations which will determine the future of local government funding.

**4 Corporate considerations**

**4.1 Consultation and engagement**

4.1.1 This report has no direct issues requiring consultation or engagement.

**4.2 Equality and diversity / cohesion and integration**

4.2.1 This report has no direct equality and diversity / cohesion issues.

**4.3 Council policies and best council plan**

4.3.1 Achievement of the priorities identified in the Best Council Plan requires that the Council's financial resources are maximised and associated risk managed appropriately. The understanding of the Business Rates Retention system and the associated risk is therefore essential to ensuring that the City can deliver on its ambitions.

4.3.2 Business rates growth is identified as a key indicator in the 2018/19-2020/21 Best Council Plan. This report gives an outline of the current business rates system which both incentivises growth and undermines it through the appeals process.

**4.4 Resources and value for money**

4.4.1 The funding implications of the current system and proposed future reform are considered in this report.

**4.5 Legal Implications, access to information and call In**

4.5.1 There are no legal implications arising from the issues discussed in this report. The report does not require a key or major decision and is therefore not subject to call-in.

**4.6 Risk management**

4.6.1 The adequacy of resources to meet the Best Council Plan objectives in a sustainable way is identified as one of the Council's corporate risks. The management of business rates risk is a key element of this and is subject to regular review. Detailed monitoring arrangements are in place and key issues are highlighted to Financial Performance Group and to Executive Board monthly.

## 5 Conclusions

5.1 This report gives an overview of the current Business Rates Retention pilot, the application for a Business Rates Retention Pilot in 2019/20.

5.2 This report also gives reasons for the volatility of Business Rates.

5.3 In addition to this, this report looks at Business Rates in the context of the Fair Funding Review and the Business Rates System Reset.

## 6 Recommendations

6.1 Strategy and Resources Scrutiny Board are asked to note the contents of the report.

## 7 Background documents[1]

7.1 None.

[1] The background documents listed in this section are available to download from the Council's website, unless they contain confidential or exempt information. The list of background documents does not include published works.

## 1. Introduction

1.1. At its meeting in June 2018, the Board requested a Business Rates update. To accompany that report this note will provide some background setting out the main elements of business rates as a tax and how the Council retains a portion of the income raised to provide services in the city.

## 2. Business rates as a tax

2.1. Business rates are a tax on all non-domestic property except for those specifically exempted by statute, such as agricultural land. The ratepayer is the occupier of the property unless it is vacant, at which time 'empty rates' become payable by the owner after a short period of exemption.

2.2. Each ratepayer's basic liability to tax is determined by multiplying the Rateable Value of the property by the relevant business rates multiplier and there are then a series of reliefs that can reduce this basic liability depending on the property or the ratepayer's circumstances.

## 3. Rateable Value (RV)

3.1. The Rateable Value (RV) of a property broadly represents the annual rent that can be expected from that property on a given date on the open market as assessed by the Valuation Office Agency (VOA) in accordance with legislation and case-law. Billing authorities like Leeds City Council have no input into this valuation.

3.2. In general the VOA collects rental information from ratepayers in an area and inspects individual properties, using this data to arrive at valuations for each property. However for some types of property a different method has to be used because there is insufficient comparable rental information in an area. These include the 'contractor's method' (a method representing the interest that would be charged on the capital required to replace the premises) or the 'receipts and expenditure method' (where the VOA deem RV to be related to a measure of profits likely to be generated from the property).

## 4. Rating Lists

4.1. Non-domestic rateable properties fall either into a local rating list or the central rating list. There is a single local rating list for each billing authority in England and Wales, and two central rating lists, one for England and one for Wales. The majority of Rateable Value is contained in local rating lists (over 95 per cent across England and Wales). The total Rateable Value in Leeds exceeds £900 million.

4.2. Some properties are deemed by the Secretary of State to form part of a network across the country, such as utilities, telecommunications and the railway network including railway stations. These are listed on a Central List and the business rates yield from these properties is collected by the Secretary of State and paid into the Treasury's Consolidated Fund.

4.3. According to the Local Government Finance Act 2012 all business rates income received from properties on the Central List, along with all income from Central Government's share of business rates from local lists, must be redistributed to local government. In 2016-17 the amount of business rates income credited to the Government's accounts from the Central List was £1.342 billion.

## 5. The Multipliers

5.1. The multipliers, or poundage, are set by Government each year and there are two basic rates, the small business rates multiplier, which, since the 1st April 2017, applies to properties with a Rateable Value below £51,000, and the higher national business rates multiplier for properties above £51,000.

5.2. Every April the small business rates multiplier can be increased by RPI although the Government has the power to limit these increases, which it did in 2014-15 and 2015-16. Billing authorities have no control over the level of the small business rates multiplier. In 2017-18 the Government announced that from the 1st April 2018 the multiplier would only increase by CPI. Authorities receive compensation for income lost as a result of this change. In 2018-19 the small business rates multiplier is 48.0p.

5.3. The higher national business rates multiplier is set so that it theoretically generates sufficient extra revenue nationally to fund the small business rates relief scheme. In Leeds City Council's area this supplement generated an additional £8.34 million in 2017-18. In 2018-19 the national business rates multiplier is 49.3p.

