Neutral Citation: [2017] NIQB 32

Ref: **COL10218**

Delivered: **15/3/2017**

Judgment: approved by the Court for handing down

*(subject to editorial corrections)**

IN THE HIGH COURT OF JUSTICE IN NORTHERN IRELAND

_____

QUEEN'S BENCH DIVISION (JUDICIAL REVIEW)

_____

IN THE MATTER OF AN APPLICATION BY MID-ULSTER DISTRICT COUNCIL

FOR LEAVE TO APPLY FOR JUDICIAL REVIEW OF A DECISION OF THE DEPARTMENT OF THE ENVIRONMENT

_____

COLTON J

The Issue

[1] The issue in this case is whether the Department of the Environment (hereinafter "the Department") has acted lawfully in determining the method by which the amount of the annual Rates Support Grant (hereinafter the "RSG") paid to the Mid-Ulster District Council (hereinafter "the Council") is calculated.

[2] I am greatly obliged to counsel and their respective solicitors in this matter for their assistance in the preparation and presentation of this case. Peter Oldham QC appeared on behalf of the applicant instructed by P A Duffy & Co Solicitors. Nick Hanna QC and Mr Donal Lunny appeared on behalf of the Department instructed by the Departmental Solicitors Office.

Background

[3] Since 1 April 2015 the Council is one of 11 District Councils responsible for Local Government in Northern Ireland. It was created after a major Local Government reorganisation, replacing the former Cookstown District Council, Dungannon and South Tyrone Borough Council and Magherafelt District Council.

[4] A District Council's income is made up largely of rates, which are levied on domestic and non-domestic properties, de-rating grant, and RSG. De-rating grant and RSG are direct financial support provided by the Department of the Environment.

[5] De-rating grant compensates Councils for the loss of revenue through the statutory de-rating of certain properties.

[6] RSG is a grant system for Local Government in Northern Ireland which is administered and operated by the Department under the provisions of the Local Government (Rates Support Grant) Regulations (Northern Ireland) 2011 and predecessor Regulations. The policy objective of the RSG is to provide supplementary financial support to those eligible District Councils whose needs relative to other Councils are deemed to exceed their wealth base relative to other Councils.

[7] The total amount of RSG available for distribution among eligible Councils each year is determined in advance by the DOE as part of the public expenditure process and can vary from year to year. Once the fixed total has been determined the Department distributes this fixed amount of money among eligible Councils. If any supplementary amounts of grant are made available by the Department during a financial year then this is similarly distributed.

[8] This dispute centres on the formula or method used by the Department to determine how the fixed amount of RSG is to be distributed between the 11 Councils in Northern Ireland.

The legislative scheme and the calculation of RSG

[9] The legislative scheme dealing with the calculation of District Rates and the RSG is complex, in my view unduly so. The calculations are governed by a labyrinth of interlinking statutes and regulations. They are further complicated by differences in how domestic and non-domestic rates are calculated and by the fact that domestic and non-domestic properties have been revalued in Northern Ireland separately.

The situation prior to 2011

[10] From 1976 until 1996 inclusive, both domestic and non-domestic properties were originally valued, for rating purposes, on the basis of their rental value (at 1 April 1967). Each District Council set a single rate and the total amount to be raised from district rates was distributed between the domestic and non-domestic sectors in each district in accordance with the original (1976) distribution of the total rental value in that district between the domestic and non-domestic sectors.

[11] In April 1997 there was a revaluation of non-domestic properties, and there have been periodic revaluations of both the domestic and non-domestic sectors since. From 1997 two rates have been set by each Council (one for the domestic and non-domestic sectors respectively) but the relative share of the total district rate burden borne by the non-domestic and domestic sectors in each District Council area has been retained at the same level as existed in 1976. The relativity was maintained

in the years subsequent to 1996 by applying what was then termed a "growth factor" to the rate set for non-domestic properties. Although the term "growth factor" was not referred to in legislation, a Council specific i.e. individual growth factor was used.

[12] In 2007, domestic properties became valued for rating purposes by their assumed sale (capital), rather than rental, value. Further, for the first time, growth factors, now termed conversion factors, were set out in statute.

[13] Thus the Rates (Making and Levying of Different Rates) Regulations (Northern Ireland) 2006 provided:

> "Making and Levying of Different Rates
>
> **2.** In respect of the year ending on 31st March 2008 and each subsequent year, different regional and district rates may be made and levied on—
>
> (a) the rateable net annual values of hereditaments; and
>
> (b) the rateable capital values of hereditaments.
>
> **3.**—(1) In respect of the year ending on 31st March 2008 and each subsequent year, a capital value district rate shall be made by a district council in accordance with the formula—
>
> Where
>
> A is the capital value district rate;
>
> B is the net annual value district rate made by that Council; and
>
> C is the conversion factor for that Council as set out in the Schedule.
>
> (2) In this regulation—
>
> 'capital value district rate', in relation to a District Council, means a district rate made by that Council on the rateable capital values of hereditaments in the district;
>
> 'net annual value district rate', in relation to a District Council, means a district rate made by that Council on the rateable net annual values of hereditaments in the district."

