LONDON COUNCILS

London Business Rates Pilot Pool 2018-19 – Draft Prospectus

Introduction

1. This draft prospectus sets out how it is envisaged that the London Business Rates pilot pool would work in practice, were the 33 Leaders/Mayors and the Mayor of London to agree to form a pool in 2018-19.

2. The Government established pilots in 6 areas of the country in April 2017, including London where the GLA's level of retained business rates increased from 20% to 37%, replacing TfL transport grant and Revenue Support Grant. An expanded London pilot in 2018-19, which would require all 33 London Boroughs and the Mayor of London to agree to pool, would seek at least to replicate the common features of the deals in the other 5 pilot areas: Greater Manchester; Liverpool City Region; West Midlands, West of England and Cornwall.

Founding principles

3. It is proposed that there are two founding principles that would require agreement at the outset by all pooling members.

1) Nobody worse off

4. The first founding principle of the agreement would be that ***no authority participating in the pool can be worse off than they would otherwise be under the 50% scheme***.

5. DCLG civil servants have indicated an expectation that a London pilot pool would be underpinned by the same safety net arrangements and "no detriment" guarantee currently offered to existing pilots in 2017-18. This ensures that the pool, as a whole, cannot be worse off than the participating authorities would have been collectively if they had not entered the pool.

6. Existing Enterprise Zones and "designated areas", along with other special arrangements, such as the statutory provision to reflect the unique circumstances of the City of London, would be taken into account in calculating the level of resources below which the guarantee would operate. For boroughs in an existing pool[1], DCLG have also indicated that the basis of comparison would include the income due from that pool.

7. The impact of the guarantee would be to ensure that the minimum level of resources available for London, as a whole, could not be lower than it would otherwise be. In order to then ensure that no *individual authority* is worse off, the first call on any additional resources generated by levy savings and additional retained rates income,

[1] Of the 33 London authorities in 2017-18 this includes Barking & Dagenham, Havering and Croydon

would be used to ensure each borough and the GLA receives at least the same amount as it would have without entering the pool.

8. The level of Revenue Support Grant (RSG) for each borough has been set by the 4-year settlement (to 2019-20). For each borough this would be replaced by retaining additional rates (just as the GLA has done this year). In addition Public Health Grant (PHG) and the Improved Better Care Fund (iBCF) would also be replaced by rates, leading to an adjustment of expected baselines and top-ups or tariffs (as appropriate). While the composition of each borough's "core funding" (retained rates plus RSG, Public Health Grant and iBCF) will therefore change, the overall quantum will not. This revised position is then the baseline against which the "no detriment" guarantee is calculated. Each borough – whether its business rate income grows or declines during the operation of the pilot pool – will receive, as a minimum, the same amount of cash it would have received under the existing 50% system.

2) All members share some of the benefit

9. Growing London's economy is a collective endeavour in which all boroughs make some contribution to the success of the whole. In recognition of the complex interconnectedness of London's economy, it is proposed that the second proposed founding principle would be that ***all members would receive some share of any net benefits arising from the pilot pool.***

10. The net financial benefit of pooling consists of retaining 100% of growth (rather than 67% across London under the current scheme), and in not paying a levy on that growth (which tariff authorities and tariff pools currently pay). The principle would mean that *any aggregate growth* in the pool overall – because of the increased retention level – would generate additional resources to share, with each pooling member benefit to some extent.

11. In addition, it could be possible to transfer of some Central List properties located in London (for example, the London Underground network) to the London pool, thereby increasing the capacity of the pool to benefit from growth on those properties. This would be explored with government as part of the pool negotiation.

Sharing the benefits of pooling

Objectives

12. Assuming the pool generates some level of additional financial benefit, the question of how to share this will be central to any final pooling agreement. The latest estimated net benefit to participating in the pool is expected to be in the region of £230 million in 2018-19, based on London Councils' modelling using boroughs' own forecasts.

13. Discussions with the Executive and informally with Group Leaders, have identified four objectives that could inform the distribution of such gains:

- **incentivising growth** (by allowing those boroughs where growth occurs to keep some proportion of the additional resources retained as a result of the pool)
- **recognising the contribution of all boroughs** (through a per capita allocation)
- **recognising need** (through the needs assessment formula); and
- **facilitating collective investment** (through an investment pot designed to promote economic growth and lever additional investment funding from other sources).