## 6. Reliefs

6.1. There are various relief schemes that can reduce a ratepayer's basic liability depending on the property's or the ratepayer's circumstances. Some of these schemes are mandatory and a billing authority has no choice but to award them if they apply to a ratepayer's circumstances; others are discretionary, with the billing authority having the ability to set its own policy regarding when to award them. A list of the various reliefs is given at **Annex 2** attached to this note alongside their cost in the Leeds City Council area in 2017-18.

6.2. Between the introduction of the business rates retention scheme and 2017-18, Leeds City Council had to meet 49% of the cost of all reliefs. In 2018-19, under the 100% retention pilot, this has increased to 99%. The exceptions are small business rates relief, where 71.1% of the cost to the authority is funded by central government, and those reliefs that have been introduced by the Government since the beginning of the business rates retention scheme in 2013-14, which are fully funded by the Government.

6.3. In recent years there has been concern about the use of mandatory reliefs by ratepayers to evade or avoid taxation, especially mandatory charity relief and empty rate relief.

## 7. Revaluations

7.1. Revaluations of RVs are normally undertaken by the VOA every five years. New valuations are made across the country as at the date two years before those valuations come into effect. So, for example, the last revaluation became effective from 1st April 2017 but was based on valuations assessed as at 1st April 2015.

7.2. When a revaluation takes place the total tax take across the country must remain constant and the multiplier is adjusted to compensate for increased or reduced total RV. A revaluation does, however, redistribute national yield between areas, meaning that regions that have experienced growth in property values above the national average will pay a higher share of business rates than other areas.

7.3. The Government delayed the last revaluation by two years so instead of taking effect on 1st April 2015 it took effect on 1st April 2017. The delay caused some opposition because the valuation date of the previous 2010 ratings list (1st April 2008) was just before the global financial crisis' impact on commercial property, and property values then fell in many areas of the country. The revaluation process is illustrated in a simple model at **Annex 1**.

7.4. Following a revaluation, ratepayers who experience a large increase in their RV will receive transitional relief to cushion the increase, with the relief gradually decreasing over five years. This relief is theoretically funded by restricting the gains that other ratepayers, who have experienced large falls in their RV, experience over the same five years.

## 8. Appeals

8.1. All ratepayers have the right to appeal to the VOA if they consider that their RV has been set too high at the time of the revaluation or if there has been "a material change of circumstance" that they consider should result in the RV of their property being reduced. Appeals can result in reductions being backdated to the point at which the valuation became effective. They can be made by a ratepayer, or their agent, at any time until a year after the next revaluation. Billing authorities have no right to present evidence at an appeal. A more detailed account of the appeals system and how it is affecting Leeds City Council's income from business rates is given at Paragraphs 3 to 8 of **Appendix 3** to the main report.

## 9. The role of the billing authority

9.1. Leeds City Council, as a billing authority, has no role in setting the RV of properties in the city or setting the multipliers and therefore has no role in setting ratepayers' basic liability for business rates. It also has no role in the appeals process when an RV is challenged by the ratepayer.

9.2. A billing authority's role is limited to calculating and collecting the business rates owed by a ratepayer and deciding what rules to set about discretionary reliefs within the statutory framework. Where a ratepayer does not pay their business rates liability to the authority, it has a range of powers to recover the sums owed.

9.3. Before the business rates retention scheme councils collected business rates purely as an agent of the Government passing all the net revenue to the Department for Communities and Local Government. Since 2013-14, however, councils act as both principal and agent, collecting business rates both to keep (a 49% share until 2017-18, and 99% in 2018-19) and to pass to central government (until 2017-18) and the fire authority (1%). As a result councils have needed to set aside funds to make provision to meet the cost of future repayments to ratepayers following successful appeals.

## 10. The 50% business rates retention scheme

10.1. The current Business Rates Retention Scheme (BRR) was introduced in 2013/14.

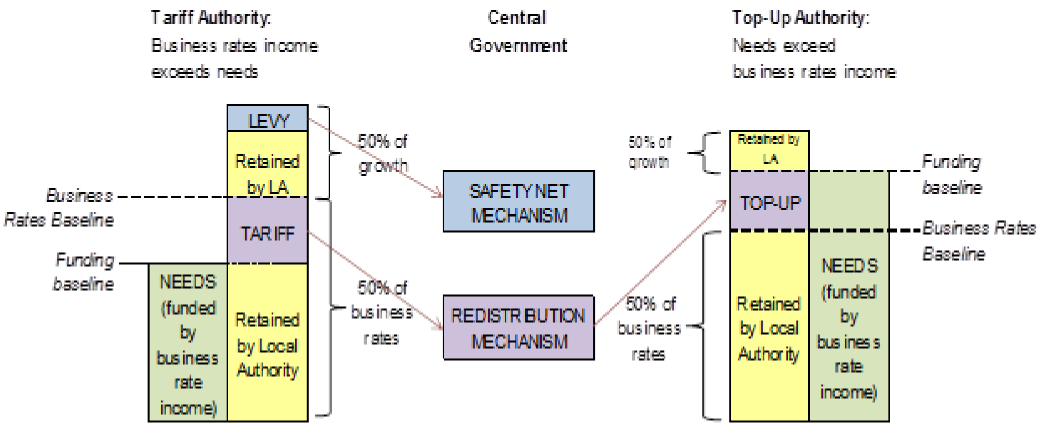
10.2. When the scheme was set up, a 'start-up funding assessment' (now known as the 'settlement funding assessment') calculated how much funding each authority required on the basis of an assessment of needs carried out in 2012/13. A proportion of this is the Funding Baseline for the authority, with the remainder being paid as Revenue Support Grant by the Government. The Funding Baseline increases each year in line with the increase in the small business rates multiplier (RPI until 2017-18, and CPI from 2018-19) until the system is reset. The first reset is planned to take place in 2020-21.

