The Financial Implications of COVID 19 for Local Government: Council Tax & Business Rates

Summary

July 2020

Overview

- This report is concerned with the forecast financial implications of COVID 19 for Local Government. It is focused on the potential losses that could occur from the business rates retention system and council tax and is based on the June returns from local authorities to MHCLG regarding the financial implications of COVID 19.

- During the LGA Conference on July 2nd, the Secretary of State, Robert Jenrick, indicated that *"at the Spending Review, the government will agree a fair apportionment of irrecoverable council tax and business rates losses, between central and local government, for 2020 to 2021".* This report considers Business Rates and Council Tax in order to inform this discussion.

- This report uses the MHCLG survey from June 2020, which asked authorities to report on Business Rates (cash losses) and Council Tax.

- Analysing the data, the report identifies the impact of the data reported for resources and cashflow, nationally, and goes on to suggest approaches to addressing the impact:

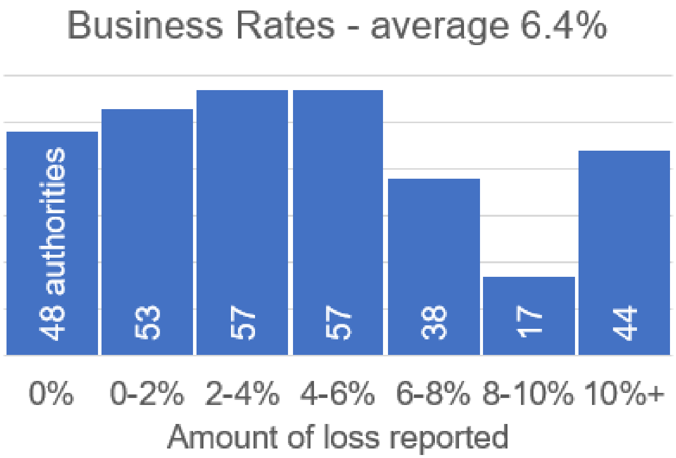
  - Business Rates – adjusting the baselines included in the business rates retention system will limit the impact on authorities, in proportion to the taxbase in their area, and address the cashflow impact.

  - Council Tax – adding resources to the Collection Fund in 2020/21 and spreading the deficit over 3 years will limit the impact on authorities, and reduce the cashflow impact.

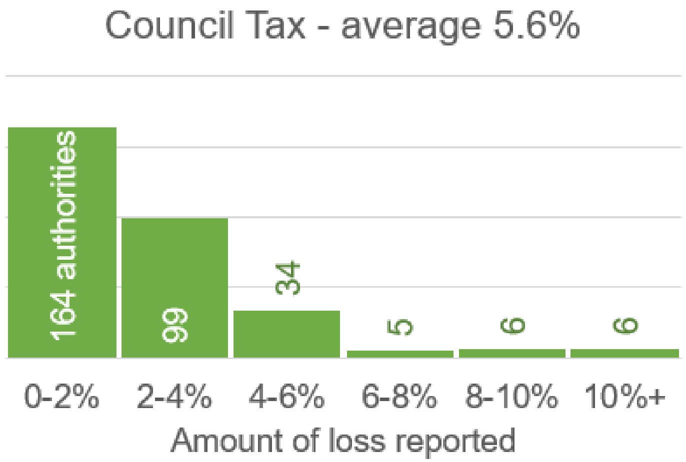
Overview
Business Rates
Council Tax

Overview

- For both Business Rates and Council Tax, the Collection Fund payments mean that the impact in 2020/21 does not cause a resources ‘problem’ until the following year (indeed for Business Rates in 2020/21 authorities receive s31 grant in addition to planned Collection Fund transfer).
- However, as payments are set before the start of the financial year, any unexpected in-year reduction means a cashflow problem for billing authorities. In Business Rates, this will total the £1.6bn reported (plus reported deferrals) and Council Tax
- The quality and consistency of the returns used, in particular for Business Rates, could be a concern. The report therefore examines solutions which use established measures for distribution of resources, rather than the data itself.
- The graphs show the quantum reported by local authorities in the survey:



