Cabinet

Date: 14 January 2019

Subject: Draft Business Plan 2019-23

Lead officer: Caroline Holland – Director of Corporate Services

Lead member: Councillor Mark Allison – Deputy Leader and Cabinet Member for Finance

Recommendations:

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1. That Cabinet notes the financial information arising from the Provisional Settlement 2019/20 and that the financial implications will be incorporated into the draft MTFS 2019-23 and draft capital programme 2019-23.
2. That Cabinet notes the latest update of the draft MTFS for 2019 – 23

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1. **PURPOSE OF REPORT AND EXECUTIVE SUMMARY**

1.1 This report provides an update to Cabinet on the Business Planning process for 2019-23 and in particular on the current position relating to the revenue budget for 2019/20, and the draft MTFS 2019-23.

1.2 It also sets out the latest information and analysis of the Local Government Finance Settlement 2019/20 which was published on 13 December 2018 and summarises the implications for Merton's budget and MTFS.

2. DETAILS

2.1 **Introduction**

2.1.1 The report provides a general update on all the latest information relating to the Business Planning process for 2019-23, including the Provisional Local Government Settlement 2019/20.

2.1.2 A review of assumptions in the MTFS was undertaken and reported to Cabinet on 10 December 2010. On 31 December 2018 a savings proposals information pack of all details previously presented to Cabinet at its meetings was sent to all Members. This can be brought to all Scrutiny and Cabinet meetings from 9 January 2019 onwards and to Budget Council. This is the same procedure as last year which is more cost effective and more manageable for councillors since it will ensure that only one version of those documents is available so referring to page numbers at meetings will be easier. It will considerably reduce printing costs and reduce the amount of printing that needs to take place immediately prior to Budget Council.

The pack includes:

- Savings proposals
- Equality impact assessment for proposals where appropriate
- Service plans (these will also be printed in A3 to lay round at scrutiny meetings)
- Budget Summaries for each department

2.1.3 The total draft amendments to previously agreed savings, and new savings proposals by Cabinet previously and the remaining gap on the MTFS as reported to Cabinet on 10 December 2018 are summarised in the following table:-

	2019/20 £'000	**2020/21 £'000**	**2021/22 £'000**	**2022/23 £'000**
Amendment to Savings previously agreed	(4,258)	(1,812)	(115)	0
New Savings proposals	(2,577)	(5,594)	(1,379)	(105)
Net Savings	(6,835)	(7,406)	(1,494)	(105)
Cumulative Net Savings	(6,835)	(14,241)	(15,735)	(15,840)
Gap remaining (cumulative)	0	3,496	7,352	8,779

2.2 LOCAL GOVERNMENT FINANCE SETTLEMENT 2019/20

2.2.1 Details of the provisional Local Government Settlement were published on 13 December 2018.

2.2.2 This section sets out the main details included in the provisional Settlement and assesses the implications for Merton's finances as set out in the Medium Term Financial Strategy (MTFS).

2.2.3 The provisional Settlement outlined provisional core funding allocations (Settlement Funding Assessment (SFA) for local authorities for 2019-20.

2.2.4 The Settlement Funding Assessment is the total of Revenue Support Grant (RSG) and Baseline Funding (BF) from Business Rates.

	2016/17 Final	2017/18 Final	2018/19 Final	2019/20 Provisional
Merton (£m)	55.5	48.5	44.7	40.5
Annual % Change	-	-12.6%	-7.8%	-9.4%
Cumulative % change	-	-12.6%	-19.5%	-27.0%
England (£m)	18,601.5	16,632.4	15,574.2	14,559.6
Annual % Change	-	-10.6%	-6.5%	-6.5%
Cumulative % change	-	-10.6%	-16.3%	-21.7%
London Boroughs (£m)	3,398.5	3,078.3	2,901.2	2,713.5
Annual % Change	-	-9.4%	-5.8%	-6.5 %
Cumulative % change	-	-9.4%	-14.6%	-20.2%

2.2.5 Core Spending Power

There have been a number of changes to Core Spending Power in this Settlement. Core Spending Power includes two new funding elements in 2019-20 compared with 2018-19. These are the adult social care “Winter pressures grant” (totalling £240 million nationally in both 2018-19 and 2019-20) and the new “Social care support grant” (totalling £410 million nationally in 2019-20).