[14] The schedule referred to in the definition of factor C in Regulation 3(1) then set out different conversion factors for the then existing District Councils. The conversion factor was to take account of:

(a) The on-going requirement to keep the relevant burden of rates for domestic and non-domestic premises the same; and

(b) To prescribe a formula linking rental values with capital values.

[15] After the Local Government re-organisation which led to the creation of the new 11 Councils the need to set conversion factors for the new District Councils was provided by the Rates (Making and Levying of Different Rates) Regulations (Northern Ireland) 2015.

[16] To bring matters up to date all domestic properties in Northern Ireland are currently valued at 2005 values. All non-domestic properties are currently valued against 2013 values.

[17] The use of a specific conversion factor for a particular Council for the purposes of calculating rates is fundamental to the understanding of the dispute in this case.

[18] Throughout all of this period, the DOE has provided additional finance to District Councils, originally termed the resources element of the General Exchequer Grant, now called RSG. As indicated above the policy objective of the RSG is to provide supplementary financial support to eligible Councils as determined by "wealth" minus "needs" approach.

The 2011 Act and Regulations

[19] RSG is provided for by Section 27 of the 2011 Act as follows:

> "27.– (1) The Department shall for each financial year make a grant under this section to councils (unless in any particular case the amount of the grant would be nil).
>
> (2) In this section "the rates support grant" means the grant made under this section for any financial year.
>
> (3) The amount of the rates support grant payable to a council for any financial year shall be determined in accordance with regulations and shall not be reduced during the financial year in question.

….

(5) Regulations under this section may in particular make provision–

(a) for the amount of the rates support grant to be calculated by reference to a formula;

(b) for determining the manner in which and time at which that calculation is to be made.

(6) The formula may be such that the amount payable is nil.

(7) For the purposes of this section 'formula' includes methods, principles and rules of any description. …."

The Regulations under Section 27(3) of the 2011 Act are the 2011 Regulations. These provide:

"**Rates support grant**

3. For the financial year beginning on 1st April 2012 and each successive year the Department shall determine the amount of rates support grant payable to a council in accordance with the formula described in Schedule 1."

[20] Schedule 1 Part 1 Paragraph 2 provides that:

"The formula to determine a Council's entitlement to rates support grant shall be –

$$\frac{\text{Wealth}}{\text{N Ireland gross penny rate produce}} \text{ x 100} - \frac{\text{Needs}}{\text{N Ireland home population adjusted}} \text{ x 100} = \text{surplus or negative}$$

Paragraph 3 goes on to provide that "to calculate the proportion of rates support grant payable to a Council, the total of negative variances shall be calculated and each Council's negative variants (if any) expressed as a percentage of the total.

$$\frac{\text{Council's negative variance}}{\text{Total of councils' negative variances}} \text{ x 100} = \text{Percentage allocation of total grant}$$

[21] It is clear from the terms of the formula that the purpose is to make provision for the distribution of RSG amongst those eligible District Councils whose needs (as defined) are deemed to exceed their wealth (as defined). The Council will be entitled to a share of RSG if, applying the statutory formula, it has a "negative variance" (in other words if its wealth (as defined) is less than its needs (as defined)).

[22] What is at issue in this case is the determination of "wealth". There is no dispute in relation to the "needs" aspect of the formula.

[23] It will be seen that a core element of the wealth calculation is what is referred to as the "gross penny rate product" (hereinafter "GPRP"). Regulation 2 of the 2011 Regulations provides that "gross penny rate product" means the income that may be raised from one penny of district rates on rateable and de-rated properties, as determined by the Department on the basis of data provided by the Department of Finance and Personnel.

[24] As is the case with the calculation of rates the calculation of the GPRP faces the same difficulties in relation to the different ways in which domestic and non-domestic hereditaments are valued and the different dates upon which they have been valued. Whilst the statute does not provide expressly for a conversion factor to deal with this difficulty it is accepted by the parties that in order to provide this calculation a conversion factor is needed.

[25] Herein arises the dispute between the parties. The Department applies a Northern Ireland average conversion factor for the purposes of the statutory formula. The Council say that a specific Council conversion factor should be applied.

[26] This issue is by no means an academic one. As a result of the calculations carried out by the Department the Council has been informed that its RSG allocation for 2015/2016 was £2,401,549. On 3 July 2014 the Department's Analytical Services Branch provided a report entitled "Local Government Rates Support Grant Formula; Methodology Note".

[27] The report investigated the impact of two possible sets of conversion factors on the Local Government Rates Support Grant Allocations 2014/15. The two sets of conversion factors were an average Northern Ireland conversation factor and the individual specific Council factor. The report prepared a table indicating what RSG the 11 districts would have received if their individual conversion factors had been used. This demonstrated that the applicant in this case would have received £975,370 RSG more than it did for 2014/2015 had individual conversion factors been used. Two other Councils would also have received more, four would have received less and four which in fact received no RWG would still have received none.

