Department for Communities and Local Government

Business Rates Retention

A step-by-step guide

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Exemplification of business rates retention scheme

This document provides a step-by-step guide on how the business rates retention scheme will be set up and will operate, including how the central and local share will operate and how levy and safety net payments will be calculated. This aims to clarify the statements of intent[1] published in May, especially around the terminology used.

The summer consultation, which this document is published alongside, sets out the technical detail underpinning the business rates retention scheme ahead of the 2013-14 local government finance report. This consultation includes income definitions for the purpose of calculating the payments from billing authorities to their major precepting authorities, in respect of the central share and for the purposes of levy and safety net calculations. It also deals with the calculation and distribution of Revenue Support Grant, which is not discussed here.

The numbers used in this document are for illustrative purposes only and do not reflect actual sums of business rates at either aggregate or individual authority level. This exemplification illustrates how the scheme will operate in a two-tier area. Other major precepting authorities, such as single purpose fire and rescue authorities, can see how the scheme will operate for them by inputting their major precepting authority shares as necessary (steps 4, 7 and 8).

Set-up

1. **DCLG will first calculate the total business rates that will be collected by all English billing authorities in 2013-14 i.e. the estimated business rates aggregate.** This will be on the basis of an Office of Budget Responsibility UK forecast. The details of how this will be done are set out in the summer consultation.

Estimated business rates aggregate: £10bn

2. **The central and local share percentages will then be applied to the estimated business rates aggregate.** The Statement of Intent, ‘Business Rates Retention Scheme: the central and local share of business rates’, set out the Government’s intention to set the local share at 50 per cent and the central share at 50 per cent.

Estimated business rates aggregate= £10bn *Central share @ 50%= £5bn* *Local share @ 50%= £5bn*

The central share will be paid by billing authorities to central government. This will be used in its entirety to fund local government through Revenue Support Grant or other specific grants.

[1] http://www.communities.gov.uk/localgovernment/localgovernmentfinance/lgfinancebill/

Payment schedules will be set up on the basis of the estimated business rates aggregate but will be subject to a process of reconciliation to ensure payments represent 50 per cent of actual receipts.

3. **DCLG calculates a proportionate share for each billing authority** in order to work out a billing authority business rates baseline**.** It first works out a proportionate share percentage for each billing authority based on its historic business rates collection averaged over a number of years. The methodology for how proportionate shares will be calculated is set out in the summer consultation.

   The proportionate share percentage is then applied to the local share of estimated business rate aggregate (as set out in step 2) to determine the billing authority business rates baseline.

Local share: £5bn
Proportionate share percentage for billing authority A: 1%
Billing authority business rate baseline: £5bn x 0.01= £50m

4. **This billing authority business rate baseline is then split between the billing authority and its major precepting authorities (on the basis of major precepting authority shares) to determine individual authority business rate baselines.**

   In December 2011, the Government set out that it intended to set the major precepting shares in two tier areas at 80 per cent for district councils and 20 per cent for county councils that have responsibility for fire and rescue services. The summer consultation proposes to set the percentage share for single purpose fire and rescue authorities at 2 per cent, and county councils in such areas would receive an 18 per cent share.

Billing authority business rates baseline: £50m
Individual authority business rate baseline (for billing authority A) @ 80%= £40m
Proportion of billing authority business rates baseline which is passed to major precepting authority B @ 20%= £10m

A major precepting authority's individual authority business rate baseline will be formed from adding together the proportions they receive from the billing authorities in their area.

Proportion from billing authority A: £10m
Proportion from billing authority C: £5m
Proportion from billing authority D: £7m

Individual authority business rate baseline (for major precepting authority B)= £22m

5. **For each authority, DCLG will then calculate the baseline funding level for the purpose of the business rates retention scheme.** This is done by applying the 2012/13 formula grant process to the local share of the estimated business rates aggregate. Proposals for using updated datasets, making limited methodological updates and other technical adjustments are set out in the summer consultation.

Billing authority A's baseline funding level = £25m

6. **Tariffs and top-ups are then calculated.** A local authority must pay a tariff if its individual authority business rate baseline is greater than its baseline funding level. Conversely, a local authority will receive a top-up if its baseline funding level is greater than its individual authority business rate baseline.

   Tariffs and top-ups will be fixed until the business rates retention system is reset but will be uprated by RPI each year.