Core Spending Power in 2019-20 is therefore made up of:

- Settlement Funding Assessment
- Estimated Council Tax Requirement excluding Parish Precepts
- Compensation for under-indexing the business rates multiplier
- Additional Council Tax revenue from referendum principle for social care
- Potential additional Council Tax revenue from referendum principle for all districts.
- Improved Better Care Fund
- New Homes Bonus and New Homes Bonus Returned Funding;
- Rural Services Delivery Grant
- Adult Social Care Support grant
- Winter Pressures Grant
- Social Care Support Grant

At the England level across the four years there will be a cumulative increase in spending power of £2.7 billion (6% in cash terms) from £43.7 billion to £46.4 billion. The equivalent figures for London boroughs are an increase of £238.4(3.6%) from £6.7 billion to £6.9 billion.

However, as Core Spending Power includes a number of assumptions, this is unlikely to be an accurate reflection of the actual resources available to local authorities. In particular it assumes:-

- All authorities that are eligible raise the social care precept to its maximum in 2019-20
- All authorities increase overall council tax by the maximum amount (3% in 2019-20)
- Tax base increases at the same average rate for each authority as between 2014-15 and 2018-19
- New Homes Bonus allocations are based on the share of NHB to date

In England the level of assumed spending power will increase by £1.3 billion (2.8%) in 2019-20 from £45.1 billion to £46.4 billion. In London boroughs the assumed increase is £157 million (2.4%) in 2019/20 from £6.7 billion to £6.9 billion.

A summary of Merton’s assumed Core Spending Power from 2016/17 to 2019/20 is included in the following table:-

Detailed Breakdown of Core Spending Power – Merton

	Final	Final	Final	Provisional	Annual Change (18-19 to 19-20)	Cumulative Change (16-17 to 19-20)
	2016-17	2017-18	2018/19	2019/20		
	£m	£m	£m	£m	%	%
Council Tax	78.920	82.563	87.009	93.320	7%	18%
Settlement Funding Assessment*	55.500	48.545	44.662	40.460	-9%	-27%
Compensation for under-indexing the business rates multiplier	0.476	0.504	0.793	1.153	45%	142%
Improved Better Care Fund	0.000	2.746	3.523	4.114	17%	-
New Homes Bonus	4.658	4.068	2.371	2.108	-11%	-55%
New Homes Bonus – returned funding	0.076	0.080	0.000	0.000	-	-100%
Transition Grant	0.567	0.557	0.000	0.000	-	-100%
Adult Social Care Support Grant	0.000	0.751	0.467	0.000	-100%	-
Winter Pressures Grant	0.000	0.000	0.748	0.748	-	-
Social Care Support Grant	0.000	0.000	0.000	1.278	-	-
Core Spending Power	**140.197**	**139.815**	**139.574**	**143.182**	**3%**	**2%**

* SFA figures do not reflect the London Business Rates Pilot Pool

2.2.6 Council tax referendum principles for principal local authorities

In terms of controlling the level of council tax increases that local authorities can set, without the need for a local referendum, the Government has decided to maintain the core principles that it used in 2018-19. However, in the Provisional Settlement the Government also states that "in recognition of substantial increases in pressures, we are providing additional flexibility for police and crime commissioners. In doing so the Government continues to ensure that council tax payers can veto excessive increases via a local referendum"

The 2019/20 Council Tax referendum principles are:-

- a core principle of up to 3%. This would apply to shire county councils, unitary authorities, London borough councils, the Common Council of the City of London, the Council of the Isles of Scilly, the general precept of the Greater London Authority, and fire and rescue authorities;
- a continuation of the Adult Social Care precept, with an additional 2% flexibility available for shire county councils, unitary authorities, London borough councils, the Common Council of the City of London and the Council of the Isles of Scilly. This is subject to total increases for the

Adult Social Care precept not exceeding 6% between 2017-18 and 2019-20, and increases being no more than 2% in 2019-20;

- shire district councils in two-tier areas will be allowed increases of up to 3%, or up to and including £5, whichever is higher;
- police and crime commissioners (PCCs) will be allowed increases of up to £24 in 2019-20 (including the Greater London Authority charge for the Metropolitan Police, and the PCC component of the Greater Manchester Combined Authority precept). This investment in the police system, combined with extra grant, will help forces meet increased demand and financial pressures, as they work towards continued efficiency savings in 2019-20.