14. A “pure” way to ***incentivise growth*** would be for the London local authorities where growth occurs to retain the full benefit, including any levy savings, after ensuring all authorities had been brought up to the level of funding they would otherwise have received under the current 50% scheme. This option would see the greatest reward go to those whose business rates grow, but would produce no net benefit for the minority of boroughs where no (or negative) growth is expected.

15. A simple ***per capita distribution*** using the latest population estimates from the ONS[2], would recognise the requirement to work collectively to grow London’s economy and ensure a share of the benefit for all authorities.

16. While the role of incentivising growth is important, some recognition of ***increasing need*** and demand for services has also been identified as a priority. Economic and business growth also drives, and is reinforced by, increasing demand for services across the capital. One measure that could be used to distribute any net benefit could therefore be to reflect the Government’s current assessment of need: Settlement Funding Assessment (although this will clearly be subject to change in future following any “Fair Funding” review).

17. Recognising the requirement for ***collective investment*** to promote further economic growth could be facilitated by retaining resources in a strategic investment pot. Such an approach is also likely to be viewed favourably by Government, as it helps address the original policy objectives behind business rate retention and would require closer working and governance arrangements to be developed between the Mayor and the 33 borough Leaders for the purposes of establishing and operating the pool, and in delivering the desired outcomes.

18. Individually, these principles would drive very different distributions of the direct benefits received by boroughs. The pure “incentives” approach would obviously favour those with the highest growth rates. Distribution according to SFA and population creates a more even spread of resources, but arguably provides less incentive to promote growth, and may therefore not optimise the opportunity for London in the longer term. It is proposed that a distribution mechanism should be a blend of all four of these objectives.

[2] The 2014-based Sub-National Population Projections for 2018

Options for weighting

19. In deciding the balance between the four objectives, and therefore the relevant weighting between the measures listed above, there are countless possible variants. However, following initial discussions with Group Leaders, four potential options are illustrated below:

    A. An even split percentage between the four pots (25:25:25:25).

    B. Reducing the strategic investment pot to 10% of the total, while the “reward”, “needs” and “population” pots are equally weighted (30:30:30:10).

    C. Greater “incentive weighting” with equal weighting for the other three pots (40:20:20:20)

    D. Greater “needs” and “population” weightings (each 30%) with equal remaining weightings of 20% for “incentives” and “investment” pots (20:30:30:20)

20. The potential net benefit for each borough from this model – based on the latest information available on estimated income for 2018-19 – is set out in the charts at Appendix A and summarised in the table below. Under the 100% pilot pool it is estimated that there might be £470m of retained growth: £229m more than under the 50% scheme (after ensuring no borough is worse off as a result of participating).

Table 1 – Distribution options for estimated £229m net benefit of pooling in 2018-19

Option	A	B	C	D
GLA share (£m)	£62	£75	£66	£66
Aggregate borough share (£m)	£110	£131	£117	£117
Investment pot (£m)	£57	£23	£46	£46
TOTAL (£m)	**£229**	**£229**	**£229**	**£229**
Minimum borough gain (£m)	£1.2	£1.5	£1.1	£1.4
Maximum borough gain (£m)	£12.4	£14.9	£19.6	£10.1

Source: London Councils’ modelling using London Boroughs’ data supplied by borough finance directors or where not available by applying the latest 2017-18 forecasts to 2018-19.

21. Leaders are invited to consider the options in the context of balancing the objectives of incentives and need, and be in a position to indicate a preference for the weighting by the October Leaders’ Committee and Congress meeting.

Investment pot principles

22. If an “investment pot” is created, the final amount of funding available will not be known until after the final audited outturn figures are confirmed for 2018-19 – likely to be in September 2019. A final methodology for allocating resources to specific projects is therefore not necessarily required at the outset of the pooling agreement. However, it will be important to consider the criteria and process for developing and approving proposals, in order to maintain a balance between simplicity of operation, strategic impact and broad appeal.

23. More immediately, it is proposed that the founding pool agreement includes *guiding principles* for the use of such an investment pot, for approval by all members of the pool. As such, it is proposed that investment proposals approved would:

- promote increased economic growth, and increase London's overall business rate income; and
- leverage additional investment funding from other sources.

24. It is proposed that these principles would be agreed as part of the founding agreement for the pool – and would therefore require unanimous support. It is then assumed that decisions on the allocation of the pot would be taken by the Congress of Leaders and the Mayor annually in accordance these principles.

Governance

25. Leaders and the Mayor have previously endorsed the view that commitment to the collective management of devolved business rates would require unanimous support, and have identified Congress as the appropriate body formally to recognize those commitments.