[28] The report is not a policy document and merely provides an analysis of applying different approaches to the calculation but nonetheless it provides an interesting insight into the methodology adopted by the Department. Under the heading "Impact of Conversion Factors on Local Government Rates Support Grant" it reports the following:

> "A key data set in the calculation of the Local Government Rate Support Grant is the gross penny rate product (GPRP). The formula is very sensitive to changes to this key variable. A major component of the GPRP is the estimated penny product, which estimates the income one penny on the district rate will provide in a given year. The calculation of the estimated penny product involves a domestic rate, based on capital values, and the non-domestic rate based on rental values. To convert between these two different values, in order to arrive at a single estimated penny product, it is necessary to use a conversion factor. From a rates support grant perspective, the theoretically correct way to do this is to use a single Northern Ireland level conversion factor and uniformly apply it to each Council and this is the method currently used. However, the regulations surrounding the calculation of the rates support grant, as presently written, do not provide any guidance as to whether individual or average conversion factors should be used when calculating GPRP. An alternative interpretation could be that individual conversion factors should provide the basis for the conversion."

[29] In its conclusions when it refers to the theoretical exercise it carried out in applying individual conversion factors the report points out that three Councils would see a change in their grant allocation of more than 25%. The report goes on to say:

> "Again it must be stressed that this is a purely theoretical sensitivity test in that the correct conversion factor to apply is the NI average. However, it may be the case that the Regulations themselves might need to be revisited in order to make them consistent with the current approach. This issue will be for policy colleagues to consider and decide."

[30] I will return to this report later and in particular to the concept of "estimated penny product" which clearly is a key element in the calculation of GPRP.

The arguments of the parties

[31] The central submissions of the parties are a mirror image of each other. The applicant argues that the use of an average factor is ultra vires and that the legislation expressly requires the use of an individual factor. Further and alternatively it argues that use of the average conversion factor defeats the purpose of the legislation providing for RSG. Conversely the defendant argues that as a matter of statutory interpretation the calculation requires the use of an average conversion factor as opposed to a Council specific conversion factor. In support of this contention the Department argues that the use of individual Council specific conversion factors would frustrate and defeat the purpose of the legislative provisions under consideration.

What does the legislation require?

[32] At this point it is necessary to refer to a further piece of legislation namely the Rates Regulations (Northern Ireland) 2007 (as amended). Regulation 6 provides:

> "(1) … For the purpose of determining under the Local Government (Rates Support Grant) Regulations (Northern Ireland) 2011 the amount of the rates support grant which is payable to a District Council for any year, the products of the rates of one penny in the pound for the district of the Council for that year shall be ascertained in accordance with Schedule 1 or 2."

[33] Schedule 1 provides for the manner of determination of capital values (domestic sector) and Schedule 2 provides for the manner of determination of NAV rates (rental values) (non-domestic sector).

[34] Schedule 1, paragraph 2 provides that the product of a capital value rate of one penny in the pound shall be the gross rate income from each hereditament or part of a hereditament in the capital value list in the district (less certain deductions which are not relevant).

[35] Schedule 2, paragraph 3 states that the "gross rate income" the gross liability or hereditaments or any parts of any hereditaments to rates for year.

[36] Schedule 2 provides similar provisions in relation to the NAV (or rental) rates.

[37] This, Mr Oldham argues, provides the short route to the answer to the issue in this case. The regulations say that the products of the rates of one penny in the pound are to be ascertained by reference to the gross rate income for capital value rates and NAV rates. Paragraph 3 of schedules 1 and 2 states that "gross rate income" is the "gross liability of the hereditaments … to rates". The argument runs that gross liability to rates of domestic properties is the product of a hereditaments capital value and the domestic district rate. The domestic district rate is calculated by multiplying the non-domestic rate by the actual Council's specific conversion factor prescribed in the 2015 Regulations.

[38] Consequently it is argued that the Rates Regulations (Northern Ireland) 2007 require that in calculating RSG, individual conversion factors must be used.

[39] Referring back to the method described in the methodology note in the Analytical Services Branch report it is noted that in coming to a calculation of the GPRP the Department relies on an "estimated penny product" (EPP), which estimates the income one penny on the district rate will provide in a given year. This estimate is based on data provided by the Department of Finance and Personnel (DFP). The Applicant points out that the legislation does not recognise EPP for RSG purposes but rather refers to the Council's actual domestic rate outturn as being the appropriate basis for calculation. It is argued that this further supports the argument that the assessment of a Council's wealth that relates to its domestic sector must be calculated using an individual conversion factor and not a Northern Ireland average conversion factor.

[40] In response, Mr Hanna argues that the reference to the individual conversion factors in the 2015 Regulations relates to the calculation of individual rates for District Councils and cannot be read across for the purposes of calculating RSG.

[41] He develops his argument by saying that the applicant's analysis is misconceived. He places particular emphasis on the reference in Regulation 6 to "the products of the rates of one penny in the pound for the district (underlining added). He says that the use of the plural in the Regulation is important. As should be clear from what is set out above the reason for the use of the plural is because two separate rates have been struck by each Council in each rating year namely the capital value district rates (for the domestic sector) and net annual value district rates (for the non-domestic sector). Again as is clear from what is set out above the capital value district rate is mathematically derived from the NAV district rate by multiplying the latter by a prescribed conversion factor for each Council as set out in the schedule to the Rates (Making and Levying of Different Rates) Regulations (Northern Ireland) 2015. This is the individual or Council specific conversion factor.