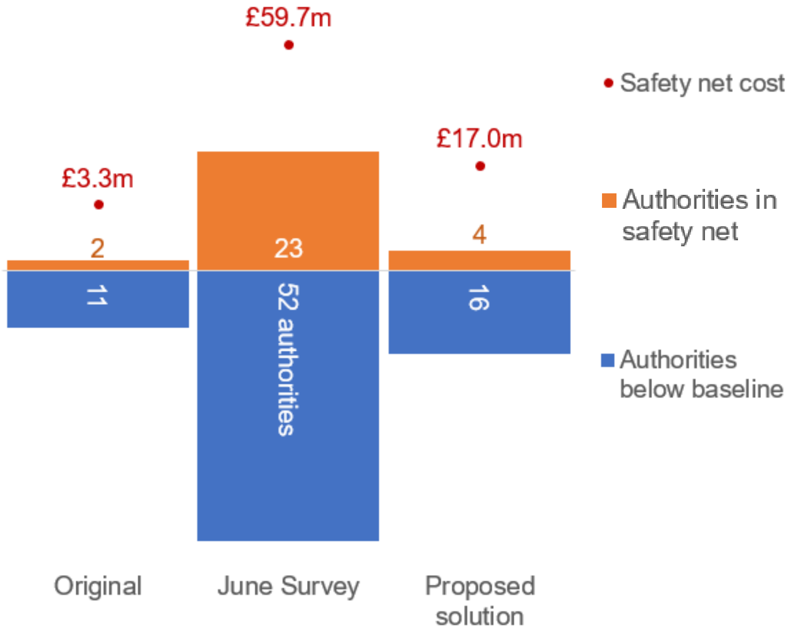
Business Rates Resource impact: (£1,044m)
(Excl. Central Share)



Council Tax Resource impact: (£844m)

Overview

- The proposed business rates solution adjusts business rates baselines so that authorities pay a lower tariff or receive a higher top up, providing cashflow support in year. This also effectively brings up the safety net level by the same amount.
- The original position, impact of the June survey, and of the proposed solution are shown in the chart:



- The proposed Council Tax solution firstly examines the impact of spreading a 2020/21 deficit over three years.
- Secondly, it considers the impact of additional funding provided direct to the Collection Fund. This supports billing authority cashflow in 2020/21 and authorities' resources in 2021/22.

Overview

Business Rates

Council Tax

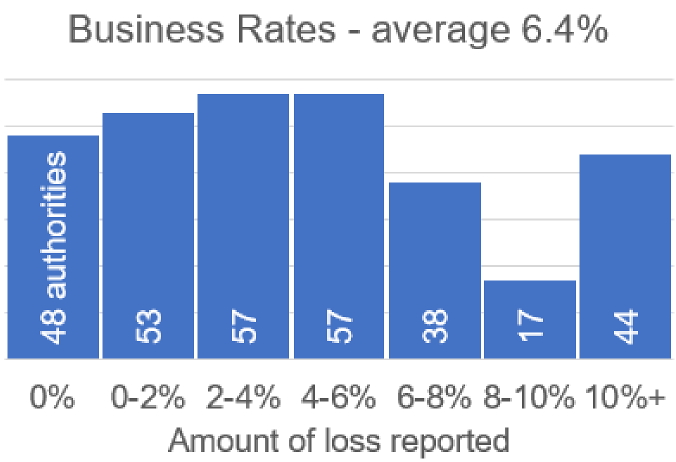
Business Rates Retention – Data Used

- The 2020/21 NNDR1 forms completed in January 2020 have been used as the starting point for comparison of this report.