26. However, the Congress of Leaders has no power to bind authorities. Local decisions would need to be taken by each authority to agree the terms of the legal agreement which would underpin the arrangements.

27. Participation in a pool in 2018-19 would not bind boroughs or the Mayor indefinitely. As with existing pool arrangements, the founding agreement would need to include notice provisions for authorities to withdraw in subsequent years.

28. Subsequent decisions (e.g. the application of a strategic investment pot) could be subject to the voting principles designed to protect group, sub-regional or Mayoral interests, such as those previously endorsed by Leaders and the Mayor in the London Finance Commission (both 2013 and 2017), and set out in London Government's detailed proposition on 100% business rates in September 2016. This will require the development of formal terms of reference for Congress to underpin collective decision-making in accordance with the decision principles previously agreed. As mentioned in paragraph 22, any such decisions would not be required until the level of available resources is confirmed after all accounts have been audited (i.e. September 2019).

29. Establishing a business rates pool in London will require each authority participating in the pool to agree to do so; and to also agree the terms upon which they will participate jointly with other members, including to appoint a lead authority as accountable body for the pool and to decide how the pool should operate. While the legal framework for the operation of the pool is yet to be determined in consultation with the authorities and the Government, should the London local authorities each resolve to delegate the exercise of their relevant functions to a joint committee, such

as Leaders' Committee, this would require the Leaders' Committee governing agreement to be formally varied which requires the agreement of all 33 authorities for the variation to be effective.

Accounting and reporting arrangements

Lead authority

30. As in other existing pools, a lead authority would be required to act as the accountable body to government and would be responsible for administration of the pooled fund. The same authority – or another – could also hold any properties transferred to London from the Central List, as there is currently no legislative provision for a "regional list". The role of the lead authority/authorities could receive political oversight from the Leaders and Mayor of London; London Councils and the GLA could provide technical support.

31. The lead authority responsibilities from existing pool agreements typically include:
    - Receiving payments from pool members and making payments to central government on behalf of pool members on time.
    - Maintaining a cash account on behalf of the pool and paying interest on any credit balances.
    - Liaising with and completing all formal pool returns to central government.
    - Administering the schedule of payments between pool members in respect of the financial transactions that form part of the pool's resources.
    - Providing the information required by pool members in preparing their annual statement of accounts in relation to the activities and resources of the pool.
    - Leading on reporting to understand the pool's position during and at the end of the financial year.

32. The lead authority would, therefore, be responsible for the net tariff payment to central government as well as the internal tariff and top up payments to the pool authorities. The partner billing authorities would make payments to the lead authority based on an agreed schedule, which could be made on the same schedule of payment dates agreed for tariff and top up payments.

33. It is likely that the resources required to perform this function would be 1 FTE post, which would likely be a senior accountant with considerable experience and understanding of collection fund accounting and the business rates retention scheme.

Reporting

34. In order to perform the functions of the lead authority, each member authority of the pool would need to provide timely information as well as making payments on time to the agreed schedule.

35. Forecast (NNDR1) and outturn (NNDR3) figures will still need to be produced, as per the existing NDR Regulations 2013, in order to enable budget processes to be complete, payments determined that need to be made to the lead authority and to government (by the lead authority) and to the GLA during the course of the year as well as transfers to General Funds.

36. The pool would use NNDR1 returns to establish the schedule of payments to be made to the lead authority and for the calculation of any notional levy savings to be made. However, it would not be until the outturn position is known (the NNDR3 form) that actual reconciliation would be made and the final growth/decline for the pool as a whole, and individual pool members, would be established. This will be in September 2019 after accounts have been audited for the financial year 2018-19.

37. The NDR income figures in the forms determine the growth/decline for that year and it is this figure that would determine the amount to be shared between pool members or between local authorities and central government in the current system.

The treatment of appeals

38. Variances against forecast in the non-domestic rating income are reflected in the forecast surplus or deficit of the collection fund at the start of the following year (information which is collected as part of NNDR1). Appeals provisions impact each year on the calculation of the NNDR income figure: a higher provision in a year, everything else being equal, reduces the NNDR income figure determining growth/decline for that year.

39. A separate pooled collection fund would be required to be established that would sit with the lead authority. A key issue will be the treatment of Collection Fund surpluses and appeals provisions within the pool. The key principle pooling authorities would have to agree is that the benefits (or costs) of actions undertaken by the boroughs prior to entering the pool should remain with the borough so that no borough can be worse off than they would have been under the 50% scheme. So – for example – if a provision established in 2013-14 proves not to be necessary and is released during 2018-19, the borough should receive at least as much as it would have under the existing 50% scheme, plus its share of any additional retained revenues.