If the 2% increase in 2019/20 proposed in the MTFS is agreed, Merton will have applied the Adult Social Care Precept in the following way:-

	2017/18 %	2018/19 %	2019/20 %	Total %
Council Tax increase - ASC	3	1	2	6

The financial projections in this report are based on the following levels of council tax increase:-

	2019/20 %	2020/21 %	2021/22 %	2022/23 %
Council Tax increase - General	2.99*	2	2	2
Council Tax increase - ASC	2	0	0	0
Total	4.99	2	2	2

* The Government's assumption in the calculation of core spending power in the Provisional Local Government Finance Settlement is that local authorities increase their Band D council tax in line with the 3% referendum limit

2.2.7 Business Rates Retention

Consultation Paper

Alongside the Provisional Local Government Finance Settlement, the Government also published a consultation paper titled "Business Rates Retention Reform – Sharing Risk and Reward, managing volatility and setting up the reformed system".

The reform of the business rates retention system will sit alongside wider changes to the local government finance system which the Government aims to introduce in 2020; notably the review of relative needs and resources, which will review the relative needs and resources of all local authorities, and the upcoming Spending Review, which will set the overall level funding for local government.

The scope of the consultation will be the reform of aspects of the business rates retention system in England, which the Government aims to implement in 2020. How local authorities transition from the current system to a reformed system and how reforms are operationalised are not being consulted on at this point; the Government expects to consult on these in 2019.

The upcoming Spending Review will determine the spending envelope for local government and therefore the quantum of funding available to local authorities is outside of the scope of the consultation.

The consultation will last for 10 weeks from 13 December 2018 to 21 February 2019. A summary of the key points in the consultation paper is included in Appendix 2.

<u>2019-20 Business Rates Retention Pilots</u>
In 2017-18 and 2018-19, a number of local authorities piloted 100% Business Rates Retention. In July 2018, the Government confirmed that authorities in Greater Manchester, Liverpool City Region, Cornwall, the West of England and West Midlands Combined Authority areas would continue to retain 100% of business rates in 2019-20.

In July 2018, the Government launched a competitive bidding round, inviting pools of authorities to bid to pilot 75% business rates retention in 2019-20. The Government has selected fifteen areas to pilot increased business rates retention as part of the move towards wider reform of the system from 2020 onwards.

Following separate negotiations with London authorities, it has also been agreed that London will be piloting 75% business rates retention in 2019-20. The arrangements for these pilot authorities have no impact on the funding available for other areas.

In all the pilot areas, authorities have agreed to forego funding streams in return for higher shares of business rates. In London, the boroughs, the City of London Corporation, and the Greater London Authority (GLA) will forego RSG. GLA will also forego the GLA Transport grant from the Department for Transport (DfT).

The 75% and 100% business rates retention pilots are cost neutral at the point of delivery, although there is a cost to the exchequer arising from the additional growth foregone.

As reported to Cabinet in December 2018, final projections for Business Rates retention in 2019/20 under the revised pool will be based on London Boroughs NNDR1 returns for 2019/20 which are due to be returned to central government by 31 January 2019. Until then the MTFS will continue to be based on the “no worse off” assumption which is calculated under the pre-pilot methodology. Updated figures based on all London boroughs completed NNDR1 returns will be included in the report to Cabinet on 18 February 2019.

<u>Business Rate Levy Account Surplus</u>
As a result of increased growth in business rates income the government has announced that it is intending to distribute £180 million of the Levy Account

surplus to local authorities on the basis of need. Merton's share of this one-off payment in 2019/20 is £0.543m.

