Birmingham City Council
Report to Cabinet
14TH NOVEMBER 2023

Subject:	TRAILBLAZER 100% BUSINESS RATES RETENTION AGREEMENT FOR THE WEST MIDLANDS
Report of:	Interim Director of Finance (Section 151 Officer) – Fiona Greenway
Relevant Cabinet Member:	Councillor Brigid Jones – Finance & Resources
Relevant O &S Chair(s):	Councillor Jack Deakin - Resources
Report author:	Peter Sebastian, Interim Head of Financial Planning

Are specific wards affected? If yes, name(s) of ward(s):	☐ Yes	☒ No – All wards affected
Is this a key decision? If relevant, add Forward Plan Reference: XXXXXX/2023	☒ Yes	☐ No
Is the decision eligible for call-in?	☒ Yes	☐ No
Does the report contain confidential or exempt information? If relevant, provide exempt information paragraph number or reason if confidential:	☐ Yes	☒ No

1 Executive Summary

1.1 The West Midlands have agreed a Trailblazer Devolution Deal with central Government. One element of this devolution deal is the principle of 100% retention of Business rates for the region. This paper is seeking Cabinet approval for the Memorandum of Understanding (MOU) between authorities within the West Midlands Combined Authority area. Cabinet approval is a requirement set out by the Department for Levelling Up, Housing and Communities (DLUHC) to confirm the proposed 100% retention of Business Rates proposal into law.

1.2 The proposed MoU is the result of substantial negotiations between regional representatives and the Department for Levelling Up, Housing and Communities (DLUHC). The key features of the proposed MoU are:

1.2.1 Extension of 100% Rates retention pilot within the region for ten years from 2024/25.

1.2.2 The deal is conditional upon the West Midlands authorities continuing to provide an annual share of business rates growth to the West Midlands Combined Authority (WMCA).

1.2.3 There will no longer be a regional no-detriment clause. However, there will continue to be a local no-detriment clause, providing support based upon local agreement.

2 Recommendations

That the Cabinet:-

2.1 Notes the performance to date of the existing West Midlands 100% Business Rates Retention pilot (summarised in **Section 3** of this report)

2.2 Approve the Memorandum of Understanding (MoU) with Government regarding the offer of 10-year, 100% Business Rate Retention for the West Midlands, in accordance with the Trailblazing Devolution Deal (summarised in **Section 4** of this report) on the basis that it offers a broad continuation of the principle of full Business Rate retention which has financially benefitted the Council to date. This approval is required by the end of November 2023 to enable this deal to proceed.

2.3 Authorise the Interim Director of Finance (Section 151 Officer) to sign the MoU on behalf of the Council.

2.4 Authorise the Interim Director of Finance (Section 151 Officer) to approve the local No Detriment agreement that is to be agreed with the other Constituent Local Authorities of the WMCA, as described in paragraph 4.10.

2.5 Notes that the provisional value of WMCA share, which is confirmed on an annual basis, will be agreed by the Section 151 Officers for WMCA and the West Midlands authorities to help place the Combined Authority on a sustainable financial footing, as set out in paragraph 4.4.6.

3 Background

3.1 In 2017, the seven Constituent Local Authorities of the WMCA entered into a pilot agreement with Government allowing them to benefit from retaining 100% of the Business Rates generated within their respective regions, compared with 50% nationally, in exchange for forgoing Revenue Support Grant ('RSG'). (RSG is a central government grant given to local authorities which can be used to finance revenue expenditure on any service. The amount of RSG to be provided to authorities is established through the local government finance settlement and is most often used for authorities that generate lower levels of Council Tax within their area, to top up funding.) Under the 2017 pilot agreement, 1% of local business rates income under both the national and pilot schemes was retained by the West Midlands Fire and Rescue Authority.