40. The pool's collection fund account would have to continue beyond the life of the pool until all appeals relating to the pool period were resolved. Provisions released after the operation of the pilot would be distributed on the basis of the pool's founding agreement – i.e. the borough where the provisions originated would receive at least as much as it would under the 50% retention system, with any additional resources being shared according to the pool's agreed distribution mechanism. There would therefore be no "gaming" benefits to individual boroughs of setting higher (or lower) provisions. The lead authority would be responsible for administering this.

41. Further work will be undertaken to set out how the accounting and reporting requirements would work in practice, which is likely to mean either additional lines on

the existing NNDR form or an additional “London pool” form administered by the lead authority. This will be confirmed as part of the final pooling agreement.

Timetable

42. A 2018-19 pilot would require agreement with Government at or around the Autumn Budget – likely to be in November 2017. This, in turn, would necessitate initial agreement in principle at the meetings of the Leaders’ Committee and Congress of Leaders on 10th October 2017 on the basis that each authority had been consulted and had either previously authorised that decision to proceed with participation in the pilot, or that their authority’s Leader had been given delegated authority to do so.

43. This draft prospectus forms the basis for internal consideration and discussion within each of the 34 prospective pooling authorities over the summer, in order for each Leader and the Mayor to be in a position to consider each authority’s in principle position about the pool and to indicate this at the Congress of Leaders on 10th October, in the event that the Government wishes to pursue a pilot pool in London.

44. A final detailed pooling agreement would then be negotiated with DCLG, with the likely deadline being the time the Local Government Finance Report is published in February 2018. Respecting the tight timeframes for the pilot’s commencement in April 2018 and the likelihood that an agreement would need to be reached with the Government in the Autumn, it is probable that further local decisions required from the 34 prospective pooling authorities relating to the legal framework to be implemented, could follow in the intervening period but all these matters would need to be resolved in a timely manner prior to April 2018 to allow for implementation.

LONDON COUNCILS

Appendix A – Modelled Options

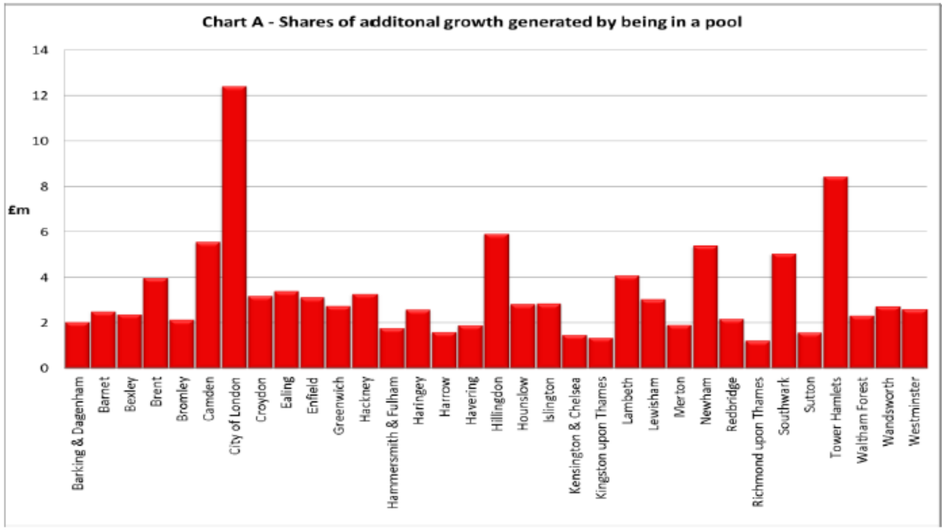
1. This appendix shows the impact of varying weightings on the overall distribution of any net additional benefit from being in the pool. It assumes the latest growth estimates for 2018-19 across London boroughs (combining where available figures from a recent survey of treasurers and, where not available, the latest published estimates of growth in 2017-18 applied as if in 2018-19). The overall net benefit being distributed is £229m.