2.2.8 Special and specific grants

The distribution of a number of grants was published alongside the Provisional Settlement. Within core spending power these include:-

- New Homes Bonus
- Improved Better Care Fund
- Rural Services Delivery Grant (not applicable to London)
- Compensation for under-indexing the business rates multiplier
- Winter Pressures Grant
- Social Care Support Grant

Outside of the Provisional Settlement, allocations of a number of other grants have also been published including:-

- Lead Local Flood Authorities funding
- Flexible Homelessness Support Grant
- Homelessness Reduction Act new burdens funding

The Government has not yet published the Public Health Grant allocations for 2019-20.

The provisional schools funding settlement for 2019/20 has been published by the Department for Education.

New Homes Bonus

Despite previously indicating that it might, the Government has decided not to make any additional change to the baseline, below which the Bonus will not be paid, and it will remain at 0.4% for the 2019-20 allocations. It retains the option of making adjustments to the baseline in future years.

Provisional NHB allocations for 2019-20 have been published. London's share of the national total has stayed broadly the same at 21%, receiving £190 million of the £918 million national total. Overall NHB funding has fallen by £30 million (3.1%). London boroughs' allocations have fallen by £10.6 million (5.3%). Funding for New Homes Bonus will be made up from £900 million provided from Revenue Support Grant, and an expected £20 million from departmental budgets.

Merton's provisional allocation for 2019/20 is £2.108m which is £0.080m more than provided for in the MTFS.

Improved Better Care Fund

There is no change to the figures announced in last year's Settlement. In 2019-20, the Government is providing £1.837 billion across England. London boroughs will receive £299 million in 2019-20. As confirmed in the allocation

methodology last year, the allocation methodology takes into account the ability to raise Social Care Precept and therefore benefits those councils with lower capacity to raise council tax.
Merton's allocation is:-

Improved Better Care Fund	**2019-20 £m**
Merton	4.114

Compensation for under-indexing the business rates multiplier
At Autumn Budget 2017, the government announced plans to bring forward a move from RPI to CPI indexation of the business rates multiplier. This change took effect from 2018/19 instead of 2020/21. In the 2018/19 Settlement £275 million of section 31 grant was made to local authorities in compensation for lost income of which £48.7 million was paid to London boroughs. This rises to £400 million in 2019/20 (£70.9 million in London). This compensation grant is included within Core Spending Power.

Merton's allocation for this is:-

Compensation for under-indexing the business rates multiplier	**2019-20 £m**
Merton	1.153

Lead Local Flood Authority Grant
The Government has also published Lead Local Flood Authority Grant allocations for 2019-20 (for the grant that sits outside the funding within SFA). London Boroughs will receive £0.87 million (from the national total of £4.3 million).

Merton's allocation for this is:-

Lead Local Flood Authority Grant	2019-20 £m
Merton	0.179

Flexible Homelessness Support Grant
The Government has also published Flexible Homelessness Support Grant allocations for 2019-20. London boroughs will receive £107.7 million in 2019-20 – this is 54% of the national total of £200 million.

Merton's allocation for this is:-

Flexible Homelessness Support Grant	2019-20 £m
Merton	0.716

Homelessness Reduction Act new burdens funding

Homelessness Reduction Act new burdens funding was published in October 2017. London boroughs will receive £9.4m(38%) of the England total of £24.8m in 2019-20.

Homelessness Reduction Act new burdens funding	2019-20 £m
Merton	0.136

Winter Pressures Grant

Additional funding of £240 million was allocated in both 2018-19 and 2019-20 to assist authorities with winter pressures. This has been distributed using the adult social care relative needs formula and London boroughs are expected to receive £37.2 million (15.5%) of the England total in 2019-20.

Merton's allocation is:-

Winter Pressures	2018-19 £m	2019-20 £m
Merton	0.748	0.748

Social Care Support Grant

As announced in the Budget 2018, an additional £410m is provided in 2019-20 for adults and children's social care. Merton's estimated share of this is £1.278m. The Government is consulting on the method of distribution and is proposing to use the adult social care relative needs formula only. This would mean London boroughs receiving £63.5 million (15.5% of the total). As some of this funding can be spent on children's social care, London Councils will encourage the Government to use the children's social care relative needs formula to determine at least part of the distribution as London boroughs receive 25% of the national total of the children's social care relative needs formula.