10.3. This funding then comes from two sources: Revenue Support Grant and Business Rates Baseline Funding, also known as an authority's 'local share' of business rates. The Business Rates Baseline is the amount of business rates income the system calculates the authority will achieve. Income collected in excess of this is business rates growth.

10.4. Until 2017-18 the BRR scheme permitted Leeds City Council to retain 49% of locally collected business rates, so 49% of income collected to achieve the Business rates Baseline and 49% of any business rates growth (the Local Share), with the remaining 50% remitted to government as the Central Share, and 1% paid to the Fire Authority.

10.5. However, because authorities' spending needs vary widely and do not match how much an authority will collect in business rates, there are mechanisms within the system to redistribute funding according to authorities' assessed spending needs.

**Figure 1: The Business Rates Retention Scheme**




10.6. This redistribution is achieved through a system of top-ups and tariffs. Tariff authorities like Leeds are expected to collect more business rates income than they need and pay a tariff to government. These tariffs are intended to meet the costs of providing top-up funding to authorities who need more funding than they can generate.

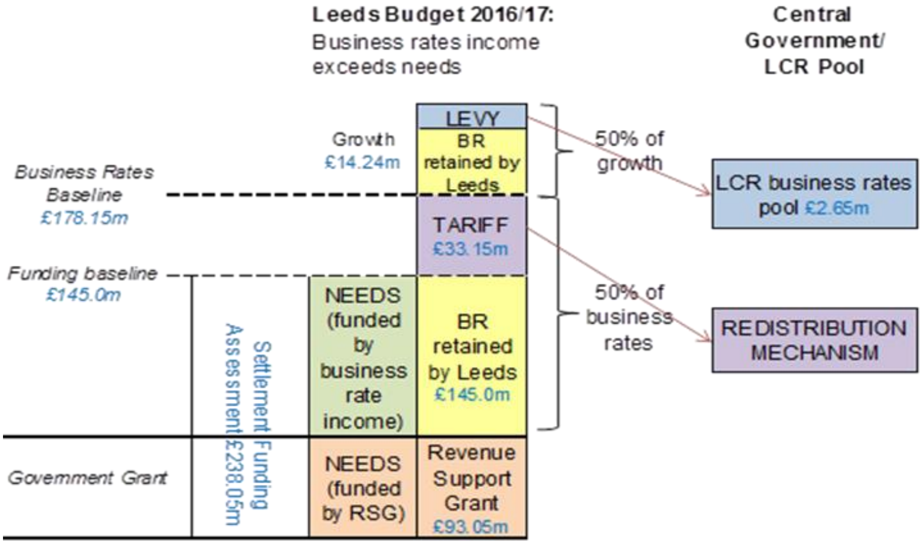
10.7. Tariffs and top-ups are calculated by comparing an authority's Funding Baseline with their Business Rates Baseline, so they do not take account of business rates growth.

10.8. Some authorities could achieve very high levels of business rates growth, whereas others might experience significant decline in business rates income, for example as a result of the closure of a major business in their area. A separate system of levies and safety net payments was established to adjust for such disproportionate gains and losses.

10.9. Authorities experiencing business rates growth will pay a levy on the 50 per cent of growth income they retain. Government use this levy income towards funding a safety net which guarantees that, each year, all local authorities will receive at least 92.5 per cent of their original baseline funding.

10.10. **Figure 2** below shows the budgeted Settlement Funding Assessment for Leeds in 2016/17. The amount actually paid to the business rates pool would have depended on the amount of growth achieved in the year.

**Figure 2: Leeds Budget 2016/17 – Settlement Funding Assessment**




## 11. Business rates pools

11.1. The BRR scheme permits local authorities to voluntarily seek designation as a 'pool', allowing them to pool their resources under the scheme (which they could do anyway), but also ensuring that they are treated as if they were a single entity for the purposes of calculating tariffs, top-ups, levies and safety net payments.

11.2. The Leeds City Region Business Rates Pool was established in April 2013 with the aim of furthering economic development activities across the region. It has seven members:

City of Bradford Metropolitan District Council;
Calderdale Council;
Harrogate Borough Council;
Kirklees Council;
Leeds City Council;
Wakefield Council; and
City of York Council.

11.3. The pool is led by a Joint Committee made up of the leaders of the seven authorities and is administered by Leeds City Council.

11.4. The pool is funded from levies which would otherwise be paid over to central government. Conversely, should any of the member authorities fall into safety net the pool would need to meet any necessary costs as these would not be funded by government.