[42] The Department say that the issue between the parties in these proceedings arises for the following reason. Although Councils are required to strike two separate rates in each rating year (each of which produces its own separate penny rate product calculated respectively in accordance with Schedules 1 and 2 to 2007

Regulations) the statutory formula fails to make express provision for the fact that there are two separate penny rate products, and simply refers to "gross penny rate product" in the singular (my underlining). Notwithstanding that Regulation 6 of the 2007 Regulations expressly requires the two separate penny rate products to be ascertained and then used in the statutory formula for determining the amount of RSG payable to a Council, the statutory formula itself does not explain how these two separate penny rate products (which are measures of wealth for the purposes of the formula) are to be conjoined in order to produce a single penny rate product for the purposes of the formula. To this extent there is a lacuna in the legislation. The question raised by this lacuna is how these measures of wealth are to be conjoined in such a way as to maintain an accurate measure of the relative wealth basis of all Councils in Northern Ireland, bearing in mind that those measures of wealth are expressed in two different "currencies". (Capital value penny rate products (domestic)) and (NAV penny rate products (non-domestic)).

[43] In resolving this particular issue as to the requirements of the legislation Mr Hanna refers me to the relevant principles of statutory interpretation which are well known namely; the intention of Parliament, the presumption against unfairness, the presumption against absurdity and the presumption of fairness and convenience.

[44] To demonstrate this point the Department (in common with the Council in support of its case) provided a worked example to illustrate, step by step, the way in which Schedules 1 and 2 to the 2007 Regulations have to be applied.

[45] The worked example after carrying out the elaborate exercise required by Schedules 1 and 2 is used to illustrate that the product of a penny rate will always be the same in respect of (1) every domestic hereditament in Northern Ireland which has the same capital value (no matter in which Council district it is situated), and (2) every non-domestic hereditament in Northern Ireland which has the same NAV (no matter in which Council district). The proposition lying at the heart of the Council's case is that the produce of a penny rate (after taking account of the adjustments required by Schedules 1 and 2 respectively in the 2007 Regulations) will always be the result of raising one penny for every pound of the rating list valuation (i.e. 1% of the rating list valuation), and that would be the case whether it is a capital value rate (i.e. domestic) or an NAV rate (i.e. non-domestic).

[46] In arguing that the 2007 Regulations require that, in calculating RSG, individual, Council's specific conversion factors must be used Mr Hanna submits that the Council has failed to recognise that the provisions require the determination of two separate penny rate products (one in respect of a capital value rate, and the other in respect of an NAV rate). He says that the Council has incorrectly and impermissibly conflated the product of a rate of one penny in the pound in paragraph 2 of each schedule with the reference to gross rate income in paragraph 3 and has incorrectly inferred that the legislation makes no distinction between a penny rate product and the total rate product.

The purpose of the legislation providing for RSG

[47] Both sides argue that the overall purpose of the legislation points to the use of the conversion factor for which they contend. As indicated already there is no dispute that a conversion factor is required, the issue is which one.

[48] As Mr Tohill, who is the lead officer for Finance at Mid Ulster District Council, says in his affidavit of 1 October 2015 the intended outcome of the statutory formula is not in dispute between the parties i.e. to distribute a fixed amount of financial assistance in an equitable and proportionate manner between those District Councils whose needs exceed their wealth at the time of the RSG distribution.

[49] Mr Tohill makes the case eloquently for the application of a specific Council conversion factor in paragraphs 17 onwards of his affidavit dated 1 October 2015 in the following way:

> "17. It is evident that the only sensible way that a District's wealth can be measured is by adding the wealth of the domestic sector to the wealth of the non-domestic sector. Quite simply it is necessary to add 'apples and oranges'.
>
> 18. If one accepts the apples and oranges analogy, the only way that apples can be added to oranges is to first convert the apples to oranges or vice versa. In the case of property wealth consisting of domestic and non-domestic properties, it is necessary to convert the wealth of the domestic sector to an equivalent non-domestic sector wealth. This requires the use of conversion factors.
>
> 19. Mathematically the intended result will be produced when the wealth of each Councils domestic sector (originally measured in capital value terms at a prescribed valuation date) is translated (or converted) into wealth measured on the same valuation basis as the wealth of its non-domestic sector (measured in rental value terms at a different valuation date).
>
> 20. I believe that for the translation/conversion to be performed correctly it is necessary to ensure that the relativity of the total value of the domestic sector to the total value of the non-domestic sector for each Council is maintained in the same proportion as was originally the case in 1976. Failure to do this will result in the aggregate measures of each Councils

> wealth being inappropriately impacted by the mathematical consequence of applying a conversion factor that cannot ensure that measures of district wealth are not distorted by variations in the relativity of domestic to non-domestic wealth in other Council districts."

[50] Obviously the use of actual conversion factors will maintain 1976 relativity within a Council district.

[51] However Mr Tohill goes on to argue at paragraph 21:

> "If the 1976 relativity of domestic and non-domestic wealth is not maintained on a Council by Council basis the relative ranking of aggregate District Council wealth (between District Councils) at the time RSG distribution will be distorted. The unavoidable consequences of this distortion would be that RSG would be distributed in a manner that did not achieve the intended purpose of the statutory formula i.e. to distribute a fixed amount of financial assistance (RSG) in an equitable and proportionate manner between those District Councils whose needs exceeds their wealth at the time of RSG distribution."