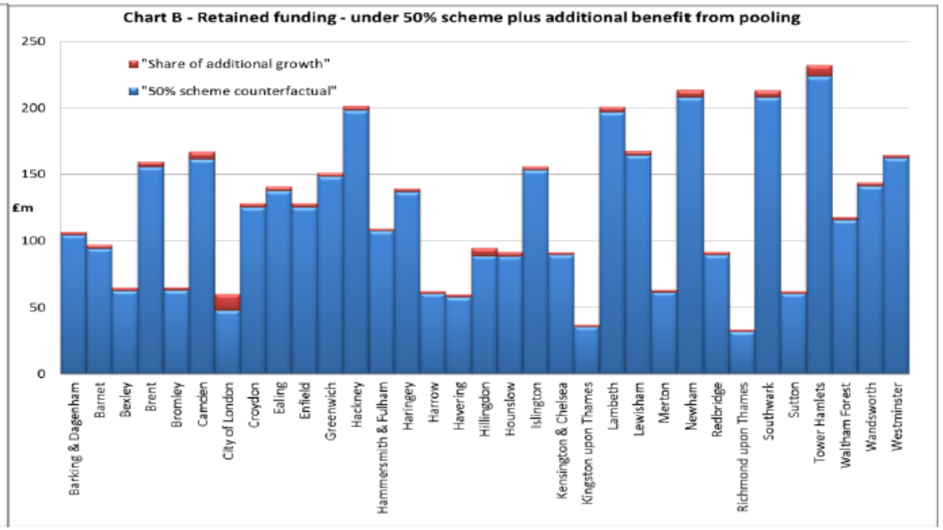
2. The charts below show the distribution of growth under four different scenarios for the relative weightings between the four potential distribution "pots" described above - i.e. incentives; needs (SFA); population (ONS 2018 projection) and investment pots.

    - Option A: weights each pot at 25%
    - Option B: Incentives (30%), Needs/Population (30% each) and Investment (10%)
    - Option C: Incentives (40%), Needs/Population (20% each) and Investment (20%)
    - Option D: Incentives (20%), Needs/Population (30% each) and Investment (20%)

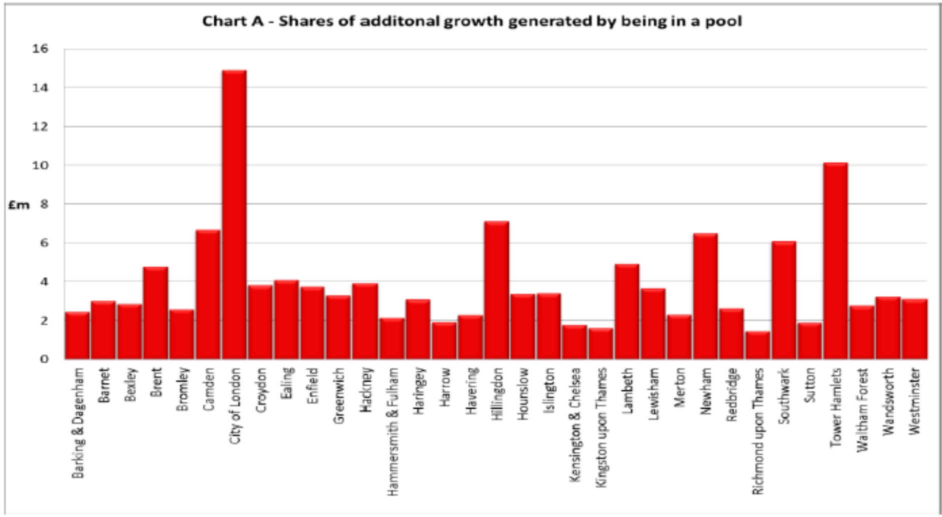
3. For each option we have illustrated both the cash gain for each borough (red, left-hand bar charts) and the marginal gain over the retained funding under the existing 50% position (red and blue, right-hand bar charts).

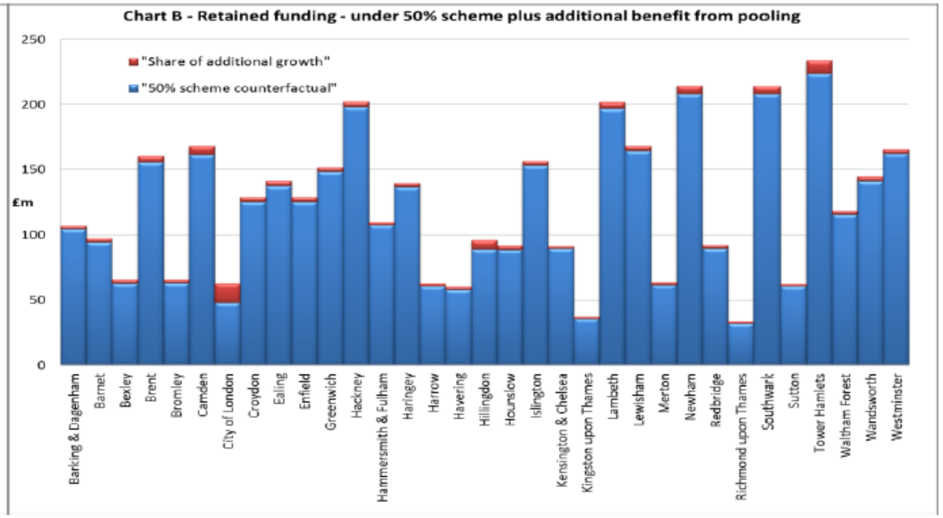
Option A: Equal split between pots – 25%/25%/25%/25%



