

## **Explanatory Memorandum to The Non-Domestic Rating (Chargeable Amounts) (Wales) Regulations 2016**

This Explanatory Memorandum has been prepared by the Local Government Finance Policy Division and is laid before the National Assembly for Wales in conjunction with the above subordinate legislation and in accordance with Standing Order 27.1.

### **Cabinet Secretary's Declaration**

In my view, this Explanatory Memorandum gives a fair and reasonable view of the expected impact of The Non-Domestic Rating (Chargeable Amounts) (Wales) Regulations 2016. I am satisfied that the benefits justify the likely costs.

Mark Drakeford  
Cabinet Secretary for Finance and Local Government

22 November 2016

## **1 Description**

These Regulations provide for a transitional relief scheme to assist ratepayers affected by the 2017 non-domestic rating revaluation.

They prescribe rules to be used to calculate the chargeable amount for hereditaments which have a reduction in their entitlement to Small Business Rates Relief as a result of an increase in their rateable value following the revaluation. The regulations operate by reducing eligible ratepayers' increases in liability, allowing any increase to be phased in over a three-year period.

## **2 Matters of special interest to the Constitutional and Legislative Affairs Committee**

None.

## **3 Legislative Background**

The Regulations are made under section 58 of the Local Government Finance Act 1988 ("the 1988 Act"). Section 58 enables the Welsh Ministers to prescribe rules to govern the chargeable amount for particular properties.

The power was originally conferred on the Secretary of State but was transferred to the National Assembly for Wales by the National Assembly for Wales (Transfer of Functions) Order 1999 and subsequently transferred to the Welsh Ministers by virtue of paragraph 30 of Schedule 11 to the Government of Wales Act 2006.

Section 58(8) of the 1988 Act provides that regulations made under section 58 must come into force before 1 January immediately preceding the financial year to which they are to apply. To have effect in relation to the 2017-18 financial year, these regulations must come into force before 1 January 2017.

The Regulations are subject to the affirmative procedure.

## **4 Purpose and intended effect of the legislation**

The Regulations will assist ratepayers whose entitlement to Small Business Rates Relief (SBRR) is reduced or removed as a result of increases in the rateable value of their hereditament following the compilation of the new non-domestic rating list, which comes into effect on 1 April 2017. Eligible ratepayers will be entitled to a phased reduction in any resultant increase in their liability over a three-year period (75% reduction in year one, 50% in year two and 25% in year three).

In order to be eligible for transitional relief, the hereditament must:

- have been shown on a local list on 31 March 2017 (the day before the new lists compiled on 1 April 2017 have effect);

- have been eligible for small business rates relief on 31 March 2017 – depending on the increase in the hereditament’s rateable value, the ratepayer may or may not still be in receipt of SBRR following the revaluation;
- have an increase in liability of more than £100 which is the de minimis threshold set below which the administrative costs of providing this relief are deemed to outweigh the benefits;
- not be in receipt of relief under section 44A of the 1988 Act (for partially occupied properties);
- not be a case to which section 45A of the 1988 applies (unoccupied hereditaments: zero rating) and
- be the same ratepayer who occupied the hereditament on 31 March 2017. This ratepayer must continue to occupy the hereditament for the duration of the transitional relief period. If not, the relief ceases to apply.

If the hereditament meets the necessary eligibility criteria, then the level of transitional relief applicable is determined by the following steps.

1) First calculate the base liability (BL) for a hereditament using the formula:

$$\frac{A \times 0.486}{E}$$

Where:

- A is the rateable value for a hereditament on a local list as at 31 March 2017;
- 0.486 is the multiplier set for 2016-17; and
- E is the amount of E which applies to the defined hereditament on 31 March 2017 in accordance with the Non-Domestic Rating (Small Business Relief) (Wales) Order 2015 – this determines the amount of SBRR the hereditament is eligible for.