Billing authority A's individual authority baseline funding level: £25m
Billing authority A's business rate baseline: £40m

Billing authority A is a tariff authority as its individual authority business rate baseline is greater than its baseline funding level.

Tariff: £40m- £25m= £15m

Running the system: Major precepting shares

7. **In setting up the system, major precepting shares will be used to determine individual authority business rates (see step 4). They will also be used once the system is running to determine how much of the business rates it collects a billing authority has to pay to central government and its major precepting authorities.**

   In December 2011, the Government set out that it intended to set the major precepting shares in two tier areas at 80 per cent for district councils and 20 per cent for county councils. After central share payments are taken into account, this percentage split becomes 40 per cent and 10 per cent respectively of the total rates collected. For single purpose fire and rescue authorities, this means they will receive 1 per cent of the business rates collected by the billing authority and a further 1 per cent would be paid to central government as a central share payment by the billing authority.

Business rates collected by billing authority A in 2013-14: £120m
Central share payment of 50%: £60m

Payment to major precepting authority B@ 10% of rates collected= £12m
Retained income by billing authority A@ 40% of rates collected= £48m

8. **Major precepting authorities will receive business rate income from each of the billing authorities in their area.** They will also receive Revenue Support Grant and are likely to receive a top-up payment because county councils in two tier areas are receiving 10 per cent, and single purpose fire and rescue authorities are receiving 1 per cent, of locally retained business rates.

10% of billing authority A’s business rate income: £12m *10% of billing authority C’s business rate income: £8m* *10% of billing authority D’s business rate income: £5m* *Total business rate income of major precepting authority B= £25m*

Running the system: operation of the levy and the safety net

9. **A levy will be calculated for each local authority.**

In the Statement of Intent, ‘Business rates retention scheme: the safety net and levy’, the Government stated that the levy would be a 1:1 proportionate levy. This means that for every 1 per cent increase in a local authority’s business rate income, the local authority would see no more than a corresponding 1 per cent increase in its baseline funding level.

This relationship is expressed in the levy rate, which is:

$$1 - \left(\frac{\text{baseline funding level}}{\text{individual authority business rates baseline}} \right)$$

If the calculation produces a negative levy rate, the local authority will not be levied.

Local authority A’s individual authority business rate baseline= £40m *Local authority A’s baseline funding level= £25m* *Levy rate: 1- (£25m/ £40m) = 0.375%*

10. Calculating levy payments

At the end of a financial year, DCLG will calculate whether a levy payment was due from an authority. It will do this by comparing an authority's pre-levy income under the business rates retention scheme with its baseline funding level.

Total business rates collected by billing authority A in 2013-14= £120m
Less:
Central share @ 50%: £60m
Payments to major precepting authority B @ 10%: £12m

=Billing authority A's retained business rate income= £48m
Less:
Tariff =£15m

=Pre-levy income under rates retention scheme = £33m

Baseline funding level = £25m
Growth= £8m
Levy rate of 0.375% = Levy due of £3m

Growth Retained= £5m

For major precepting authorities, the levy ratio will be applied to the cumulative total of business rate payments from their billing authorities.

11. Calculating safety net entitlements

At the end of a financial year, DCLG will calculate whether a safety net payment should be paid. It will do this by comparing an authority's pre-safety net income under the business rates retention scheme with its baseline funding level. For the purpose of these calculations, the baseline funding levels will be indexed to RPI.

Safety net payments will ensure that a local authority's income does not drop below more than a set percentage of its baseline funding level uprated by RPI. In the Statement of Intent, 'Business rates retention scheme: the safety net and levy', the Government announced that the safety net threshold would be set at between 7.5 per cent and 10 per cent. The Government is consulting on the safety net threshold in the summer consultation, as well as the mechanism for providing in-year safety net payments.

Assuming a safety net threshold of 8.5%.

Total business rates collected by billing authority A in 2013-14= £80m
Less:
Central share @ 50%: £40m
Payments to major precepting authority B @ 10%: £8m

=Billing authority A's retained business rate income= £32m
Less:
Tariff= £15m

=Pre-safety net income under rates retention scheme = £17m

Baseline funding level = £25m
Safety net level (@ 8.5% threshold) = £22.9m
= Safety net payment of £22.9m- £17m= £5.9m