[52] He then goes on to provide a worked example to demonstrate that the application of a Northern Ireland average conversion factor to three hypothetical Councils in circumstances where their domestic wealth is revalued will result in an inconsistency in the amount of RSG to be distributed.

[53] The essential point made by the Council is that for the purposes of RSG a particular Council's wealth should be derived from its actual rates income. It is argued that a Council's wealth is not dependent on the wealth of any other Council. An average factor does not give an accurate representation of the Council's wealth at a given time. Applying an average factor where the domestic sector has grown by more than allowed for by the Northern Ireland average factor will under-estimate domestic property wealth and lead to an over-distribution of RSG. Conversely applying a Northern Ireland average factor where the domestic sector has grown less than allowed for by the NI average will over estimate domestic property wealth and lead to under-distribution of RSG. In other words an average factor will misstate the amount that one penny in the pound will raise. The use of an average conversion has the effect of under-estimating or over-estimating a Council's domestic property wealth which is contrary to the purposes for which the duty to give RSG is provided by legislation.

[54] In response Mr Hanna focuses on the fact that in calculating RSG entitlement the Department is engaged in a comparative exercise. He says that at its heart, the statutory formula requires (1) the wealth of a Council being measured; (2) the total wealth of all the Councils in Northern Ireland (including that of the individual Council) to be measured; and (3) the former to be expressed as a percentage of the latter. Because of (3) this is indisputably a comparative exercise. It follows therefore that however the wealth of a Council is to be defined it must, if it is to be expressed as a percentage of the total wealth of all Councils in Northern Ireland, be measured, valued and expressed in the same way, and on the same basis as that of all the other Councils. The basis of valuation must be the same in each case. Otherwise there would be no valid comparison of "like with like".

[55] The focus on the fact that a comparative exercise is involved is important in understanding the Department's view. If the wealth of a Council is to be defined on the basis of the rates struck by that Council this fails to take into account the fact that individual Councils may choose to strike higher or lower rates depending on local political considerations. Thus it is arguable that there might be an incentive for the members of a Council to manipulate its wealth by deliberately striking a lower rate than a comparable Council with equal wealth with the objective of securing a greater share of RSG for its district.

[56] Mr O'Reilly, who is the Permanent Secretary of the Department, sets out the rationale behind the Department's use of a Northern Ireland average conversion factor in paragraph 20 onwards as follows:

> "The purpose of using the conversion factor for RSG purposes is different from the purpose it has in the rate setting process. Instead of using Council specific conversion factors, which focus on maintaining the relativities between the domestic and non-domestic sectors within a **specific Council area**, the DOE's objective is to ensure that the actual relative wealth position of Councils across NI as a whole is reflected correctly. The exercise in this case, unlike that of striking rates, does therefore involve comparison; viz comparing the wealth (domestic and non-domestic) of the 11 District Councils of Northern Ireland relative to each other. The only way that the relative wealth position of Councils can be accurately reflected in the GPRP figure used in the RSG formula is by applying an average NI conversion factor to domestic values. Applying the different Councils specific conversion factors would introduce distortions in the values of the domestic data."

[57] Like Mr Tohill he then goes on to provide some worked examples to support this contention. He concludes by saying:

> "28. … The conclusion, therefore, is that using a NI average growth, or currently NI average conversion factor, to convert domestic value to non-domestic rental values is the only way that the actual domestic relative wealth position of Councils can be maintained.
>
> 29. The Department believes that use of the NI average growth/conversion factor is the only way of achieving the objective of the RSG."

[58] Returning to Mr Hanna's submissions in relation to Schedules 1 and 2 of the Regulations it is argued that the only way in which a capital value penny rate product determined under Schedule 1 to the 2007 Regulations can be conjoined with a NAV penny rate product (determined under Schedule 2 to the 2007 Regulations) to produce a "gross penny rate product" for the purposes of the statutory formula is by using a conversion factor which is the same for every Council.

[59] Adding to the worked example which he relied on he gives the following example. If the aggregate capital value of all the domestic hereditaments in a particular Council (Council A) is the same as that of all the domestic hereditaments in another Council (Council B) the two Councils will have the same domestic wealth (as defined for the purposes of the formula). If the aggregate NAV of all the non-domestic hereditaments is the same in each Council, the two Councils will also have the same non-domestic wealth. If they have the same domestic wealth and the same non-domestic wealth they must necessarily have the same overall wealth and it would be absurd to suggest otherwise. It is common case that the two gross penny rate products cannot simply be conjoined by adding them together, and that some conversion factor must be applied. Mr Hanna argues that the only conversion factor that can be applied which is capable of bringing about the result that they have the same overall wealth is a conversion factor which is the same in every case (i.e. the Northern Ireland average conversion factor). Application of individual, Council specific, conversion factors will inevitably lead to a result that the two Councils have different overall wealth for the purposes of the statutory formula. This is demonstrated by further worked examples.

Evidence in relation to the decision to adopt an average conversion factor/discovery

[60] A striking feature that emerged in the course of these proceedings is the apparent uncertainty and indeed disagreement between Government agencies in relation to the use of average conversion factors and historically the lack of any

indication as to how, when or why the DOE in fact adopted the use of an average factor.