2) Calculate the notional chargeable amount (NCA) for a hereditament using the formula:

If the hereditament meets the conditions to be eligible for SBRR –

$$\frac{A \times B}{E}$$

In all other cases –

$$A \times B$$

Where:

- A is the rateable value for the hereditament on a local list as at 1 April 2017;
  - B is the non-domestic rating multiplier for the financial year beginning on 1 April 2017 to be set by the Welsh Ministers according to paragraph 4B of Schedule 7 to the Local Government Finance Act 1988; and
  - E is the amount of E which applies to the defined hereditament on 1 April 2017 in accordance with the Non-Domestic Rating (Small Business Relief) (Wales) Order 2015.
- 3) Compare the base liability to the notional chargeable amount to determine whether the hereditament is entitled to relief using the following formula:

$$NCA > (BL + 100)$$

To be eligible for relief the increase in liability for the hereditament as a result of the revaluation must be more than £100. This figure was determined to be the level below which the administrative costs of providing the relief outweigh the benefits.

- 4) Calculate the chargeable amount for the relevant day in accordance with section 43 or 45, as appropriate, then reduce that amount by the level of transitional relief which applies for the relevant year using the following formula:

For a year commencing 1 April 2017

$$\frac{(NCA - BL) \times 0.75}{365}$$

For a year commencing 1 April 2018

$$\frac{(NCA - BL) \times 0.5}{365}$$

For a year commencing 1 April 2019

$$\frac{(NCA - BL) \times 0.25}{365}$$

For the years commencing 1 April 2020 and 2021, the chargeable amount is reduced by zero.

If, in any year, applying the above formulas would result in a negative figure, then the chargeable amount will be zero.

The effect of calculating the level of transitional relief applicable in this way is that the ratepayer will be required to meet the costs of any increase in liability due to inflationary pressures in that year, rather resulting from the

revaluation. This is due to the multiplier. The relief is calculated using the multiplier set for the financial years 2016-17 and 2017-18, to reflect that the relief is designed to ease the impact of revaluation. That relief is then deducted from the chargeable amount for the relevant day which would be calculated by using the multiplier set for the financial year in which the relevant day falls.

If there is a change in the rateable value of the hereditament during the transitional relief period, for example because of an appeal, then the notional chargeable amount will be recalculated using the new rateable value.

These regulations also revoke the following sets of regulations which are no longer required as the relevant rating list is now closed and all appeals against it resolved:

- The Non-Domestic Rating (Chargeable Amounts) (Wales) Regulations 1999; and
- The Non-Domestic Rating (Chargeable Amounts) (Wales) Regulations 2000.

## **5 Consultation**

Details of the consultation undertaken are included in the Regulatory Impact Assessment below.

## **6 Regulatory Impact Assessment (RIA)**

### **Options**

#### **Option 1 – Do nothing**

If no regulations were made, then any ratepayer with an increase in their rateable value following the revaluation would have to pay a higher rates bill from 1 April 2017. No transitional relief would be provided to help phase in any increases in liability.

#### **Option 2 – Make regulations providing for transitional relief for small businesses affected by the revaluation**

Regulations could be made providing transitional relief for small businesses affected by the revaluation, which is funded by the Welsh Government. This transitional relief would enable ratepayers whose entitlement to SBRR was affected by an increase in their rateable value following the revaluation to phase in their increase in liability over a three-year period.

#### **Option 3 – Make regulations based on the transitional relief provided in England**

Regulations could be made providing transitional relief based on the self-financing scheme currently operating in England. This means that all

ratepayers with an increase in their liability (over a certain percentage) would be able to phase in their increase in liability over a five-year period. However, this relief would be funded by limiting the reductions in liability for those ratepayers whose rateable value decreases as a result of the revaluation.

## Option 1 – Do nothing

### Costs

If no transitional relief were provided, then all ratepayers with an increase in their rateable value following the revaluation would have to pay their resultant higher non-domestic rates bills from 1 April 2017.

The impact on ratepayers will depend on their increase in rateable value, whether they are entitled to any relief, for example charitable relief or empty property relief, and whether they lose entitlement to any relief as a result of increases in their rateable value, for example Small Business Rates Relief. Increases in liability will therefore vary significantly for ratepayers across Wales. A number of illustrative examples showing potential increases in liability, as a result of increases in rateable value following the revaluation, are set out in the following table.