3.2 Other Mayoral Combined Authority areas also adopted broadly similar 100% pilot arrangements over time.

3.3 Whilst initially expected to be a short-term pilot in advance of the national roll-out of 100% business rates retention, the arrangement has been rolled forward under the same terms and conditions annually and remains in effect during 2023/24.

3.4 As part of the West Midlands Trailblazer Deeper Devolution Deal, Government has offered to Local Authorities forming both West Midlands and Greater Manchester Combined Authorities only, the opportunity to extend the arrangement on longer term basis; for ten years commencing April 2024.

2017 Pilot Background and Performance

3.5 As detailed above, the pilot was initially expected to be in place for only one or two years and represented a fundamental change to the pre-2017 arrangements, where 50% of business rates were retained locally and the remainder was remitted centrally to HM Treasury; whilst Revenue Support Grant (RSG) was also received from Central Government by each West Midlands authority.

3.6 The pilot arrangements essentially meant RSG was foregone in exchange for the remaining 50% Central Share of business rates now being retained locally, rather than remitted to HMT, with the result that any growth in business rates was therefore retained locally.

3.7 Given this fundamental shift in the Local Authority financing mechanism and associated risk allocation, Government provided a “no detriment guarantee”. This guarantee meant that each financial year, DLUHC compared funding generated under this pilot (i.e. 100% business rates retention) against funding levels if the pilot did not exist (i.e. mirroring the arrangements for other authorities in which 50% of business rates were retained within the region and any funding gaps covered with additional RSG from Government). This calculation was carried out across the pilot area – i.e. all seven constituent Local Authorities within the WMCA. In the event that, collectively, these seven authorities were worse off, Government agreed it would directly reimburse the pilot as a whole (i.e. to ensure no detriment).

3.8 If, however, there were instances of isolated detriment (i.e. some Local Authorities worse off but the region as a whole benefitting in aggregate), the collective no detriment clause would not be triggered, and so no compensating funding from Government would be received. However, the arrangement agreed with Central Government stipulated that those Authorities in a gain position would directly reimburse those in a detriment position

3.9 The pilot also contained an enhanced “safety net” level for each West Midlands authority of 97% of its Baseline Funding Level, compared with 92.5% nationally, to reflect the increased exposure to Business Rates risk by way of 100% retention. The safety net is the level below which Government guarantees an authority's income from business rates will not fall.

WMCA Share of the existing Business Rates Retention Pilot

3.10 The 2016 Devolution Deal with Government (which was effectively the catalyst for the WMCA and the associated Investment Programme) included an arrangement whereby the Combined Authority would benefit from a share of Business Rates Growth in the region.

3.11 At the time of the 2016 Devolution Deal, Local Authorities (and the WMCA) were in the national retention system in which local areas retained 50% of their business rate income and 50% was paid back to HM Treasury.

3.12 The move from the national 50% arrangements to the 100% retention arrangements complicated the calculations of Business Rates Growth and hence the amount due to the WMCA. The Local Authorities agreed to fund (from Business Rates gains) the WMCA Investment Programme income profile in line with the original financial modelling expectations; that being £1.5m in year one growing incrementally by £1.5m each year. This arrangement, which is subject to annual agreement, remains intact and the sum due to the Combined Authority from the seven constituent local authorities for 2023/24 totals £12.0m.

3.13 The increasing value of the anticipated contribution is included in WMCA Medium Term Financial Plans which are discussed with West Midlands Finance Directors at each planning cycle; with the in-year amount agreed and confirmed annually. Contributions for 2023/24 are shown below for information.

Local Authority	Amount (£)
Birmingham	5,253,100
Coventry	1,444,700
Dudley	1,022,800
Sandwell	1,264,400
Solihull	1,209,800
Walsall	865,300
Wolverhampton	939,900
TOTAL	**12,000,000**

3.14 For local purposes, the WMCA share has been deducted in the gain/detriment calculations before the "no detriment" assessment is carried out.

