



<b>Report for:</b>	<b>Cabinet</b>
<b>Date of meeting:</b>	<b>21 March 2017</b>
<b>PART:</b>	<b>1</b>
If Part II, reason:	

<b>Title of report:</b>	<b>Hertfordshire Enviro-Tech Enterprise Zone Designation</b>
Contact:	Cllr Andrew Williams, Leader of the Council  James Deane, Corporate Director (Finance & Operations) Mark Gaynor, Corporate Director (Housing & Regeneration)
Purpose of report:	For Cabinet and Council to consider the financial analysis of the Enterprise Zone business plan and to agree to proceed to formal designation.
Recommendations	That Cabinet recommends Council to: <ol style="list-style-type: none"> <li>1. note the financial analysis set out in the report; and,</li> <li>2. progress to formal designation of the Enterprise Zone on 1<sup>st</sup> April 2017.</li> </ol>
Corporate objectives:	Ensuring economic growth
Implications:	Contained within the body of the report.
Monitoring Officer/S.151 Officer Comments	<p><b>Monitoring Officer:</b></p> <p>On the 29<sup>th</sup> November 2016, Cabinet agreed for the Council to progress to formal designation of the Enterprise Zone (EZ) subject to a further report analysing the business plan for the EZ.</p> <p>The financial analysis is set out in this report, and therefore, subject to agreement of Council, the Enterprise Zone will proceed to formal designation on 1<sup>st</sup> April 2017.</p> <p>Cabinet also delegated authority to complete a memorandum of understanding (MOU). The MOU has now been completed and sets out the strategic direction of the Enterprise Zone and the governance structure for the organisation and operation of the zone.</p>

	<b>S.151 Officer</b> My comments are incorporated into the report.
Consultees	Corporate Management Team
Background papers	Report to Cabinet, November 2016: Hertfordshire Enviro-Tech Enterprise Zone Memorandum of Understanding (attached at Appendix A)
Glossary of acronyms and any other abbreviations used in this report:	DCLG – Department for Communities and Local Government EZ – Enterprise Zone HCC – Hertfordshire County Council LEP – Local Enterprise partnership MoU – Memorandum of Understanding SADC – City of St Albans and District Council

### Executive Summary

1. The Hertfordshire Enterprise Zone (EZ) was approved by the Department for Communities and Local Government (DCLG) in November 2016, and consists of four sites within Dacorum and St Albans (SADC). (Detailed background on the EZ partnership and the governance arrangements was provided to Cabinet in November 2016, attached to this report as Appendix A.)
2. Enterprise Zones enable local economies to unlock key development sites, consolidate and provide infrastructure, attract business and create jobs. All business rates growth generated within the EZ in its 25-year lifespan is kept by the relevant Local Enterprise Partnership (LEP) and local authorities in the area and reinvested in local economic growth. This is a primary benefit of an EZ – outside of a designated EZ, the majority share of business rates growth is not kept locally; instead it is paid over to central government for national redistribution.
3. The principle of retaining 100% of business rates growth for locally determined infrastructure priorities is clearly attractive to all bodies within the EZ. Current modelling suggests that receipts of around £160m over a 25-year period would be retained and spent locally. This amount would make a significant contribution to the cost of the transport improvements required to ensure that growth in the Maylands area, and the East of Hemel Hempstead generally, is sustainable in the medium- to long-term.
4. For HCC, as the Highways Authority, the prospect of this new funding stream means that Maylands infrastructure improvements become more viable, and thus the project can be prioritised above competing projects which are reliant on less certain sources of funding. For DBC and St Albans, bringing forward the infrastructure improvements will unlock local growth potential more quickly and sustainably than without the EZ, and will provide a long-term solution to existing and predicted transport problems.
5. Whilst the potential benefits of the EZ are clear, a key consideration for DBC in considering whether to progress the EZ, is what would be the cost of realising these benefits. As per Recommendation 3 in the November 2016 Cabinet report, the purpose of this report to provide Members with further analysis of the financial considerations in order to inform their decision as to whether to progress the EZ to formal designation (or 'go-live') on 1 April 2017.