2010 Rateable Value	2016-17 Liability*	2017 Rateable Value	2017-18 Liability*	Increase in Liability
£3,500	£0	£8,000	£1,330	£1,330
£5,995	£0	£12,500	£6,238	£6,238
£15,000	£7,290	£20,000	£9,980	£2,690
£24,000	£11,664	£35,000	£17,465	£5,801
£50,000	£24,300	£70,000	£34,930	£10,630

\* using the multiplier of 48.6p

\*\* using provisional multiplier of 49.9p

As can be seen from the examples above, increases in rateable value for smaller properties can be significant as this can result in the loss of entitlement to 100% relief under SBRR (if the rateable value increases above £6,000) or partial SBRR (if the rateable value increases above £12,000).

As non-domestic rates can represent a higher proportion of overheads for smaller businesses and these businesses also have less opportunity to adapt to an increase in costs in the shorter term, for example by increasing prices or reducing production costs, then it is likely that small businesses are most likely to be affected by an increase in their rates bills following the revaluation.

Ratepayers who might be particularly affected by the provision of no transitional relief include those in Gwynedd, Conwy and Monmouthshire where the average change in rateable value is an increase of 7% or more, compared to the average change for Wales as a whole which is decreasing by nearly 3%.

## **Benefits**

If no transitional relief were provided, then there would be no amendments required to local authorities' software systems and no associated administrative costs from applying the relief to the bills of eligible ratepayers.

Not providing a relief scheme would also ensure the NDR system remains relatively simple, meaning that ratepayers are able to calculate their liability easily from year to year.

There would also be no dilution of the principle of regular revaluations which is to accurately reflect the fluctuation in rental values in the property market and to redistribute rates paid accordingly.

As the Welsh Government intends to fund a transitional relief scheme, not providing a transitional relief scheme would mean there would be additional funding available for other Welsh Government priorities. In 2017-18 the cost of providing transitional relief to small businesses is estimated to be approximately £10 million.

## **Option 2 – Make regulations providing for transitional relief for small businesses affected by the revaluation**

### **Costs**

The transitional relief scheme will be funded by the Welsh Government, rather than through restricting the reductions for ratepayers whose rateable value is decreasing, or by reducing the amount of funding available for local authorities. This means that funding allocated to the scheme will not be available to support other Welsh Government priorities.

The cost of the scheme depends on the number of ratepayers eligible for the scheme, which is primarily based on being in receipt of SBRR on 31 March 2016. This excludes certain types of property such as that owned by local authorities, car parks or electronic communication devices. If a property is in receipt of other types of relief, such as empty property relief or charitable relief, it will also not be eligible. The other determinant of the cost of the scheme will be the total value of the increases in liability for eligible ratepayers as the transitional relief allows ratepayers to phase in their increase in liability over a three-year period, with a 75% reduction in year one, 50% in year two and 25% in year three. Taking these factors into consideration, it is estimated that £10 million of transitional relief will be provided to assist more than 7,000 eligible ratepayers in 2017-18. This relief will be fully funded by the Welsh Government.

In addition to the actual cost of providing the relief, there will be some additional costs such as the administrative costs to local authorities and associated costs for amending core software systems. The actuals costs will depend on the arrangements that individual authorities make to administer transitional relief. However, steps have been taken to seek to minimise these costs where

possible for example, ensuring that the transitional relief is as simple as possible and can be directly applied to ratepayers bills so that no application process is required, as well as introducing a minimum increase in liability below which transitional relief is not applicable.

As the transitional relief will only apply to eligible ratepayers whose entitlement to SBRR is affected by the revaluation, it will not assist all ratepayers who have an increase in their rateable value following the revaluation. Nevertheless, as approximately three-quarters of ratepayers are currently eligible for SBRR, this transitional relief will provide assistance to many of those affected.