4 Ten Year Retention Process – summary of new proposed deal

4.1 Government is offering a ten year Business Rate Retention deal to those Local Authorities forming Greater Manchester and West Midlands Combined Authorities. This deal enables those authorities to retain 100% of Business Rates for a further ten-year period from 1 April 2024.

4.2 The process for entering into this arrangement will require agreement to a new MoU which is still being finalised. The MoU is not a legally binding document, but it will set firm parameters for how this funding stream will be managed over the period for which it is effective.

4.3 If the region is not able to reach a timely agreement with DLUHC on the contents of the MoU **by the end of November 2023**, then DLUHC have confirmed the existing pilot arrangements will continue for a further year (2024/25) with the potential opportunity to enter into a 9-year arrangement from April 2025. Whilst there may be no financial implications in 2024/25 for not agreeing the MoU, there is a risk that the opportunity for 100% retention may be withdrawn.

4.4 The MoU which requires formal approval is still being finalised. Some of the key factors to highlight are:

4.4.1 **Term**: The ten-year arrangement represents a fundamental improvement over the rolling one-year term of the pilot. This should allow Authorities to assemble financial plans with more confidence and where enhanced incomes are projected, Authorities may be enabled to make longer term investment decisions given the arrangements have a degree of longevity.

4.4.2 **No Detriment**: In discussions with DLUHC, they have been clear that the existence of the “no detriment” protection will not carry over to the ten-year arrangement. Further information on negotiations around potential mitigations for this are included in paragraphs 4.5 – 4.10.

4.4.3 **Impact of a Reset**: The ten-year arrangement will be affected by national resets to Business Rates baselines. At the point of a re-set, at a national level, the resources available to all LA's are unchanged in aggregate. However, a reset changes how Government distributes these resources nationally and as such, some LAs could benefit from a reset, others could be worse off. All core funding systems underpinned by Business Rates (the pilot, the national 50% scheme and the ten-year arrangements) are exposed to this issue. The MoU describes how WMCA and its constituent LAs will seek to protect individual West Midlands authorities as far as is possible from adverse outcomes associated with any reset. The detail of how a reset will be undertaken, and when, has yet to be determined.

4.4.4 **Safety Net**: The safety net is a protection within the system for local authorities which guarantees that reductions in Business Rates income is limited to a minimum percentage of the Baseline Funding Level. Under the pilot arrangements, each authority had an enhanced safety net level of 97%, compared with 92.5% nationally. The retention of this level of protection has been successfully negotiated.

4.4.5 **Grants Foregone:** There is no change to the grants foregone compared with the pilot arrangements. West Midlands authorities will continue to forgo RSG only in exchange for increased business rates retention.

4.4.6 **WMCA Share:** A share of regional business rates due to the Combined Authority (as discussed in Section 3) is required to remain in place, with details subject to local agreement

No Detriment Clause

4.5 As detailed above, DLUHC will <u>not</u> retain the “no detriment” protection that existed under the pilot arrangements, whereby Government would reimburse the West Midlands authorities were they collectively to be in a net deficit position. DLUHC’s view is that the removal of this protection creates a more equitable balance of risk and reward for both Local and National Government.

4.6 The no detriment protection has not been called upon since 2016, indicating it may be unlikely that the pool encounters a net detriment. However, the region is yet to experience the impact of a baseline re-set which could make the overall position more marginal, particularly in the early years following a re-set.

4.7 DLUHC have indicated there will not be a re-set until 2025/26 at the earliest. Additionally, it is as yet unclear what form a reset will take – for example whether it will be a full or partial reset, whether baseline funding levels will be updated in addition to business rates baselines (and if so on what basis) and which year(s) will be used to set the new baselines. These technical details are likely to have a significant influence on the outcome / impact of this national event. Nevertheless, the negotiating team have sought to agree appropriate protections which are acceptable to both sides.