[61] In relation to the former in his second affidavit (dated 1 October 2015) Mr Tohill refers to conversations he had with a Mr Fred Hempton, a senior officer of Land and Property Services ("LPS") (LPS is a section of the DFP) who provide data for the purposes of rate setting for DFP and also to the DOE for RSG purposes. In his affidavit he averred that some officers in LPS had misgivings about how the Department was asking LPS to calculate the GPRP for the purposes of determining RSG. LPS expressly required a service level agreement with the Department which should require it to acknowledge its responsibility for the calculation of GPRP and instruct LPS to undertake the calculation of GPRP on the basis of a Northern Ireland average conversion factor. Further a recognition was sought that LPS held a contrary view to that held by the Department in relation to the appropriateness of using an NI average conversion factor.

[62] This was met by a robust response from Mr McClure on behalf of DFP pointing out that Mr Hempton had retired on 3 September 2015 and that he was "no longer in a position to represent the Department of Finance and Personnel". The affidavit goes on to point out that DFP's role is solely to provide data to the Department for use in the RSG process. The affidavit made it clear that the DFP has no policy view on RSG calculation and sees the RSG as matter that falls entirely within the policy and legislative competence of the DOE.

[63] In the course of the proceedings the Council sought extensive discovery from the Department seeking in particular:

> "All documents containing or evidencing discussions and decisions within the Department about how to calculate gross penny rate product for the purposes of RSG, including any discussions and decisions about whether or not to use an average conversion factor, a district conversion factor or some other conversion factor and
>
> …. All documents evidencing or referring to discussions between the Department and LPS about the calculation of GPRP."

[64] By letter dated 15 January 2016 the Department provided a list of documents which were heavily redacted. This matter was pursued by way of further correspondence and on 17 February 2016 the Department's solicitors sent a further bundle of documents replacing the redacted and incomplete ones which in effect removed most of the previous redactions. Subsequently on 3 March 2016 the Department's solicitors sent additional documents obtained from LPS/DFP.

[65] In the course of the hearing I was asked to draw an adverse inference from the decision to redact the documents. My attention was specifically drawn to some of the material which was redacted and which it was argued was clearly material to the issues in this case. I declined to conduct any "inquiry" into the matter as I was satisfied that all the relevant material was now before the court and the Council was able to make use of the material in support of its arguments.

[66] I propose to refer to some of the material disclosed.

[67] Firstly, it is clear from a thorough examination of the material that at no stage does the Department set out a reasoned basis for its decision to use a Northern Ireland average conversion factor. The genesis of that decision appears in a memo from an economist employed by the DFP Ms Burke dated 12 November 1996.

[68] The memo had been sent to various officials in the DOE. It is headed "**Calculation of Estimated Penny Product**". The text reads:

> "The 1997/98 estimated penny product (EPP) for each district will be calculated by adding factorised domestic NAV to the non-domestic RV at 1995 rental values and applying the relevant percentage (i.e. 100% - minus cost and loss of collection). The factorisation process for calculating the EPP for both district rate and general grant purposes is set out below.
>
> EPP for District Rate ….
>
> **EPP for General Grant**
>
> The main purpose of the resources element of the general grant is to distribute grant to the relatively poor Councils i.e. those Councils whose gross penny product (EPP plus 1p product of de-rated value) per capita falls below a specified amount. It follows, therefore, that if domestic NAVs are factored up by specific district factors, those Councils whose non-domestic rental values have grown relatively faster than others may be unfairly disadvantaged if this pattern has not been reflected in the domestic sector. Although it could be argued that the growth in domestic rental values within Councils is likely to reflect the growth for non-domestic sector, VLA do not have enough evidence to confirm this. Moreover, as the growth factor in some Councils may be skewed by the presence of outliers, for example, electricity

> generators in Larne and Carrick, we (and VLA) feel the most equitable option is to assume equal growth in domestic rental values between Councils. Therefore, for the calculation of EPP for general grant purposes, it is proposed that domestic NAV for all District Councils be factored up the NI average growth factor, i.e. 6.299."

[69] This memo was written in 1996 and so for references to the general grant read current RSG. The VLA was the predecessor of the LPS.

[70] The Council point out that there is actually no evidence on the central issue - "VLA do not have enough evidence to confirm this". Thus the subsequent references to "may be skewed" and "we feel the most equitable option is to assume etc." It appears from the examination of the documents that this approach has simply been adopted throughout the years. By way of example an internal audit review of May 2000 at paragraph 2.6 states:

> "Economics Branch advise that individual growth factors would need to be used for the district rate penny product calculation and average growth factors would need to be used for the general grant penny product calculations. A memo regarding this issue was sent to RCA, VLA a Local Government division dated 12 November 1996.
>
> RCA was not able to locate a copy of this memo on their files but there was a copy on LGD's file. This memo was concerned with providing advice solely in respect of the estimated penny products.
>
> 2.7 During the period 1997/1998 there were 3/4 people in RCA with some knowledge of the penny product calculations. However, during 1998 three of these people left the agency and were replaced by staff who had little or no prior knowledge or expertise in the calculation of the penny products."

[71] The Northern Ireland average conversion factor has been applied since 1997.