The sectors which may be affected by the provision of transitional relief which is targeted at small businesses, include those where average rateable values are increasing and properties are generally valued over £12,000 (ie. outside the thresholds for SBRR), for example:

- Universities
- Car parks
- Hotels
- Libraries and museums
- Garages and petrol stations

### Benefits

This scheme will assist ratepayers whose eligibility for SBRR is affected by the revaluation. As many of these ratepayers will have been entitled to 100% relief and therefore not previously paid any rates, any increase in liability will be significant. Examples of this are set out in the following table.

2010 Rateable Value	2016-17 Liability*	2017 Rateable Value	2017-18 Liability*	
			Before TR	After TR
£3,500	£0	£8,000	£1,330	£333
£5,995	£0	£12,500	£6,238	£1,560
£7,000	£567	£11,500	£5,260	£1,740
£8,500	£1,721	£17,000	£8,483	£3,412

\* using the multiplier of 48.6p

\*\* using provisional multiplier of 49.9p

As non-domestic rates can represent a higher proportion of overheads for smaller businesses and these businesses also have less opportunity to adapt to an increase in costs in the shorter term, for example by increasing prices or reducing production costs, then it is likely that small businesses currently in receipt of SBRR are most likely to be affected by an increase in their rates bills following the revaluation. As such, targeting a transitional relief scheme which is to be fully funded by the Welsh Government at those most likely to be affected represents an effective use of finite resources.



In addition to these benefits, this transitional relief scheme:

- is considerably simpler than a self-financing transitional relief scheme;
- ensures that all ratepayers are paying their full liability before preparation for the next revaluation exercise commences; and
- does not disadvantage ratepayers with a reduction in their liability by restricting these reductions to pay for a cap on increases.

### **Option 3 – Make regulations based on the transitional relief scheme provided in England**

#### **Costs**

If regulations were made providing for a self-financing transitional relief scheme like the one currently operating in England, then the relief would need to be financed by limiting reductions for ratepayers whose rateable value has decreased as a result of the revaluation.

This means that areas or business sectors which have decreased in value as a result of the revaluation (for example, because there is less demand to be located in that area or the business sector is doing less well, and rental values have decreased accordingly) would need to fund the relief that was provided to those areas increasing in rateable value. As a result, these ratepayers would not be able to benefit from the full reduction in their liability for a number of years, and a small minority would not receive their full reduction before the next revaluation exercise. The effect of this is likely to be exacerbated by the fact that the 2015 revaluation was postponed until 2017, meaning that these ratepayers will have been paying their current liability based on rateable values set in 2008, which reflected rental values prior to the recession.

The caps on increases and decreases in rateable value required in order to provide for a self-financing transitional relief scheme will depend on the total rateable value increasing compared to that decreasing, whether different thresholds are applied for smaller and larger hereditaments, and the distribution of properties across the rateable value range.

The following table provides an illustrative example of a transitional relief scheme financed by caps on increases and decreases in liability.

	<b>2017-18</b>	<b>2018-19</b>	<b>2019-20</b>	<b>2020-21</b>	<b>2021-22</b>
Upward Cap (Small)	5%	10%	15%	20%	25%
Upward Cap (Medium / Large)	15%	20%	25%	30%	35%
Downward Cap (Small)	20%	30%	40%	50%	60%
Downward Cap (Medium / Large)	5%	7%	9%	11%	13%

To be self-financing:

- The more beneficial the upward caps on increases in liability are, the more restrictive the downward caps need to be;
- The greater total rateable value within the upward cap range, the lower the caps on downward reductions would need to be to offset this;
- The more generous upward and downward caps are for smaller properties, the less generous they would need to be for larger properties.

In the illustrative example above, if such a scheme were introduced in Wales, then the relief provided to ratepayers with an increase in their liability would need to be financed by those ratepayers with a reduction in their liability in sectors and geographic areas such as:

- Iron and Steelworks
- Surgeries and Health Centres
- Power generators
- Shops selling non-food products
- Ratepayers in Merthyr Tydfil, Neath Port Talbot and Newport where average rateable values are decreasing by more than 7%.