## 12. The 100% retention pilot in 2018-19

12.1. In 2017-18 the LCR business rates pool successfully applied to become a 100% retention pilot, which meant that the authorities within the pool would retain 99 per cent of business rates growth above the baseline rather than 49 per cent.

12.2. However participating authorities do not simply retain double the resources from business rates income because they agree to forego Revenue Support Grant (worth £46.48m in the case of Leeds City Council) and their top ups, received from Government, are significantly reduced or tariffs, paid to Government, significantly increased (from £13.81m to £136.93m in the case of Leeds City Council). The benefit arises from the increased share of growth retained by the Pool authorities, collectively estimated to be around £41m.

12.3. Half of this ‘additional growth’ is retained by the Pool to be spent on regional projects and half returned to the participating authorities to support their financial sustainability. Half the funding returned to authorities is allocated in proportion to the growth they have achieved and half in proportion to population. This methodology was proposed in response to the Government’s stated dual aims of further retention, i.e. to provide greater incentive to authorities to encourage economic growth and to support financial sustainability in the face of increasing need. Further information about the 100% retention pilot is included in **Appendix 2** to the main report.

## Annex 1: Revaluation

1. Revaluation is the point in the system at which economic changes in property values are reflected in rateable values. Between revaluations, rateable values only change through appeals and physical changes to the property or location. The Government is required at the point of revaluation to reset the multiplier to ensure no more is raised in total business rates, although rates payable for individual properties can change.

### Figure 1.1: Simple Revaluation Model

| | Authority A | Authority B | Authority C | Authority D | Total |
|---|---|---|---|---|---|
| Before Revaluation | | | | | |
| Property 1 | 800 | 250 | 900 | 800 | |
| Property 2 | 1,000 | 1,200 | 900 | 700 | |
| Property 3 | 1,500 | 600 | 1,000 | 600 | |
| Total RV before revaluation | 3,300 | 2,050 | 2,800 | 2,100 | 10,250 |
| Multipier | 0.48 | 0.48 | 0.48 | 0.48 | |
| **Income generated** | **1,584** | **984** | **1,344** | **1,008** | **4,920** |
| After Revaluation | | | | | |
| Property 1 | 1,000 | 300 | 1,000 | 1,011 | |
| Property 2 | 2,000 | 1,300 | 1,000 | 885 | |
| Property 3 | 2,000 | 700 | 1,000 | 758 | |
| Total RV after revaluation | 5,000 | 2,300 | 3,000 | 2,654 | 12,954 |
| New Multiplier | 0.38 | 0.38 | 0.38 | 0.38 | |
| **Income generated (unchanged)** | **1,899** | **874** | **1,139** | **1,008** | **4,920** |
| % increase in RV | 52% | 12% | 7% | 26% | 26% |
| % change in income | 20% | -11% | -15% | 0% | 0% |

2. As the illustration shows, a revaluation will increase the business rates income generated for some authorities but others will lose income. The Government then adjusts each authority's tariff or top-up to ensure that their retained income is the same after revaluation as immediately before.

## Annex 2: Table of Reliefs awarded and their cost to Leeds City Council in 2017/18

| Reliefs | Max relief to be awarded | Amount awarded by Leeds City Council in 2017-18 | Leeds' share of the cost | Comments |
|---|---|---|---|---|
| Mandatory Reliefs | | | | |
| Mandatory Charity Relief | 80% | 28,609,918 | 14,018,860 | Must be awarded to charitable organisations using non-domestic property for charitable purposes |
| Empty Rate Relief | 100% | 17,391,178 | 8,521,677 | Must be awarded to owners of empty properties for up to 3 months (6 months for industrial properties) |
| Small Business Rates Relief | 100% | 25,843,614 | 7,468,804 | 71.1% of the cost of this relief is paid by Government |
| Partially Occupied Premises | N/A | 225,569 | 110,529 | Available for distinct parts of a building certified by the VOA |
| Rural Rate Relief | 50% | 6,166 | 3,021 | |
| less Small Business Supplement | | -8,335,328 | -4,084,311 | Paid by buildings with an RV over £51,000 |
| **Subtotal - Mandatory Reliefs** | | **63,741,116** | **26,038,580** | |
| Discretionary Reliefs | | | | |
| Non-profit making bodies | up to 100% | 426,171 | 208,824 | Available to organisations that are not charitable but are not for profit at the billing authority's discretion as set out in a published scheme |
| Charitable occupation top up | top up to 100% | 110,243 | 54,019 | Can increase mandatory relief to 100% at billing authority's discretion |
| Rural shops | up to 100% | 1,736 | 851 | |
| Small rural businesses | up to 100% | 0 | 0 | |
| Localism Act reliefs | up to 100% | 585,836 | 287,060 | At the billing authority's lawful discretion any ratepayer can receive this relief if the authority believes it to be in the best interests of the council tax payer |
| Hardship relief | up to 100% | 151,493 | 74,231 | |
| **Subtotal - Discretionary Reliefs** | | **1,275,480** | **624,985** | |
| **Government mandated reliefs** | | | | |
| "New Empty" properties | 100% | 10,568 | 0 | |
| "Long term empty" properties | 100% | 96,870 | 0 | |
| Retail Relief | £1,500 | -265 | 0 | |
| In lieu of transitional relief | N/A | -2,271 | 0 | |
| Rural rate relief | up to 100% | 8,052 | 0 | |
| Local Newspaper Relief | £1,500 | 0 | 0 | |
| Supporting small businesses relief | N/A | 119,271 | 0 | |
| Discretionary scheme relief | N/A | 1,626,979 | 0 | |
| Enterprise Zone relief | £55k | 512,697 | 0 | |
| Pub relief (RV < £100k) | £1,500 | 244,875 | 0 | |
| **Subtotal - Government mandated reliefs** | | **2,616,775** | **0** | All of the cost of these reliefs is funded by Government |
| **Total cost of reliefs** | | **67,633,371** | **26,663,565** | |