6. Since the Cabinet report in November 2016, a review of the EZ business plan has been undertaken by PwC in order to gain assurances over the estimates and assumptions within the plan. Following this review, and based on a range of assumptions, DBC officers have been able to model the potential Dacorum-specific costs of entering the EZ. Based on a range of assumptions detailed later in this report, the cost to DBC in forgone business rates is estimated to be around £6.2m over the next 25 years.
7. It is recommended that Members approve the progression of the EZ on the basis that the potential benefits available to Dacorum, in the form of increased local investment (up to £160m) outweigh the modelled costs to DBC in terms of potential funding forgone (around £6.2m). Whilst both of these figures are subject to change, depending on changes to government policy on business rates and development risk of the sites within the EZ, the material consideration of the benefit being greater than the cost is highly likely to remain constant.

### **Background**

8. Whilst the principle of sacrificing a portion of the Council's potential business rates growth over the next 25 years in order to achieve much needed transport infrastructure may be appealing, in order for members to make an informed decision they need to be aware of the potential cost versus the potential benefit.
9. The 25 year time horizon of an EZ makes the forecasting of this information difficult. There are highly likely to be changes to government policy on business rates and planning over such a long period of time, and there are innumerable variables that could affect the timing of business rates cash flows within the EZ.
10. In order to provide Members with a sound basis for making this decision, Officers have taken a four-stage approach:
  1. Seek assurance that the EZ business plan is robust, i.e. that the planning and development assumptions are sound, and that the resulting forecast on business rates cash-flows is justifiable;
  2. Based on these robust forecasts, model the likely financial benefit that would accrue to DBC in the form of retained business rates if the decision were made not to enter into the EZ;
  3. Compare this DBC financial benefit against the potential additional infrastructure investment if the decision were made to enter the EZ, i.e. cost versus benefit;
  4. Based on the above, make a recommendation to Members as to whether to progress the EZ.
11. Each of these stages is detailed in the subsequent sections of this report.

## The Enterprise Zone business plan

12. As part of the application process to DCLG, financial analysis and modelling was undertaken by the EZ partners to identify the likely forecast scenario for business rates generation and growth. The current financial model forecasts growth of around £160m in business rates which could be retained by the EZ over 25 years. A financial summary is provided on page 7 of this report.
13. The fundamental purpose of this summary is to demonstrate the likely amount of funding which will be retained for local investment if the EZ is progressed. It is important to note that if the EZ does not go ahead, under the current system of business rates over 80% of this funding would be repaid to government for national redistribution rather than spent on local priorities.
14. The current model assumes minor revenue costs for the running of the project and investment in the road network already scheduled, subject to the EZ progressing, of £50m. This leaves a net surplus of £104m for further infrastructure expenditure, which will be planned into the programme on completion of the work currently being undertaken by Highways planners.
15. The key assumptions which underpin the forecast business rates are summarised in the subsequent paragraphs.
16. The business rates income forecast within the financial summary is driven by the **additional floor space** which will be created through the development of the sites within the EZ. The amount of business rates chargeable on this floor space depends on the type of business, so assumptions on the type of business that is likely on these sites is fundamental in determining the overall accuracy of the forecast.
17. The assumptions on business type within the EZ model reflect the planning requirements detailed in the Local Plans of DBC and St Albans together with evidence of considerable market interest in the area demonstrated by land agents and by direct contact with DBC. Account was also taken of proposals in the pipeline such as the development on the 30 acre Homes and Community Agency site in Maylands Gateway. The assumptions were further refined through senior planners from the two councils working in conjunction with the LEP and external consultants, Cushman Wakefield.
18. The next assumption driving the forecast income is the **rateable value** of the businesses likely to be established within the EZ. Estimates have been made by the Revenues Team at DBC based on properties of a similar type currently in the Maylands area.
19. The **occupancy rate** of the sites is assumed to be 95%. The EZ area is hugely attractive to a range of employment types. The location, off junction 8 of the M1, ensures excellent access to London and the greater South East and the national/international transport network. Although the emphasis will be placed on attracting high technology manufacturing through the intervention of, and marketing by, the EZ there is huge demand for logistics and distribution uses.
20. There is also evidence of demand for office space as prices in London continue to be high and office space continues to be lost to housing conversions in town and city centres. The focus of the EZ on provision of the

required infrastructure, largely transport and incubation/research space, further adds to the confidence that occupation rates will be high.