[72] There is one interesting qualification to the practice since 1997 and by way of short diversion I will set this out. In the years 1997/98 and 1998/99 General Grant (the predecessor of RSG) was distributed on the basis of calculations using individual, Council specific, conversion factors rather than the Northern Ireland average conversion factor. This was recognised by the Department to have been a mistake and it clawed back overpayments by reducing subsequent payments of

General Grant to the Councils which had been overpaid. Proceedings were then brought by a number of Councils resisting the clawback. However these proceedings were never pursued to court by any of the Councils.

[73] With that exception the General Grant and the RSG have continued to be calculated by use of the average conversion factor without challenge by any Council apart from the one brought in these proceedings.

[74] Whilst it is correct to say there has been no legal challenge by any Council the material produced on discovery makes it clear that there has been significant internal debate at the very least concerning which conversion factor is appropriate.

[75] What emerges from the fully unredacted discovery is that there was a very real and live dispute between LPS (a division of DFP) and the Department in relation to the proper conversion factor which should be applied. LPS is clearly of the view that the use of an average factor is not justified and indeed is a "deviation from the statute". This resulted in an on-going debate between LPS and the DOE in respect of a service agreement between the respective parties. LPS made it clear that it was only prepared to provide data for RSG if the Department expressly relieves it of responsibility for adopting that methodology.

[76] Whilst this issue was on-going a Penny Product Working Group (PPPWG) had been established. A sub-group namely the Estimated Penny Product Working Group (EPPWG) had also been established to deal with the on-going issues arising in relation to how this was to be dealt with.

[77] The following extracts from the discovery make the point clearly. By way of example:

(a) There is a note from Lizanne Kennedy of the finance team dated 19 May 2014 which looks at the issue of the Northern Ireland average conversion factor in the provision of gross penny rate product (CPRP) data which contains the following.

> "**Legislative position …**
>
> The GPRP for RSG purposes is calculated by adding the EPP for non-domestic valuations (based on NAV figures) and the EPP for domestic valuations (based on CV figures). The CV figures being converted into NAV using **the NI average conversion factor**. This has been the practice from December 2006 and has been used in the calculation of grant entitlement of 2007/08 onwards.
>
> Individual Council conversion factors are used for calculating the EPP used by Council to set district rates.

> While individual conversion factors are prescribed by the Rating Policy Division (RPD) under power provided by Article 6(6) of the Rates (Northern Ireland) Order 1977 (copy at Annex 4), there does not appear to be any supporting legislative basis for calculating.
>
> …. Whilst it is very unlikely that the current process of applying an average conversion factor would be legally challenged, one option would be to seek DSO's opinion. This could be in advance of the GWG considering."

(b) In a memo dated 10 October 2014 concerning the service level agreement between LPS and DOE there is an e-mail on behalf of LPS to Lizanne Kennedy which contains the following:

> "As we have laboured repeatedly there is no statutory formula for calculating EPPs and that indeed a sub-group has just considered the EPP process for next year and made recommendations that would go to PPWG. That provides an audit trail not only for Councils in the event of a challenge to any district rate in the High Court but also protects LPS and the Minister. The formula for resources would be different and in our view it is a matter for you to set out clearly what that should be. It provides an audit trail and we will calculate to your requirements subject to statutory matters …
>
> I have read your comments about the terms GPRP. As far as LPS is concerned there is no statutory formula or methodology for these terms and to ensure that there is no ambiguity we believe that the agreement should clearly state what and how things will be undertaken."

(c) On 5 June 2015 Fred Hempton on behalf of LPS writes to Jeff Glass of the Department in the following terms:

> "This scrutiny of the statute has indicated to LPS that since at least 2011 the penny product calculation DOE has asked LPS to undertake in respect of the Rate Support Grant is not in keeping with the statute and therefore wrong in law. For Rate Support Grant purposes LPS has been asked to provide an **estimated penny product for the incoming year for each District Council.** LPS has always argued that there is no statutory formula for any estimated penny product calculations and as the body has statutory responsibility for

the RSG calculations DOE should set out the calculation basis. The draft SLA is also clear on this and in our view would have brought clarity to the matter at least for LPS.

However when we examined the Local Government (Rates Support Grant) Regulations (Northern Ireland) 2011 (No. 375) it is clear that those Regulations also set out the formula for determining the penny product element of the rates support grant calculations for the incoming year. In Regulation 2 'gross penny rate product' is defined as 'the income that may be raised from one penny of district rates on rateable and de-rated properties, as determined by the (DOE) on the basis of data provided by (DFP). We then turn to Regulation 4 of those same Regulations the provisions of which say that DOE shall use data in the formula based on the latest information available to DOE regarding the immediately preceding year. This is not the penny product calculation which is undertaken for or used by DOE in its allocation of rates support grant to District Councils and is why all along LPS has asked DOE to clarify the formula. The formula included in the 2011 Regulations does I believe recognise the imperfection of undertaking estimated calculations and how they might stand up to a challenge and also that it is not possible to legislate for the estimated penny product."