- The June survey asked authorities to forecast cash losses from business rates in 2020/21 due to COVID 19. A total of £12.2bn was given. A breakdown of these losses by type was also requested, these being due to:
    - COVID reliefs – forecast at £10.3bn (taken to be the funded reliefs announced in March)
    - Deferrals – forecast at £0.2bn
    - Other – forecast at £1.6bn

- For the purposes of this analysis, the Business rates “other” category has been treated as losses.   The reliefs figures are consistent with those already submitted by authorities in April (which are being paid directly by S31 grant) and the deferrals have been assumed to be collected in future years.

- From the returns, the average loss is forecast at 6.4% of NNDR income. However, 48 of the 314 billing authorities forecast no loss at all, whereas 44 authorities are forecasting a loss of greater than 10%.



Business Rates Retention – June Data - Loss in Resources (Local Share)

- The financial implications of these projected reliefs & reduced business rates collected is made more complex by: the operation of the collection fund, the billing & preceptor relationship, and the levy / safety net calculation. The impact of these has been included in this report. Further complicating factors around: pooling, the implications on existing and future approaches to bad debt and the prospect of appeals based on reductions in use, are not factored in.

- The table below shows the forecast resources received by local government from business rates retention based on January 2020 NNDR1 and the revised projection.

	2020/21 Original £m	2020/21 Amended £m	Change £m	2021/22 Original £m	2021/22 Amended £m
Business Rates Income (2020/21)	15,860	15,860	-	-	(7,076)
S31 Grants Forecast	1,872	7,904	6,032		
Tariff / Top Up	(611)	(611)	-		
Total	**17,121**	**23,153**	**6,032**		**(7,076)**
Levy	(172)	(71)	101		
Safety Net	3	60	56		
Business Rates Income	16,952	23,142	6,189		(7,076)
G/ F Resources Change			**6,189**		**(7,076)**
Change over the two years					**(887)**

- The table shows a decrease in resources of (£887m) in resources over the two years.

- However, this is increased to **(£1,044m)** (-£101m & -£56m), after adding in the impact on the levy / safety net account (which is usually returned to local government).

Business Rates Retention – Cash Flow

- In addition to considering the lost resources, cash flow projections also need to reflect: the collection fund, the billing / preceptor relationship and the extended retails reliefs / S31 grants payments. The table below summarises the position of local government overall. However, the scale of the cash flow changes is more apparent when looking at the results by authority type (due to the relationship between billing and precepting authorities).

Local Government	2020/21 Original £m	2020/21 Amended £m	Change £m	2021/22 Original £m	2021/22 Amended £m
Business Rates Collected	25,616	14,250	(11,365)		
Collection Fund Payments	(25,616)	(25,616)	-	-	11,365
Collection Fund Received	15,860	15,860	-	-	(7,076)
S31 Grant Payments In - Original	1,872	1,872	-		
S31 Grant Payments In - Extended Relief		9,726	9,726		
Top Up / Tariff	(611)	(611)	-		
Total	**17,121**	**15,482**	**(1,639)**		**4,289**
Year End Accounting Adj					
Levy	(172)	(71)	101		
Safety Net	3	60	56		
S31 Grant to Central Gov / Preceptors		(5,111)	(5,111)		
S31 Grant from Billing authorities		1,417	1,417		
Accounting Adjustments	**(169)**	**(3,706)**	**(3,537)**		
Resources Change	**16,952**	**11,776**	**(5,176)**		**4,289**
of Which					
Collection Fund			(11,365)		
General Fund			6,189		
Change over the two years					**(887)**

- The table shows the decrease in resources of (£887m) in resources over the two years.
- It assumes that the amounts will either be lost (due to reliefs) or through accounting adjustments (e.g. bad debt provisions created) in 2020/21 declared at NNDR1 in January 2021, thereby creating a deficit.
- It shows a cash flow shortfall of £1.6bn in 2020/21.

Business Rates Retention – Tested Solution

- In order to try and remove the subjective nature of the forecast BRR losses, a solution has been modelled that uses additional funding and BRR system change. This solution adjusts each authority's NNDR Baseline by a uniform percentage, therefore reducing its tariff or increasing its top up grant.