### **Business Plan Risks**

21. Pages 8 and 9 of the report show four additional scenarios which have been modelled to test alternative outcomes for the EZ. The following analysis relates to the scenario modelling shown on these pages.
22. **Scenario 2** reflects a general assumption of a 30% reduction in forecast business rates income over the period of the EZ. There are innumerable scenarios that could be modelled, with each of the assumptions detailed in the previous section open to myriad different outcomes, so a high level 30% reduction has been assessed. The graph shows that in this case over the 25 year period the EZ would continue to generate a surplus of £45m for further local investment. (This is in addition to the £57m investment already planned to be funded through the EZ.)
23. The reduction in the surplus of c£60m may have an impact on the infrastructure improvements that could be delivered in the area depending on whether HCC, LEP and the EZ itself could attract additional external funding for the scheme. However, the key point is that there would still be, in total, over £80m of funding retained locally that would be paid over to central government if the EZ does not proceed.
24. **Scenarios 3, 4, and 5** demonstrate how the EZ would be affected by different permutations of the sites within St Albans to reflect the potential impact of any issues arising from the delayed approval of their local plan. The key point is that although the overall funding available locally will be reduced, due to the impact on business rates growth, in each case there will be substantially more funding available than if the EZ did not proceed.
25. It should be noted that scenarios 3 and 4 show the majority of the currently capital investment removed because it relates to the unlocking of the Crown Estate site within St Albans, which clearly would not be required should SADC withdraw from the EZ.
26. PwC were commissioned by the LEP and associated LA partners to undertake a review of the EZ business plan. PwC made a number of recommendations for keeping the plan under review, but there were no errors or inconsistencies identified which would materially affect the outcome of the scenarios modelled.

### **Financial benefit to DBC of not proceeding with the EZ**

27. Following the review by PwC, DBC officers have used the business rates forecast for sites within Dacorum to model the level of business rates growth that DBC would have received from the development of the sites if the EZ did not proceed.
28. This process required a number of assumptions and estimates covering a period of 25 years that are highly likely to change depending, amongst other things, on future governments' approach to business rates. On this basis the modelling assumes that the current scheme of business rates will continue as per the current business rates scheme. The key elements contained within this assumption are:

1. DBC retains 20% of all business rates growth above its baseline; and,
  2. DBC attracts Business Rates Baseline Funding broadly equal to 5% of the taxbase.
29. In addition, and to reflect current conversations which are forming part of the government's review of the current business rates scheme, we have assumed that business rates baselines would be reset every 5 years.
30. Based on these assumptions, of the total £81m business rates growth generated on EZ sites within Dacorum over the next 25 years, DBC would retain £6.2m of additional funding which would not be retained if the EZ proceeds. This funding would be unrestricted and could be spent by DBC to support any of its services or objectives. £2.8m of this funding would be generated over the 5-year period between 2019 and 2024.
31. It is important to note that this forecast is based on the significant assumption that retention rates will continue as they are currently for the next 25 years. In reality, we know that this assumption will effectively become outdated when the government implements its new business rates scheme in 2019. In the absence of any detail on the future scheme, forecasting based on any other assumptions would be more akin to speculation than providing a robust rationale for Members' decision-making.

### **Summary**

32. In summary, the modelling indicates that in the worst case scenario (scenario 3) there would be £88m available for local investment if the EZ proceeds. This is an extremely unlikely scenario, with a more likely outcome a combination of scenarios 1 and 2, which would deliver between £111m and £160m of additional local investment.
33. The 'cost' for DBC of securing this additional local investment, based on the current business rates scheme would be £6.2m over the 25 year period.