4.8 A reset presents particular risks for the size of the WMCA share because in the year(s) immediately following a reset when business rates baselines are higher, the likelihood of there being insufficient business rates growth from which to fund the expected contribution is increased. Local authorities were concerned that in that scenario they might be expected to mitigate this risk from core resources, in which case they could be financially better off (particularly in the immediate year/s post re-set) in the national 50% scheme.

4.9 Through the negotiations with DLUHC steps have been taken to mitigate the loss of the no detriment protection. Firstly, the MoU includes a commitment from Government that, in the event a reset has adverse, unintended consequences on the West Midlands authorities’ ability to fund the WMCA share at the level expected, Government will work with the region to protect the substance of the WMCA share. Secondly, it provides a means of reviewing and modifying the arrangements throughout the ten-year term with the agreement of all Parties.

4.10 Outside of the MOU, locally-agreed no detriment protections (i.e. where Authorities in a gain position may compensate Authorities in a detriment position) are able to remain in place and it is recommended that these principles are maintained, with the precise details and mechanics to be worked through with the WM Finance Director Group and local technical group (both of which are groups of officers from each of the seven constituent Authorities)

Post Business Rates Reset

4.11 Following a national re-set, which DLUHC have indicated will not take place until 2025/26 at the earliest the region will need to assess how best to use the financial tools at its disposal to ensure that an appropriate share of business rates continues to be provided to assist with the sustainability of the Combined Authority in the most effective and equitable manner, without undermining the resources available to individual local authorities. The MoU is clear in stating that these decisions can be made locally.

5 Options considered and Recommended Proposal

5.1 National business rates retention arrangements are highly technical. The extent of the advantages/disadvantages to the West Midlands local authorities and the West Midland Combined Authority (WMCA) from increased retention arrangements is dependent upon numerous factors.

5.2 These factors include:

5.2.1 Future growth/decline in regional income from business rates;

5.2.2 The timing of, and outputs from, national business rates resets; and

5.2.3 Central Government policy and future reform to the business rates system.

5.3 It is therefore extremely difficult to accurately forecast the West Midlands pool gain/detriment position, particularly in the long-term after the next national business rates reset[1].

5.4 The Department for Levelling Up, Housing and Communities (DLUHC) have stated in negotiations that any new arrangements **will not** contain a full no detriment clause, which is currently in place.

5.5 Should West Midlands collectively as a region ultimately not agree long-term increased retention arrangements with DLUHC, and return to the national 50% retention scheme, the region will reduce its long-term dependency on funding from business rates and sensitivity to falls in regional income from business rates below the Baseline Funding Level (‘BFL’).

5.6 However, the region would also lose the opportunity to benefit from 99% of any growth that occurs above the BFL and would need to develop an alternative strategy to provide the funding for WMCA expected from Business Rates (‘WMCA Share’)[2].

5.7 It is DLUHC’s ambitions for the new arrangements to be implemented from 2024/25. Should agreement not be reached between the West Midlands and DLUHC in accordance with the timescales required for 2024/25 implementation, the current pilot arrangements would continue for one additional year (being 2024/25).

DLUHC have verbally stated that work for a nine-year arrangement to be implemented from 2025/26 would “probably” continue, although this is dependent upon the reasons for non-implementation in 2024/25. Therefore, there is a risk that should arrangements not be agreed for implementation from 2024/25, the West Midlands may lose the opportunity to participate in 100% increased retention arrangements from 2025/26 onwards.

5.8 The Council could choose to not agree to the proposals. This this would reduce its long-term dependency on funding from business rates and sensitivity to falls in regional income from business rates below the Baseline Funding Level ('BFL'). However, it would also lose the opportunity to benefit from 99% of any growth that occurs above the BFL and would need to develop an alternative strategy to provide the funding for WMCA expected from Business Rates ('WMCA Share'). This is therefore not recommended.

5.9 It is therefore recommended that the proposals are approved, in order that the Council receives the maximum gain from future growth in Business Rates Income.

6 Consultation

6.1 The proposed MoU has been discussed with West Midlands Finance Directors and the West Midlands Finance Technical Group.

