Planning Magazine Article on Enterprise Zones

Author

Dr Paul Greenhalgh

Reader in Property Economics

School of the Built and Natural Environment

Northumbria University

Title

Opportunity knocks – what prospects for the 'new breed' of Enterprise Zones?

Introduction

Enterprise Zones were first introduced in the U.K. in 1980 and their influence, and the distortion they create in local property markets, is well recognised and long-lived. There is a wealth of literature both from the U.K. and U.S. about their strengths (encouraging capital investment in locations that might otherwise receive little attention) and weaknesses (occupier displacement and poor value for money to name a couple). Scrutinising the Enterprise Zone Prospectus (CLG 2011) published shortly after the Chancellor announced the Government's intention to introduce up to 21 new EZs in England, it is evident that there is some cognisance amongst policy makers of the flaws and side-effects of the old model. This article reviews the new proposals and offers comparison with the 'old style' EZs.

The Government announced its intention to a 'new breed' EZs, with a first 'vanguard' phase of 11 LEP-led zones to be designated in selected urban areas/city regions. Remaining LEPs are invited to submit expressions of interest in a second phase, of up to 10 zones, by the end of this month. The driver for their reintroduction is the Government's desire to be seen to be reducing barriers and burdens for business, including planning reform, and the pro-growth agenda being promoted by the Chancellor. The Government claims to be interested in '*creating growth conditions*' by backing areas with '*real potential'* and '*genuine economic opportunity*'. Clearly there is significant potential for optimism bias in the resulting bids for EZ status.

Designation and Selection of sites

New breed EZs are to be designated only in England, whereas old style EZs were one of the few urban initiatives that were rolled out across the whole of the U.K.. Local Enterprise Partnerships are to take the lead role in the selection and designation of new EZs, with a notional allocation of one per LEP. It is unclear what will happen where there are overlapping LEPs. The distribution of zones based on natural/functional economic areas is a potential improvement on old style EZs which often bore little relation to local economies.

An interesting question is who will have the final say in determining designation. Will it be the business-led LEP, its Local Authority partners or Central Government? The EZ prospectus indicates that there must be unanimity between all LAs making up the LEP for designation, thus it only needs one authority in a LEP area to oppose designation for it not to happen. This will add an interesting dynamic to the horse trading that will inevitably take place over where zones should be located, and increase the prospect of parochialism and vested interests coming to the fore, as areas compete for a zone in their area. Managing this process could be the sternest test faced by the fledgling LEPs to date.

The prospectus suggests that most zones, when designated, will be cleared and predominantly empty sites, presumably to avoid deadweight payments to existing businesses. It will therefore take some time, even with simplified planning in place, for new accommodation to become available and it is therefore critical that sites 'hit the ground running', to avoid potential occupiers missing out on the five year rates holiday, the qualification for which closes in 2015. The focus on 'new' sites that are not already built up, may favour greenfield development rather than the redevelopment of brownfield, with all their inherited problems. Many of the later phase 'old' EZs were situated on greenfield sites located close to major trunk road, for example Doxford Park in Sunderland. Previous EZ evaluations (see PA Cambridge 1995) confirm that the most successful zones not only benefitted from excellent road and IT communications and were not encumbered by dereliction, contamination and outdated infrastructure.

The new breed zones will be in the region of 50-150 ha and appear to be framed around single or contiguous sites in single ownership. In contrast, most of the old style zones were a collection of fragmented and disconnected sites, sometimes spread across different authorities. In theory new zones could straddle LA boundaries or be covered by two overlapping LEPS although this may be unlikely. It is also worth contemplating how compatible these locations will be with PPS4 and the need to plan for sustainable economic growth. Too many old EZs were developed in unsustainable locations, with poor public transport provision, that encouraged car use, and benefitted from few amenities and facilities, for example Cobalt Business Park in North Tyneside and Doxford International in Sunderland.

A major concern is that of the ownership of land that is given EZ status. A lesson learnt during the last EZ experiment was that landowners receive a windfall benefit from designation, as their land holdings increase in value many-fold, but have done nothing to earn it. For this reason, later EZ designations required all EZ land to be in public ownership at designation, to the extent that private landowners even sold land to a local authority at non-zone values and bought it back again at inflated on-zone prices. It appears that this lesson has not been heeded as some of the first tranche of zones are not publicly owned and that private landowners will benefit, e.g. the Boots Campus in Nottingham, and Liverpool Waters owned by the Peel Group (contrasted with Manchester Airport owned by a consortium of LAs and the Royal Docks owned by the London Development Agency). The potential for private companies and individuals to receive windfall gains from EZ designation makes it even more crucial that the process of site selection, by the business-led LEPs, be handled in a transparent and accountable way and for there to be a clear justification and rationale as to why a site in private ownership may be chosen ahead of publicly owned land.

Planning and end uses

The Government appears keen to encourage the use of Local Development Orders to simplify and fast-track EZ development. This is not dissimilar to the Simplified Planning Zones of the eighties, a status that was incorporated into the old EZ model. LPAs are also encouraged to extend the simplified planning framework beyond the boundaries of the EZ itself. This 'fuzzy boundary' may diminish some of the boundary issues associated with the old zones, although it is unlikely to prevent boundary hopping as the land benefitting from rates free status will still have a hard boundary.