- This allows for a proportion of losses in line with business rates tax base, whilst avoiding perverse incentives around collection (as authorities still retain everything they collect). The retention system's safety net (funded by levies on growth) will ensure that authorities' losses are capped, in proportion to their funding, and limit windfall gains.

- For the purposes of modelling, the forecast funding loss of £1,044m has been used. As mentioned previously, the extent to which this is figure is realistic is unknown. However, in the absence of any other figure, we have used it for modelling.

- The national NNDR Baseline for 2020/21 is £14,162m. Therefore a reduction of £1,044m would mean a **6.9% reduction to all authorities' NNDR Baselines**, with corresponding changes to top up / tariff amounts. This would be at a cost to MHCLG of £1,044m, through higher top up payments out and lower tariff payments in.

- The adjusted forecast resources for each authority have been re-calculated using the revised tariff / top up amounts, with the levy and safety net applied.

Business Rates Retention – Tested Solution

- The table below shows the original NNDR1 figures, the forecast changes due to COVID and the changes due to the tested solution. It includes the £1,044.2m in additional resources.

	2020/21 Original £m	2020/21 Amended £m	2020/21 Solution £m	Change £m	Change £m	2021/22 Original £m	2021/22 Amended £m	2021/22 Solution £m
Business Rates Income (2020/21)	15,860	15,860	15,860	-	-		(7,076)	(7,076)
S31 Grants Forecast	1,872	7,904	7,904	6,032	6,032			
Tariff / Top Up	(611)	(611)	433	-	1,044			
Total	**17,121**	**23,153**	**24,198**	**6,032**	**1,044**		**(7,076)**	**(7,076)**
Levy	(172)	(71)	(146)	101	27			
Safety Net	3	60	17	56	14			
Business Rates Income	16,952	23,142	24,069	6,189	7,116		(7,076)	(7,076)
G/ F Resources Change				**6,189**	**7,116**		**(7,076)**	**(7,076)**
Change over the two years							**(887)**	**40**

£1,044m Additional Resources

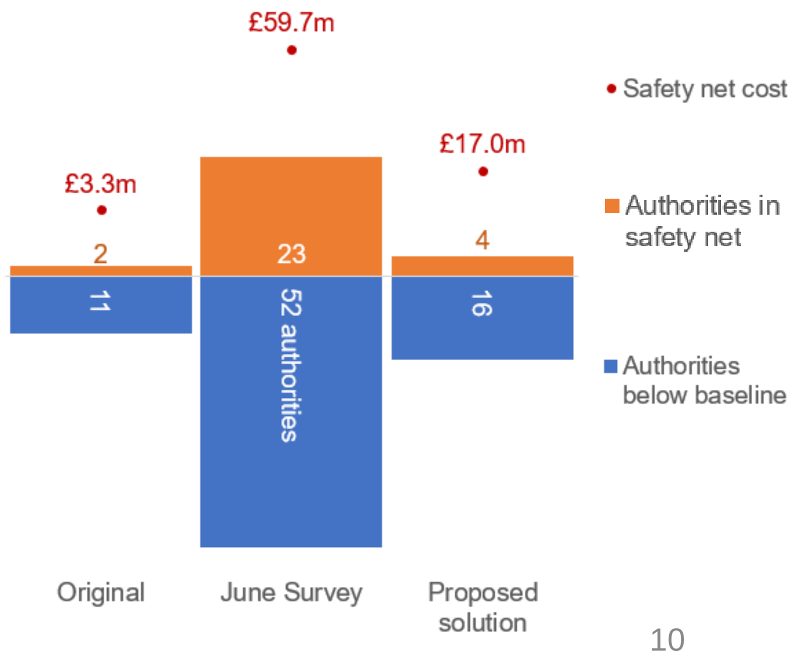
- The table shows the £1,044m received through the tariff and top up line, leading to net additional resources of £0m (compared to the NNDR1 projection) after taking into account the levy safety net account.