(d) On 4 September 2015 Mr Hempton again writes to Mr Glass in relation to the proposed service level agreement in the following terms:

> "As I see it the SLA simply clarifies the calculation basis of data provided by LPS for use by DOE and that calculation is according to prescription under DOE legislation. If you wish to deviate from a statute that is not a problem and the SLA provides for this. You simply instruct LPS and set out the methodology for calculation of data. Ultimately the statute is vested in DOE and to safeguard LPS from any further misunderstandings, I understand a service level agreement is a prerequisite."

(e) On 2 October 2015 Mr O'Hagan on behalf of LPS writes again to Lizanne Kennedy in the following terms:

> "We will only be providing data in line with the legislation. You have mentioned a date of October 2015 and also average conversion factors in this paragraph, neither of which are in line with the legislation. As advised previously we will only

> be carrying out calculations in line with legislation. We will also need to (sic) DOE to define the terms 'gross penny rate product' as it is referenced in DOE legislation and we do not have a full understanding of (next part unclear). LPS has been at pains to alert DOE to this (see Fred Hempton's note of 5 June 2015) for the last number of months and have requested a meeting early in the summer in order to discuss. If/when legislation is amended, we can look at this, however assume there will be no change before the end of this year."

Again referring to the on-going debate regarding the SLA on 2 October 2015 Mr O'Hagan again writes to Lizanne Kennedy and the following is included:

> "Finally this brings me to the paragraph entitled 'Deviation from the Statute'. This allows for LGPD to request data that is inconsistent with our interpretation of the statute governing the grants, however in order to use this we will need the SLA to be signed and clear written instructions from LGPD detailing what data is required."

[78] Thus while Mr McClure on behalf of DFP has averred that it has no "policy view" on the RSG calculation and sees the RSG as a matter that falls entirely within the policy competence of DOE it is abundantly clear that LPS who provide the necessary calculations has a different view of this matter. Of course this is not determinative of the issue.

Conclusion

[79] I have come to the conclusion that the legislation does not require the use of either a specific conversion factor or an average conversion factor. It would be a very simple matter for the Regulations to provide for the basis upon which this calculation should be made. It has done so in relation to the appropriate conversion factor for the striking of rates. Applying the principles of statutory interpretation I accept that the use of a conversion factor is required to properly interpret the legislation. However I am not persuaded that I can take the next step and come to a definitive view that the statutory formula requires the use of any of the conversion factors argued for by the parties in this case.

[80] In those circumstances the department is obliged to exercise its judgment or discretion as to how the formula should be applied. In my view the approach it has adopted is a rational one and not one which could be described as Wednesbury unreasonable. It has adopted a particular approach for over 20 years which has resulted in a workable method of distributing RSG to the Councils during that period. The underlying principle it seems to me relates to the argument that the Department is engaged in a comparative exercise between Councils and this is best

achieved by the use of an average rather than an individual conversion factor. I have referred in this judgment to the various worked examples prepared by each of the parties and I do not mean any disservice to their industry by not setting them out in detail in this judgment. Rather I have referred to the principles the examples support. There was no fundamental flaw that I could identify in respect of the examples and ultimately what is required is a policy decision as to how best to achieve the objectives of the statutory scheme. Thus whilst I accept that the approach of the Department is a rational one I also accept that a case can be made that a specific conversion factor is appropriate.

[81] Therefore I am not prepared to declare the use of a Northern Ireland average conversion factor unlawful.

[82] However I am of the view that this matter should be dealt with urgently by the Department of the Environment by way of an amended regulation which makes it clear the basis upon which the calculation is to be made. Such regulation would obviously require the necessary consultation with the appropriate parties.

[83] I accept that on an analysis of the documentation provided the Department has not carried out the type of exercise it has engaged in in defending these proceedings in reaching the conclusion that the Northern Ireland average conversion factor is the proper method to be used in calculating the RSG allocation. Having adopted the use of the Northern Ireland average conversion factor back in 1996 it has simply continued to apply it notwithstanding issues that have been raised, in particular by LPS, as to whether it is the appropriate method.

[84] However it is clear that in responding to these proceedings significant effort and thought has been expended in demonstrating why the use of the average conversion factor is indeed an appropriate method consistent with the objectives of the statute providing for the payment of RSG.

[85] I have considerable sympathy for Mr Oldham's submission that what the court has been presented with is a "post hoc" explanation of why the DOE believes that the average factor should be used.

[86] Having regard to the fact that I have come to the conclusion that there is a rational basis for using the average Northern Ireland conversion factor and that this is has been applied for 20 years I have concluded that it would be wrong to declare its use unlawful.

Costs

[87] At the commencement of the proceedings Mr Hanna properly conceded that this was an appropriate case for leave to be granted. However for the reasons set out I have refused to grant the relief sought.

[88] In relation to costs I have come to the conclusion that the appropriate order in this case is that each party should bear its own costs.

[89] In coming to this conclusion I bear in mind that the regulations are the responsibility of the Department and as I have found they do not provide the appropriate clarity which would have avoided this dispute.

[90] Further it seems to me that, as I have explained, there is merit in the applicant's contention that it was these proceedings that forced the respondent into providing an evidential basis for the method they used in the past.

[91] I also take the view that it was in the public interest for these proceedings to be brought to bring some clarity to what clearly was a live issue between the LPS and the Department of the Environment and is of benefit to the other ten District Councils in Northern Ireland who were notice parties to the proceedings.