7 Risk Management

7.1 The monitoring of the Council's Collection Fund Income is part of the Council's arrangements for the management of financial issues.

8 Compliance Issues:

8.1 How are the recommended decisions consistent with the City Council's priorities, plans and strategies?

The proposal supports the following objective of the Council:

A prosperous city, built on an inclusive economy – by attempting to maximise the benefit from growth in Business Rates.

8.2 Legal Implications

8.2.1 Section 151 of the 1972 Local Government Act requires the Chief Finance Officer (as the responsible officer) to ensure the proper administration of the City Council's financial affairs.

8.2.2 Section 111 of the Local Government Act 1972 contains the Council's ancillary financial and expenditure powers in relation to the discharge of its functions.

8.3 Financial Implications

8.3.1 The forecast for future business rates income will be updated as part of the 2024/25 budget-setting process and will factor into the updated Medium Term Financial Plan (up to 2027/28).

8.3.2 The 10 year 100% Business Rates Retention Agreement, proposed for approval in this report, is a broad continuation of the existing pilot arrangements. Therefore, it is not expected that this new agreement will alter the basis for forecasting business rates income within the MTFP.

8.3.3 Business Rates income constitutes a significant percentage of the Council's income. Table 1 shows that Business Rates income was forecast to be £410.9m (as per the budget for the 2023/24 financial year). This made up 44% of the total resources requirement of the Council that was approved by Full Council in February 2023.

Table 1 – funding requirement for 2023/24

	2023/24 £m
Base budget 2023/24	759.231
Changes in pay and price inflation	85.045
Budget pressures	24.851
Corporate adjustments:	
Other net change in use of / contribution to reserves	145.954
Corporately managed budgets	18.322
Changes in corporate government grants	(59.468)
Total expenditure	**973.935**
Business Rates	(410.863)
Top Up Grant	(69.303)
Council Tax	(429.159)
Collection Fund (surplus)/deficit Business Rates	(1.721)
Collection Fund (surplus)/deficit Council Tax	(14.032)
Total resources	**(925.078)**
Savings requirement	**48.857**
Planned savings	(48.857)
Other solutions to be determined	**0.000**

8.3.4 For information, Table 2 shows budgeted income from Business Rates and associated Section 31 Grants in the Financial for the next ten financial years from 2023/24:

Table 2: Budgeted Business Rates and associated Section 31 Grants

Budget per MTFP	2023/24 £m	2024/25 £m	2025/26 £m	2026/27 £m	2027/28 £m	2028/29 £m	2029/30 £m	2030/31 £m	2031/32 £m	2032/33 £m
Business Rates	410.863	487.854	495.937	501.120	515.316	528.684	542.390	555.877	569.696	583.869
Section 31 Income	151.545	113.322	115.285	116.176	119.455	122.460	125.537	128.590	131.715	134.764
Total	**562.408**	**601.176**	**611.222**	**617.296**	**634.771**	**651.144**	**667.928**	**684.467**	**701.411**	**718.633**

8.3.5 This forecast is currently being reviewed as part of the budget-setting process for 2024/25 and the Medium-Term Financial Plan.

8.3.6 It should be noted that all of this income from business rates is not ringfenced – with the exception of the contributions to the Fire authority and the West Midlands Combined Authority (reviewed yearly) – a is used to support a full range of activities within the Council's General Fund.

8.4 Procurement Implications (if required)

8.4.1 N/A

8.5 Human Resources Implications (if required)

8.5.1 N/A

8.6 Public Sector Equality Duty

8.6.1 There are no additional Equality Duty or Equality Analysis issues beyond any already assessed in the year to date. Any specific assessments needed shall be made by Directorates in the management of their services.

9 Appendices:

9.1.1 Draft Memorandum of Understanding (MoU) for the Trailblazer 100% Business Rates Retention Agreement: West Midlands

10 Background Papers:

10.1.1 None