In addition to the cost to ratepayers who would have to finance the transitional relief, there are a number of additional costs. Given the complexity of the scheme and the number of ratepayers likely to be in transition, the software and administrative costs of introducing such a scheme would be significant. A self-financing transitional relief scheme also adds complexity to the NDR system making it more difficult for ratepayers to calculate their liability in future years. In turn, this can result in additional administration for local authorities or the VOA.

Also, as the caps to make the relief self-financing can only be based on estimates of changes in rateable values and are based on the draft rating list, there is a financial risk to the Welsh Government that the scheme will not be self-financing. This is particularly the case if there are changes between the publication of the draft rating list on 30 September 2016 and the new list coming into effect on 1 April 2017, or if there are appeals which result in reductions in rateable values during the transitional relief period, once the new list is in force.

## **Benefits**

The primary benefit of a self-financing transitional relief scheme is that it would benefit all ratepayers with an increase in rateable value within the relevant cap thresholds. In the illustrative example above, in year one this would be small properties with an increase in liability of more than 5% and larger properties with an increase in liability of more than 15%.

The beneficiaries of such a scheme would be ratepayers with an increase in their rateable value in sectors and geographic areas such as:

- Universities
- Car parks

- Hotels
- Libraries and museums
- Garages and petrol stations
- Ratepayers in Gwynedd, Conwy and Monmouthshire where rateable values are increasing (on average by 7% or more).

As the Welsh Government intends to fund the transitional relief scheme, implementing a self-financing transitional relief scheme would mean there would be additional funding available for other Welsh Government priorities, in 2017-18 the cost of providing transitional relief is estimated to be approximately £10 million.

## **Consultation**

A consultation on transitional relief for small businesses affected by the 2017 non-domestic rates revaluation was published on 30 September for a five-week period.

<https://consultations.gov.wales/consultations/transitional-relief-small-businesses-affected-2017-non-domestic-rates-revaluation>

The shorter than usual consultation period was necessary because of the limited time between the publication of the Draft Rating list by the Valuation Office Agency and the date by which regulations need to be in place for the scheme to be in effect from 1 April 2017. There were 45 responses to the consultation from local authorities, ratepayers, representative organisations and other stakeholders. A summary of responses is provided as an annex to this document.

## **7 Duties**

### Well-being of Future Generations (Wales) Act 2015

In drafting these regulations, consideration has been given to the Well-being of Future Generations (Wales) Act 2015 and how the policy supports the well-being objectives.

Non-domestic rates can represent a higher proportion of overhead costs for small businesses and those businesses which have a reduction in their small businesses rates relief as a result of the revaluation could, in relative terms, have a significant increase in their liability. Small businesses may also have less ability to adapt in the short term to an increase in costs.

As the transitional relief will assist small businesses who are affected by a reduction in the small business rates relief they receive after the revaluation, these regulations will help to contribute to the Well-being goals of a more prosperous Wales and a more equal Wales.

### Tackling poverty

These Regulations will assist small businesses affected by the revaluation by allowing them to phase in their increase in liability over three-year period, which could help to prevent hardship.

### UNCRC

No particular impact, positive or negative, on the rights of children of the provision of transitional relief to children has been identified. The Regulations will not result in a reduction in funds available for local authorities as the relief will be fully funded by the Welsh Ministers. There should therefore not be any impact on the provision of children's services by local authorities.

### Welsh Language

The consultation included questions in relation any effects the policy decision may have on the opportunities for persons to use the Welsh language and treating the Welsh language no less favourably than the English language in accordance with policy making standards 91 to 93. No responses were received to the consultation on these matters. No specific effects on such matters have been identified in the development of this policy and neither have any opportunities to formulate the policy decision to have positive impacts on the opportunities for persons to use the Welsh language and ensuring the equal treatment of the Welsh language compared to the English language.

### Public sector equality duty

In developing these proposals the Welsh Ministers have had regard to the matters contained in section 149 of the Equality Act 2010. No particular impact, positive or negative, of the provision of transitional relief to businesses on persons who share a protected characteristic. The consultation responses received did not raise any issues which may cause any adverse impact on such persons.

## **8 Competition Assessment**

No competition impacts have been identified as arising from these Regulations.