# Appendix 2: Leeds City Region Business Rates Pool: 100% Retention Pilot 2018/19

Leeds CITY COUNCIL

Members of the Leeds City Region Business Rates Pool bid successfully to pilot 100% business rates retention in 2018/19, resulting in estimated additional business rates income of around £41m being retained in the region.

The Leeds City Region 2018/19 Pilot has two complementary aims:

- **To support and enable regional economic growth; and**
- **To improve financial stability in member authorities**

Of the estimated gain to the LCR the Pool will retain 50% (£20.7m) to continue to support and enable regional economic growth. The other 50% (£20.7m) will be allocated to the member authorities themselves to improve financial stability within their authorities. Of the 50% allocated to member authorities, half will be based on each authority's actual additional growth and half will be redistributed by population.

This briefing note outlines the Pool's progress in achieving these aims and explains the development of our approach to allocating funds to regional projects.

## Regional Economic Growth

The Business Rates Pool continues to build on more than a decade of successful economic collaboration and partnership, retaining a further 50% share of this additional growth income to continue to support and enable regional economic growth.

The aims identified in the 100% pilot bid included delivering significant additional regional investment, with a continued focus on culture and sport, reflecting the economic importance of both these sectors to the direct visitor economy but also in making the region an attractive place for inward investment and improving quality of life. These objectives are very much aligned with the Government's Northern Powerhouse Strategy, which seeks to boost local economies by investing in skills, innovation, transport and culture.

Following the announcement by Government at the end of 2017 that Leeds City Region had been selected as a pilot to retain 100% of growth above the business rates baseline in 2018/19, a new and revised approach to project selection and fund allocation was developed to ensure the Pool monies contributed as fully as possible to the growth of the Leeds City Region economy and were invested in those projects which would create inclusive growth and contribute to the economic development and regeneration of the area.

In order to allow a revised approach to project selection and fund allocation a Prospectus for Investment was developed by the West Yorkshire Combined Authority, as a leading organisation in driving the region's growth ambition.  The

Business Rates Pool Joint Committee agreed for the Prospectus to be designed around four, previously agreed, key strategic thematic areas: Culture, Sport and Major Events; Enabling Housing Growth; Business Support, Trade and Investment; and Inclusive Growth.

The Prospectus Specifications were developed and finalised through a policy led local authority workshop. This allowed full engagement with local authority partners and a set of co-produced specifications in the spirit of partnership and collaboration. The Prospectus was launched in April 2018 with bids selected by the Committee in July 2018. The selection criteria also aimed to put greater emphasis on the ability of projects to lever in further funding as well as those which would increase business rates in the future and improve the legacy for the Pool.

In 2018/19 estimated funds available to the Pool are £20.7m in-year income and £2.8m in balances brought forward from previous years, in total £23.5m. The successful bids fit into the themed areas accordingly:

| **Percentage of funding, split according to strategic area** | |
|---|---|
| Inclusive Growth | 39% |
| Culture, Sport and Major Events | 34% |
| Business Support, Trade and Investment | 20% |
| Enabling Housing Growth | 7% |
| **Total** | **100%** |

### Case Study 1: Expansion of digital engagement in Leeds

This project forms part of the member council's wider digital inclusion programme, 100% DIGITAL LEEDS, which has an ambitious digital literacy plan to work with community organisations and partners to get people online. By enhancing digital skills for everyone, we can help people to access online services and get the best deals. We can improve digital resilience to help people progress in their existing roles, move into employment, or secure better jobs around the city and region. The project underpins the Council's Inclusive Growth Strategy, which focuses on shaping a compassionate city that has a strong economy benefitting everyone; where inequality and deprivation is reduced; and which acts as a driver to local and regional economic growth.

### Case Study 2: Inclusive Growth in the Leeds City Region – Skills, External Challenge & Connectivity

The Inclusive Growth project will improve the skills of those entering the workplace and ensure that a coordinated approach is taken to support business in understanding the benefits of apprenticeships. It will strengthen the links between schools and business and ensure that apprenticeships and technical education are championed and promoted in schools. This is vital to accelerating productivity, competitiveness and economic prosperity across the region. The broadband aspect will tackle market failure and enhance digital inclusion by targeting investment to specific points in the network which have not received superfast broadband investment to date and are unlikely to in the near future. The project will therefore bring forward critical infrastructure to support both future business growth and wider economic growth.