## Financial summary of the Enterprise Zone forecast business case

	2016/17 Yo	2017/18 Y1	2018/19 Y2	2019/20 Y3	2020/21 Y4	2021/22 Y5	2022/23 Y6	2023/24 Y7	2024/25 Y8	2025/26 Y9	2026/27 Y10	2027/28 – 2041/42 Y11 – Y25	Total
Cumulative rateable area (m <sup>2</sup> )	-	-	4,000	36,625	71,715	85,915	85,915	94,915	94,915	94,915	114,915	246,915	246,915
Total forecast Business Rates income (£'000)	-	-	139	1,270	2,836	3,621	3,810	4,047	4,047	4,047	5,039	129,300	158,200
Other grant income <sup>a</sup> (£'000)	150	-	1,500	1,600	-	-	-	-	-	-	-	-	3,250
<b>Revenue sub total (£'000)</b>	<b>150</b>	<b>-</b>	<b>1,639</b>	<b>2,870</b>	<b>2,836</b>	<b>3,621</b>	<b>3,810</b>	<b>4,047</b>	<b>4,047</b>	<b>4,047</b>	<b>5,039</b>	<b>129,300</b>	<b>161,450</b>
Forecast revenue costs (£'000)	(30)	(120)	(186)	(186)	(193)	(197)	(99)	-	-	-	-	-	(1,011)
<b>Net revenue position (£'000)</b>	<b>120</b>	<b>(120)</b>	<b>1,453</b>	<b>2,684</b>	<b>2,643</b>	<b>3,424</b>	<b>3,711</b>	<b>4,047</b>	<b>4,047</b>	<b>4,047</b>	<b>5,039</b>	<b>129,300</b>	<b>160,439</b>
Forecast capital costs (£'000)	(170)	(25)	(10)	(1,000)	(1,000)	(9,000)	(5,000)	(5,000)	(35,000)	-	-	-	(56,205)
<b>Net Position (£'000)</b>	<b>(50)</b>	<b>(145)</b>	<b>1,443</b>	<b>1,684</b>	<b>1,643</b>	<b>(5,576)</b>	<b>(1,289)</b>	<b>(953)</b>	<b>(30,953)</b>	<b>4,047</b>	<b>5,039</b>	<b>129,300</b>	<b>104,234</b>
<b>Cumulative Net Position (£'000)</b>	<b>(50)</b>	<b>(195)</b>	<b>1,248</b>	<b>2,932</b>	<b>4,575</b>	<b>(1,001)</b>	<b>(2,290)</b>	<b>(3,243)</b>	<b>(34,196)</b>	<b>(30,149)</b>	<b>(25,110)</b>	<b>104,190*</b>	

\*The £44,000 difference is due to rounding.

## Considerations for further scenario planning

### Scenario planning performed by management

The current business case for the Enterprise Zone includes a management defined worst case scenario financial projection. This assumes that there will be an additional 30% reduction on the existing 95% occupancy rate. The business rate income is therefore discounted by 30% from the financial summary included on page 9 of this report. This reduces the surplus over the 25 life of the Enterprise Zone from £104m to £45m.

We also reviewed a paper produced by management which considered the following scenarios:

Scenario 1: Proceed with the Enterprise Zone in its current state.

Scenario 2: Reduction in 30% in the business rate income.

Scenario 3: Assume that the Crown Estate will be delayed by five years.

Scenario 4: Assume that the Enterprise Zone will not include the Crown Estate.

Scenario 5: Assume the Enterprise Zone proceeds without St. Albans sites.

The paper lists the risks and assumptions included in the scenario, the total business rate income which would be generated and the costs which would be covered.

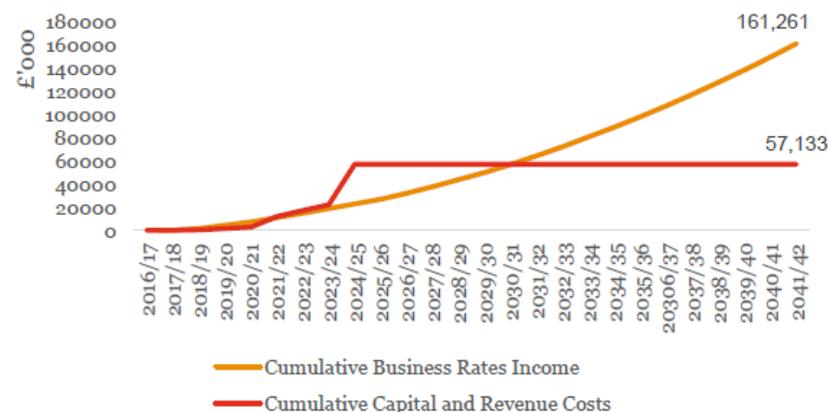
On the following page we have represented each of the scenarios graphically, including both the annual business rate income and the capital infrastructure funding that will be needed.