	£m	£m
Change in Resources vs NNDR1	(887)	40
Change in the levy / safety net account vs NNDR1	(157)	(40)
Overall Change	**(1,044)**	**(0)**

Tested Solution & the Safety Net

- The table below shows the impact on the safety net of the tested solution, compared to the original projections and those amended for the June return. The table shows:
  - Originally there were 11 authorities below Baseline Need, with 2 of those below the safety net at a cost of £3.3m.
  - This increased to 52 authorities, with 23 below the safety net at a cost of £59.7m.
  - Finally, the proposed solution reduced the number below baseline need to 16, with 4 below the safety net at a cost of £17.0m.

	Original	June Survey	Proposed Solution
Below Baseline Need	11	52	16
In the safety net	2	23	4
Safety Net Cost £m	3.3	59.7	17.0



Tested Solution – Cash Flow Changes

- From a cash flow perspective, the forecast £1,639m c/f deficit of 2020/21 is offset by the £1,044m of extra funding provided in year to £595.3m.

Local Government	2020/21 Original £m	2020/21 Amended £m	2020/21 Solution £m	Change - Original to Amended £m	Change Original to Solution £m	2021/22 Original £m	2021/22 Amended £m	2021/23 Solution £m
Business Rates Collected	25,616	14,250	14,250	(11,365)	(11,365)			
Collection Fund Payments	(25,616)	(25,616)	(25,616)	-	-	-	11,365	11,365
Collection Fund Received	15,860	15,860	15,860	-	-	-	(7,076)	(7,076)
S31 Grant Payments In - Original	1,872	1,872	1,872	-	-			
S31 Grant Payments In - Extended Relief		9,726	9,726	9,726	9,726			
Top Up / Tariff	(611)	(611)	433	-	1,044			
Total	**17,121**	**15,482**	**16,526**	**(1,639)**	**(595)**		**4,289**	**4,289**
<u>Year End Accounting Adj</u>								
Levy	(172)	(71)	(146)	101	27			
Safety Net	3	60	17	56	14			
S31 Grant to Central Gov / Preceptors		(5,111)	(5,111)	(5,111)	(5,111)			
S31 Grant from Billing authorities		1,417	1,417	1,417	1,417			
Accounting Adjustments	**(169)**	**(3,706)**	**(3,823)**	**(3,537)**	**(3,654)**			
Resources Change	**16,952**	**11,776**	**12,703**	**(5,176)**	**(4,249)**		**4,289**	**4,289**
of Which								
Collection Fund				(11,365)	(11,365)			
General Fund				6,189	7,116			
Change over the two years							**(887)**	**40**

Council Tax

- The 2020/21 Council Tax Requirement for England is £33,100m. Based on the June 2020 returns, billing authorities forecast a reduction in Council Tax income of **£1,849m**.
- The survey data shows 164 authorities are forecasting losses of between 0% and 2%, with 51 forecasting losses over 4%.
- Of the £1,849m forecast loss, £586m was attributed to new LCTS, with £1,073m due to payment failure and a further £190m to "other".
- For resources, there is no "in-year" implication for 2020/21, with the collection fund payments from the billing authorities to themselves and their preceptors remaining fixed in-year. In terms of the future years' impact:
  - **Payment Failure** – Amounts should be collected from 2021/22 onwards, decreasing each year , but with an element that will eventually need to be written off
  - **LCTS** – Initial cost of the deficit in 2021/22, but with potentially a double cost in that year (as the forecast taxbase for 2021/22 includes the higher number of claimants) with an ongoing cost in future years based on increased claimants.
  - **Other** – Assumed as a one-off cost in 2021/22.

Council Tax

- The table shows the forecast collection fund deficit implications from 2021/22 onwards of the June survey data and the potential in year implications for the period 2021/22 to 2024/25. Of note is the potential in year cost of LCTS in 2021/22, coupled with the collection fund deficit from 2020/21.