## Financial Stability in Member Authorities

The remaining 50% of additional income is being shared by the member authorities, 25% in proportion to the business rates growth achieved by that authority and 25% in proportion to population to ensure an element of regional redistribution of the gains realised through that business rates growth.

The Leeds City Region 2018/19 pilot bid proposed that the additional funds retained regionally would enable member authorities to invest in financial sustainability, with a focus on:

- Putting valuable local services on a more stable financial footing
- Building financial resilience
- Putting in place longer term strategies to deliver improvement and transformation

This intention has been borne out by the benefits noted by member authorities, summarised below.

### 1. Putting valuable local services on a more stable financial footing

Single tier authority members have largely focussed on using this 50% share to improve financial stability within their authorities by supporting and improving existing service provision. Members have used this additional funding to manage in year pressures predominantly against social care budgets but also waste collection, and towards social care investment and transformation.

For example, following an Ofsted inspection of Children’s Social Care Services, Wakefield Council recognised weaknesses in the quality of the service provided. The additional funding retained through the 2018/19 business rates pilot enabled the Council to respond positively to these findings and will support rapid improvement across children’s social care, including additional investment in leadership, management and capacity issues in front-line social work. Without the additional retained business rates funding, the Council would have been forced to draw on its limited reserves in order to fund the critical and immediate response.

As a further example, the additional business rates income received has supported the setting of a robust budget for Leeds. This has included the decision to increase the children’s social care budget by almost 8% in response to continuing demographic and inflationary pressures.

## 2. Building financial resilience

Member authorities have identified that the additional business rates income retained has assisted in building financial resilience, including the management of ongoing pressures. This recognises that, without the additional funding, further cuts to services would have had to be made or unplanned use of reserves needed.

For example, Calderdale have been able to use the additional income to contribute towards budgeted savings, therefore limiting any consequent impact on service provision or requiring a further call on reserves. Leeds have budgeted to use a proportion of this income to contribute additional funds to reserves. The reduced need to call on reserves in-year and the ability to sustain, and indeed budget to contribute to, reserves is a key aspect of members medium-term financial planning and longer term financial resilience.

## 3. Longer term strategies to deliver improvement and transformation

The member authorities have identified that investment in medium to long term strategies is key to improving financial sustainability in view of the uncertainty surrounding the national funding landscape post 2019-20.

City of York are considering use of the additional income to assist with delivery of major projects, which are expected to provide economic benefits to the region once complete. Whilst Harrogate have identified that part of the funding will be used to invest in their asset base to improve financial sustainability.

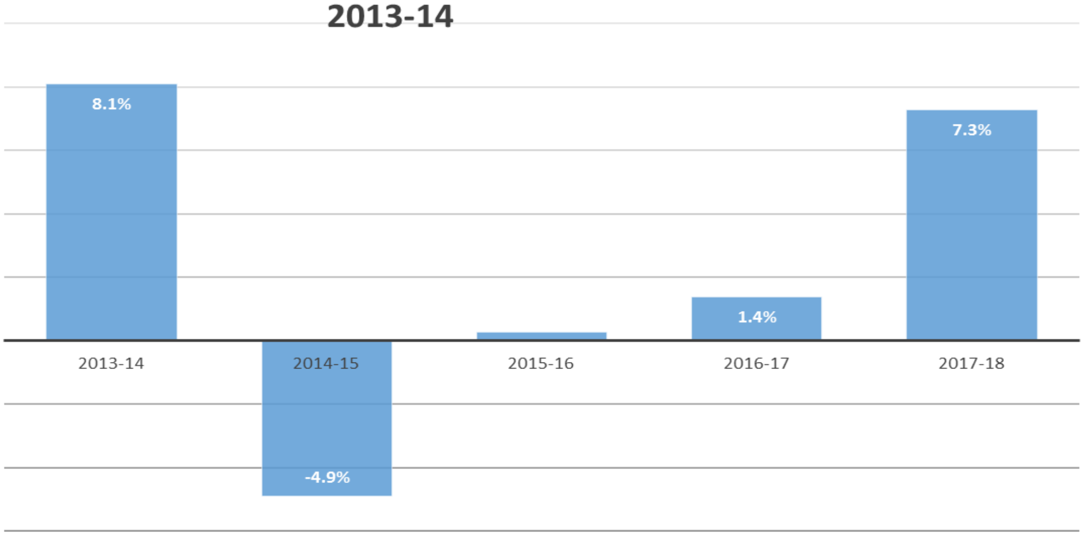
Kirklees have earmarked some of the additional funding from the pilot for social care investment and transformation and at Bradford there has been specific investment into Prevention and Early Help for Children’s Services.

In summary, the Business Rates Pilot builds on many years of successful regional collaboration, providing members and partners with the opportunity to further develop existing relationships and processes to help in the move towards powers, resources and decision-making being undertaken at the optimum level to deliver a growing, inclusive economy.

**Introduction**

1. The key difference between business rates income and grant income is its uncertainty. Although business rates income in Leeds has included growth above the baseline in every year since the beginning of the retention scheme except 2014/15, from year to year the income has been very volatile (see **Figure 1** below). This volatility has presented a significant challenge for medium-term financial planning.