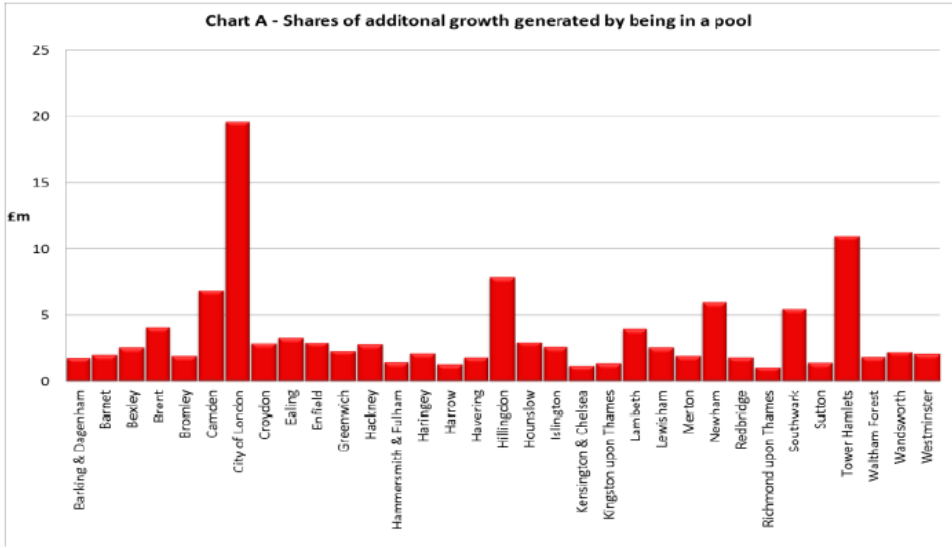


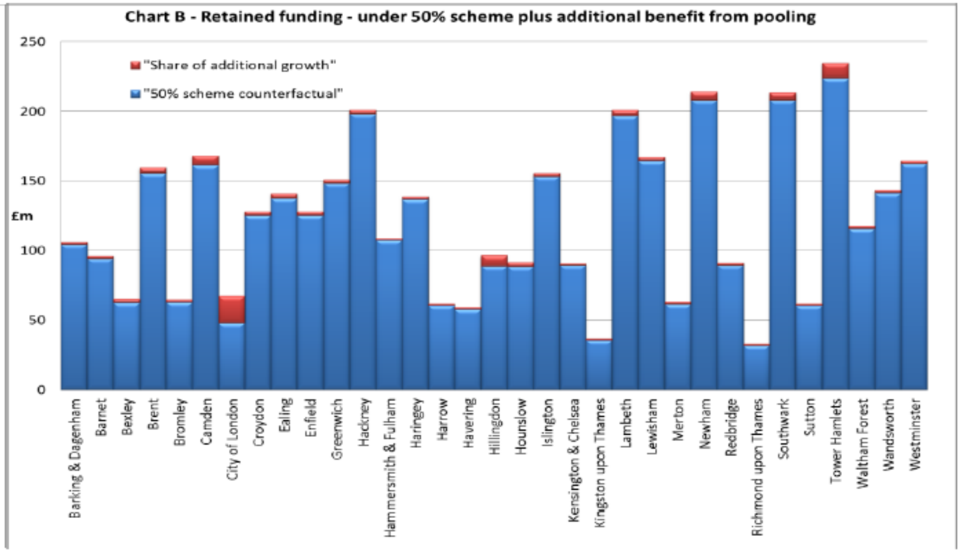
Option B: Reduced "investment pot": 30%/30%/30%/10%





Option C: Greater “incentive” weighting: 40%/20%/20%/20%





Option D: Greater “Needs/population” weighting: 20%/30%/30%/20%