	2021/22	2022/23	2023/24	2024/25
Payment Failure – Bad Debt Projection	(£69m)			
LCTS - Cost of 2020/21 deficit, plus the in-year forecast cost, with potentially a decreasing cost per annuum going forward	(£586m) +/- (£781m)	+/- (£670m)	+/- (£558m)	+/- (£446m)
Other - Treated at a one-off loss and no future years' recovery £0.181bn	(£190m)			

Council Tax – Payment Failure – Cash Flow

- The table below shows the forecast cash flow position based on the payment failure and LCTS analysis.

	2020/21	2021/22	2022/23	2023/24	2024/25
Payment Failure	(£1,073m)	+£429m	+£307m	+£161m	+£107m
LCTS -	(£586m)	+/- (£781m)	+/- (£670m)	+/- (£558m)	+/- (£446m)
Other	(£190m)				

Council Tax – Potential Solutions

- The analysis shows the extent of the forecast council tax losses for resources (projected at a loss of £1,849m reducing to £844m over time, based on historic arrears collection) and cash flow problems for billing authorities (Shire Districts in particular -£744m in 2020/21).
- In order to support authorities in dealing with these issues, the following solutions have been considered:
  - Resources – Allow the projected 2020/21 reduction in resources to be spread over multiple years
  - Cash Flow / Resources – Provide resources to collection funds in 2020/21, thereby supporting all authorities with resources in 2021/22 and easing cash flow problems for billing authorities in 2020/21.
- It is important to note that the future years' cost of any increased LCTS claimants are not considered.

Council Tax – Spreading the Resources Cost

- This approach would provide authorities with time to adjust to a large (and unexpected) 2020/21 collection fund deficit. It would allow the projected reduction in resources to be spread over multiple years.
- Rather than the full deficit being included in 2021/22, a proportion could be held back to be spread over subsequent years. This would also allow the deficit to be in part addressed by the forecast amounts still owing from 2020/21 (due to payment failure). This would mean that forecast loss in resources of £844m is split over the 3 years (£281m per annum) and adding this to the forecast arrears to be collected amount for each year.
- From a cash flow perspective, there is a longer period (to 2023/24) that the part of the deficit is retained in the collection fund, due to the delay in releasing £562m (2x £281m) in 2022/23 and £281m in 2023/24.

	2020/21 £m	2021/22 £m	2022/23 £m	2023/24 £m	2024/25 £m
Deficit Released		(711)	(588)	(442)	(107)
Arrears Collected		429	307	161	107
Resources Change		(281)	(281)	(281)	0
Deficit retained in the collection fund	(1,849)	(1,138)	(550)	(107)	(0)

Council Tax – MHCLG Support in 2020/21

- Whilst the previous solution allowed the 2020/21 loss to be spread over the medium term, it:
  - Would also spread the collection fund deficit from preceptors over the medium term, generating cashflow issues for billing authorities in the medium term
  - Does not solve the cash flow issue for 2020/21
  - Does not provide additional resources for the forecast overall loss (of £844m) over the period.
- A potential solution to both the resources loss and part of the cash flow issue would be for additional funding to be provided by government direct into collection funds in 2020/21. For example, if this amount was based on 2020/21 loss, net of estimated future years' collection of 2020/21 amounts outstanding, it would reduce the cashflow impact and mean medium term resources shortfall of £0.
- Whilst this approach could potentially address the 2020/21 resources loss (albeit over the medium term), and provides some support on cash flow, further issues to consider in its operation are:
  - It requires additional funding from MHCLG.
  - Unless new funding was greater than the 2020/21 resources loss, it does not address all of the cash flow issues (for billing authorities), with deficits still retained in the collection fund (until arrears are collected).
  - LCTS losses beyond 2020/21 are not covered.
  - It may be reliant on future years collection of payment failure amounts (which may not follow historic trends going forward).

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