Figure 1: Business rates growth above the baseline since 2013-14




2. The volatility of business rates income is mainly caused by a series of factors that are largely outside the control of local authorities including: -

- Ratepayers' appeals to the Valuation Office Agency (VOA) against their Rateable Value (see **paragraph 3** below).
- The national economic environment affecting local growth, 'Empty Rates Relief' and non-collection of income (see **paragraph 9** below).
- Decisions about valuation methods elsewhere in the country that affect similar classes of properties locally (see **paragraph 13** below).
- Policy decisions by central government that affect business rates income (see **paragraph 17** below).
- Legal decisions affecting matters other than Rateable Value (see **paragraph 19** below).

**Ratepayers' appeals against Rateable Value**

3. Ratepayers have a right to lodge appeals against the valuation given to their property by the VOA, usually because they believe the original value to be wrong or following a material change in the property or local area. The result of an appeal can be backdated to the beginning of the relevant ratings list.

4. Leeds City Council, along with all other billing authorities, have no right to present evidence at an appeal or have any other part in the decision-making process, but must meet its share of any cost, including any backdated refund.

5. The cost of successful appeals has varied significantly from year to year since the introduction of business rates retention in 2013/14 (see **Table 1** below). The total cost incurred in year includes costs relating to the current year and also costs arising in the current year but relating to a previous year. The Council has been able to smooth the costs to some extent with the use of provisions, but their inherent volatility has made forecasting the level of provisions required particularly difficult. The provision we make is a cost to the General Fund and can impact on our revenue position in the year it is set.

**Table 1: Total costs of appeals and Valuation Officer Reports to Leeds City Council** (as at 30 September 2018)

| Year | Total cost incurred in year | Leeds share (%) | Total cost to Leeds' General Fund |
|---|---|---|---|
| **2013-14** | 12,948,390 | 49% | 6,344,711 |
| **2014-15** | 29,070,661 | 49% | 14,244,624 |
| **2015-16** | 39,061,572 | 49% | 19,140,170 |
| **2016-17** | 21,947,570 | 49% | 10,754,309 |
| **2017-18** | 32,623,545 | 49% | 15,985,537 |
| **2018-19** | 5,483,096 | 99% | 5,428,265 |
| **Total** | 141,134,834 | | 71,897,617 |

6. There were a large number of appeals lodged against the 2010 ratings list. By 30 September 2018 there were 21,164 individual appeals affecting approximately 13,060 businesses in Leeds, and 6,224 resulting in reductions to Rateable Value. 1,843 appeals remain outstanding, and 9 are still outstanding against the 2005 list.

The Government, after significant pressure from local government, has made a number of changes to the appeals system to try and reduce this volume of appeals and help local authorities manage the costs, with varying degrees of success, including: -

- In 2016 the Government made statutory provision to allow the VOA to release more information about individual appeals to billing authorities. However, the VOA, part of HMRC, take a very restrictive view of this power and the information remains minimal.

- During the lifetime of the 2010 ratings list, a ratepayer could simply lodge an appeal against their Rateable Value without giving any substantive argument. Local government argued this led to many speculative appeals and a lot of small alterations to the list which were cumulatively having a significant impact on local authority budgets. The Government has reformed the process with a new system coming into force for the 2017 list called 'Check, Challenge, Appeal'. Under this system ratepayers have to put forward a suggested alternative Rateable Values for their property, and give arguments why this Rateable Value should apply. There are also strict rules about when new evidence can be submitted to the process and strict deadlines for each stage of appeals process. Although it is too early to be certain, this appears to have had a significant impact on the volume of appeals, and it is hoped it will greatly reduce delays. However a new portal, allowing ratings agents to lodge appeals on behalf of multiple clients, is to come online in the Autumn of 2018, which may at least partially reverse this trend.

- The Government has discussed with local government the possibility of centralising the cost of some appeals known as 'tone of the list' appeals. These are appeals that result in reductions of Rateable Value stretching back to the beginning of the current ratings list and, under the proposals, would be assumed to be as the result of an error in the original valuation by the VOA which local authorities should not have to fund. If such a system had been in force during the 2010 ratings list it is estimated that, of the 6,224 appeals that resulted in a reduction to Rateable Value, 4,006 would have been funded by a central fund. It should be noted, however, that this central fund would be funded by a top-slice from the funding available to local authorities through the Settlement process and careful analysis is required to see if the savings from not having to meet the costs of 'tone of the list' appeals locally are outweighed by the reduction in Settlement funding.

7. With the introduction of the 2017 ratings list there appears to have been a much reduced level of appeals compared to the 2010 list (see **Table 2** below for a comparison of the volume of appeals at the same stage in the life of the two lists). A number of explanations have been put forward for this difference including: -

- The 2010 ratings was set at a date (1st April 2008) at the height of the commercial property boom, but came into force once the financial crisis had happened, encouraging ratepayers to appeal their high valuations.

- The 2017 ratings is simply more accurate than the 2010 ratings list.

- The new Check, Challenge, Appeal system has deterred speculative appeals from ratepayers and ratings agents.