### Observations on the scenario planning

The five scenarios have very different profiling for the capital costs which will be incurred as part of the programme.

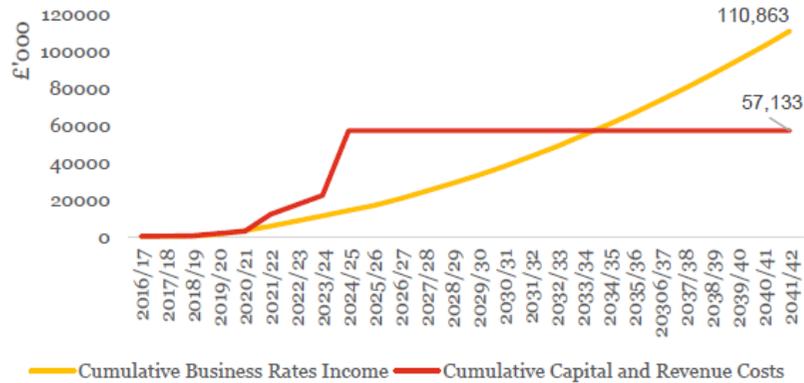
It is clear that the business rate income retention levels vary significantly across the scenarios. In developing scenario analysis going forward, management should consider the benefit for agreeing a performance metric for retained levels that could act a floor threshold. Retention levels that are forecast to be below this level could then trigger further management review and the need for potential remedial action.

### Scenario 1 - Current Business Case

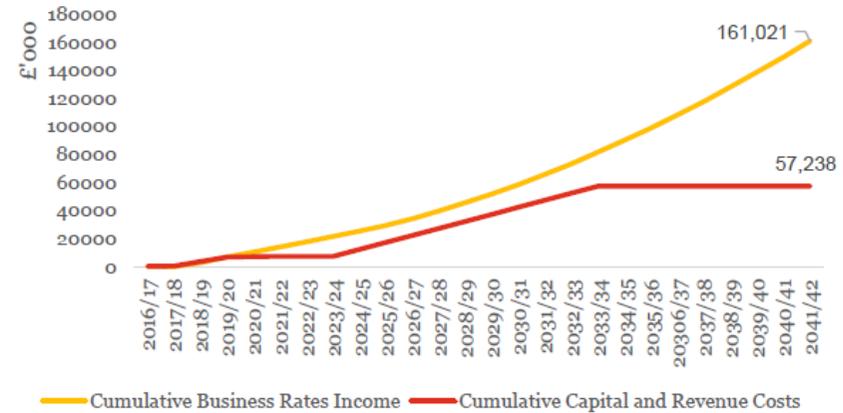


## Considerations for further scenario planning

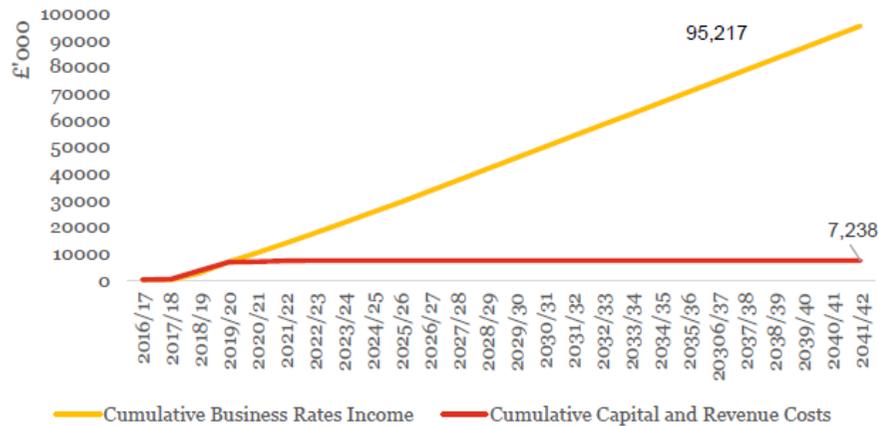
**Scenario 2 - 30% Reduction on Business Rates**



**Scenario 3 - Delay in the Crown Estate**



**Scenario 4 - No Crown Estate**



**Scenario 5 - No St. Albans Sites**