LEPs are expected to define and agree the 'sectoral focus' for zones although quite how they will identify and enforce such focus is unclear. The potential to use planning use classes and restrictive covenants to control the type of development and occupation would seem contradictory in the face of the Government's reform of what it sees as an unnecessarily restrictive and inflexible planning system. There have been some suggestions that zones should not only exclude retailing, as the later phases of old EZ's did, but should focus solely on manufacturing (B1 (b) (c), B2, B8) by excluding B1 (a) office development.

Infrastructure and investment

A key lesson learnt from the old EZs was that, to be successful in property development terms, sites needed significant investment in infrastructure; those that were poorly served tended to underperform. Where will the capital funding for investment for infrastructure come from during this period of austerity? Previously it was Zone Authorities and UDCs, that exploited a variety of funding streams to pay for zone infrastructure. The Government would like to see the use of Tax Increment Financing (TIF), in combination with EZ designation, to pay for infrastructure investment. The introduction of TIF is subject to primary legislation, but the model has been used for decades in the U.S. to raise money secured against future income streams (see below). New EZs could also be strategically aligned/overlapped with Regional Growth Fund projects and Tier 1 and 2 ERDF qualifying areas to exploit these alternative funding streams to pay for necessary infrastructure investment.

Business rate relief and capital allowances

The Localism Bill, which is scheduled to receive Royal Assent by November 2011, will introduce the power for Local authorities to grant business rates discounts of up to 100% to property occupiers in the new EZs. Businesses occupying accommodation in a zone by April 2015 may qualify for a maximum of £55k p.a. or £255k over 5 years (half the duration of old EZs). The upper limit is the *de minimis* state aid threshold. As with the old style EZs, HM Treasury will reimburse LAs for the rates revenue foregone (see Annex A of EZ Prospectus for further information). We know from evaluation of the previous EZ experiment that around half of any rates relief received by tenants will be captured by landlords through increased rents. This again raises the question of who benefits from zone designation and also exposes tenants to a double hit of the reintroduction of rates at zone expiry plus inflated rents on upward only rent review terms. In the past this double whammy was enough to send some firms under, however the absence of capital allowances (see later) may result in a smaller differential between on and off zone rents.

The Localism Bill, currently before Parliament, will allow LAs to retain the uplift in business rates for a period of at least 25 years and it is against this potential long term income stream that forms the basis for the introduction of TIF. The increased rates generated in an EZ will be pooled and redistributed amongst participating LAs to support LEP priorities, although how will this be done in unclear. LAs in a LEP, that do not benefit directly from EZ designation, may be concerned that the authority where the EZ is located may claim the lion's share of the additional rate revenue generated by the zone.

The incentive that made old EZs successful in terms of attracting investment into an area and the construction of prodigious quantities of floorspace, was the availability of 100% capital allowances. It certainly helps explain what the largest shopping centre in Europe is doing in Gateshead (the Metro Centre was in the Tyneside EZ) and why soon the biggest office park in the U.K. will be in North Tyneside (Cobalt Business Park was in the Tyne Riverside EZ). Capital allowances also contributed to the greatest market distortion, not only by creating a 'honey pot' of investment in one location, to the detriment of others, but also indirectly subsidising the occupation of zone property by way of incentives such as rent free periods, to the extent that off-zone development cannot compete. Perhaps mindful of this, the Government has made it clear that there will be no capital allowances (tax breaks) in the new EZs except in exceptional circumstances, for example for plant and machinery for manufacturing, perhaps linked to special sector that requires intensive capital investment e.g. manufacturing of machinery for renewable energy generation etc. Such allowances would also be subject to state aid clearance and thresholds.

Summary

The big question about the new breed of EZ is whether the package of incentives will be enough to make a difference. There is a view from some in the business community that the EZ offer is decidedly modest and may make little difference to most firms. The proposed new EZs are certainly a 'lite' version of their forbears, with half the lifespan, reduced availability of capital funding for infrastructure and no significant capital allowances. This may not necessarily be a bad thing as there were manifest problems with the old style of EZs; indeed their influence is still to wane in some parts of the country due to the use of golden contracts that extended the life of capital allowance for five year or more. Some commentators have suggested that new EZ status may worth only around £1m over the lifetime of the zone, which is small change compared to the hundreds of millions of pound of ERDF funding that England is missing out on due a lack of match fund, however if a zone is successful in attracting investment and occupiers, then the value of the additional rates revenue over 25 years will be considerable. Uncertainty will surround the creation of new EZs for some time, not least because some of the legislation required to make them happen still has to pass through Parliament, and it will be interesting to see how well the LEPs perform in reconciling the broad range of competing interests, to identify a clear winner and negotiate how the winnings are shared out. Finally, the tipping point between success and failure may well lie with the ability of a LEP and its partners to align the new EZ with other funding streams to secure vital capital investment for infrastructure.

Bibliography

Communities and Local Government (2011) *Enterprise Zone Prospectus*. London. CLG

Larkin, K. And Wilcox, Z. (2011) *What would Maggie do? Why the Government's policy on Enterprise zones needs to be radically different to the failed policy of the 1980s*. Centre for Cities. London

Office of the Deputy Prime Minister (2003) *Transferable lessons from enterprise zones* (Summary No. 12). London. HMSO

PA Cambridge (1995) *Final Evaluation of Enterprise Zones*. London. DoE

Sissons, A. and Brown, C. (2011) *Do Enterprise Zones Work? An Ideopolis policy paper*. London. The Work Foundation