**Table 2: Comparison of the number of appeals after 18 months of the 2010 list and the 2017 list**

| | No. of appeals after 18 months (in Leeds) |
|---|---|
| **2010 ratings list** | 5,804 |
| **2017 ratings list** | 1,243 |

There remain a number of risks in assuming this situation will continue. As mentioned in **paragraph 6** above, a new portal for ratings agents to lodge appeals is being launched this Autumn and there have been a number of problems with the introduction of the new appeals system for the 2017 ratings list which, when resolved, could see a return to a higher level of appeals being received by the VOA.

8. Taking into account all the uncertainties about appeals, Leeds City Council currently hold provisions against losses from appeals of £12.61m, and estimate maintaining the required level of provisions will cost the Council’s General Fund £8.88m in 2018/19.

**The National Economic Environment**

9. The national economic environment affects the ability of local authorities to generate growth in their area as demand for new premises reduces during an economic downturn, and yet most of the levers that can improve the national economic climate are held by central government.

10. Economic downturns also increase Empty Rate Relief. Although full business rates (known as ‘Empty Rates’) have to be paid by a landlord after a property is empty for 3 months (6 months for industrial properties), there are an increased number of business failures during a downturn, and relief can be claimed indefinitely by a company in administration. In 2013/14, the first year of the business rates retention scheme and still feeling the effects of the financial crisis, in real terms Empty Rate

Relief reduced business rates by £22.61m in Leeds. In 2018/19 it will reduce business rates income by £19.50m and has been reducing for a number of years.

11. Finally there is an increased level of written-off debts during a downturn as it becomes clear that it is not economical to collect money owed for business rates. During the last financial crisis the provisions for non-collection held by Leeds City Council increased from 1% of net amounts billed to 1.2%, although it has returned to 99% collection since. If 1.2% had to be applied to provisions again in 2018/19 it would cost the authority an additional £1.75m.

12. Leeds City Council currently hold bad debt provisions of £6.85m on 31st March 2018 for all as yet uncollected amounts, with the estimated cost to the General Fund of maintaining the required level of provisions being £3.47m in 2018/19.

**Valuation Officer Reports**

13. Weekly the Council receives notices from the VOA instructing the Revenues department to increase, or reduce, a property's Rateable Value. These can be in response to a billing authority report to the VOA about a change to a property (usually resulting in an increase), a change encountered by VOA inspectors or a change in valuation practice outside the Leeds area but affecting a class of property locally and about which the Council has no prior notice.

14. In Leeds, billing authority reports to the VOA, usually as a result of visits by Council inspectors, increased business rates by approximately £7.27m in 2017/18, with the Council's share of that income being £3.56m.

15. The most recent example of action in an area outside of Leeds affecting properties within the Leeds area was the reduction of Rateable Value, by around 50%, of all purpose-built medical centres in 2015. The reductions were backdated to 1st April 2010 because the method of valuation was changed and this cost Leeds City Council an estimated £7.5m.

16. The future cost of Valuation Officer Reports cannot be estimated reliably from year to year and therefore it is impossible for the Council to hold any provisions for these losses using proper accounting practices. However, taking this uncertainty into account, we currently estimate that Valuation Officer Reports will cost Leeds City Council's General Fund £1.32m in 2018/19.

**Central Government policy decisions that affect business rates income**

17. Local government usually receives compensation for Government policy decisions that directly affect business rates income. For example Government recently mandated a series of reliefs that were to be given by billing authorities to help

businesses transition to the new 2017 ratings list. The Government meets the cost of lost income to authorities through a grant. The Government also changed the rate by which the multiplier increases from the Retail Prices Index (RPI) to the Consumer Prices Index (CPI) and pays the losses this causes to councils through a grant.

18. However there are other policies that have affected business rates income that are not compensated for. For example, when a school is controlled by a local authority it must pay 100% of business rates but an Academy School can claim 80% Mandatory Charity Relief (along with private schools). As the number of Academies increases, this reduces income to the local authority for which there is no compensation.

**Legal decisions affecting matters other than Rateable Value**

19. In recent years there have been a number of legal decisions that have affected matters other than Rateable Value and yet have a direct impact on local authorities' business rates income and challenge long-held general practice.

20. For example, in 2016/17 a case was taken to the Court Appeal arguing that an office covering two floors in an office block, but separated by a common staircase should be treated as two separate properties rather than one (the 'Mazaars' case). This has had a significant impact on some authorities' business rates income where a single property becoming two separate properties has resulted in both becoming entitled to Small Business Rates Relief. In Leeds it was estimated that this change of practice would have little direct effect on our Revenues, because our properties tend to have high values and therefore Small Business Rates Relief is not an issue, and also in some cases two separate properties generated more income than a single property. However the Government has since introduced legislation to override the decision of the Court of Appeal, but only where it adversely affects the ratepayer. This will have an adverse effect on the Council's income.

21. There is also a legal case being brought by a number of Foundation Hospital Trusts arguing that they should be treated in a manner similar to Academies and receive 80% Mandatory Charity Relief backdated to 1st April 2010. Legal advice has been sought by CIPFA and stated that the argument put forward by the hospitals should not be successful and therefore, following proper accounting practice, no provisions have been made. However if the case is successful it is estimated this could cost Leeds City Council as much as £5.43m, with an ongoing cost of approximately £0.75m a year.