Merton's allocation is:-

Social Care Support Grant	2019-20 £m
Merton	1.278

Fair Funding Review – Technical Consultation paper
Alongside the Provisional Local Government Finance Settlement, the Government also published a technical consultation paper "Review of local authorities' relative needs and resources - Technical consultation on the assessment of local authorities' relative needs, relative resources and transitional arrangements".

This consultation seeks views on the approach to measuring the relative needs and resources of local authorities, which will determine new baseline funding allocations for local authorities in England in 2020-21. The consultation will last for 10 weeks from 13 December 2018 to 21 February 2019. A summary of the key points in the consultation paper is included in Appendix 3.

Provisional Settlement Consultation Response
The government is consulting on the provisional settlement figures with a four week deadline of 10 January 2019.

2.2.9 **School Funding Announcement 2019/20**

The School Revenue Funding Settlement: 2018 to 2019 was published on 17 December 2018. The distribution of the DSG to local authorities is set out in four blocks for each authority: a schools block, a high needs block, an early years block, and the new central school services block. The main allocations for Merton announced on 17 December 2018 are:-

Dedicated schools grant: 2019-20 allocations local authority summary	**2019-20 DSG allocations, prior to recoupment and deductions for direct funding of high needs places by ESFA**				
	2019-20 schools block (£million)	**2019-20 central school services block allocation (£million)**	**2019-20 provisional high needs block allocation (£million)**	**2019-20 early years block (£million)**	**2019-20 total DSG allocation (£million)**
Merton	**122.978**	**1.041**	**33.319**	**15.571**	**172.909**

Dedicated schools grant: 2019-20 allocations local authority summary	**2019-20 DSG allocations, after deductions for academies recoupment and direct funding of high needs places by ESFA**				
	2019-20 schools block (£million)	**2019-20 central school services block allocation (£million)**	**2019-20 high needs block allocation (£million)**	**2019-20 early years block (£million)**	**2019-20 total DSG allocation (£million)**
Merton	**122.978**	**1.041**	**33.033**	**15.571**	**172.623**

There will be a more detailed update on Schools funding in the February Cabinet report when further details are known.

3. Public Health Grant 2019/20

3.1 The Government announced allocations of the local government public health grant for 2019/20 on 20 December 2018. The allocation is unchanged from the provisional allocation announced in December 2017.

3.2 The public health grant is ring-fenced for use on public health functions exclusively for all ages.

3.3 Merton's allocation for 2019/20 is:-

	2019/20 £000
Merton – Public Health Grant	10,175

4.. **GLA PRECEPT**

4.1 On 20 December 2018 the Mayor of London announced his proposed council tax precept for 2019-20Tand consultation budget for 2019/20, subject to consultation. The proposed (Band D) precept for the 32 London boroughs is £320.51 – a £26.28 or 8.9% increase compared to 2018/19. Of this increase £24 will be applied for policing and the balance to fund the London Fire Brigade. The consultation period lasts until 14 January 2019.

4.2 The GLA is using the following timetable to produce its budget and agree its precept on London boroughs

20 December 2018
Following the publication of the provisional Local Government, Fire and Police Settlements, issue the Mayor's Consultation Budget, including the Capital Strategy and borrowing limits. Statutory scrutiny of Mayor's budget proposals starts.

24 January 2019
Assembly to consider Draft Consolidated Budget.

25 February 2019
Assembly to consider Final Draft Consolidated Budget.

28 February 2019
Statutory deadline by which the GLA precept must be approved and the Mayor's statutory Capital Spending Plan is published.

6. DRAFT CAPITAL PROGRAMME

6.1 Both the draft Capital Strategy 2019-23 and Draft Treasury Management Strategy 2019/20 were reported to Cabinet in December 2018. Updated versions of both strategies will be included in the Business Plan report to Cabinet in February 2019.

7. GENERAL FUND BALANCES AND RESERVES

7.1 The General Fund balance can be seen as an authority's working balance. In considering the budget plans for the medium term, it is also necessary to give some attention to the level of this working balance. In coming to this decision a number of issues should be considered.

These include:

(a) the retention of working balances to cushion cash flow variations and to avoid increased borrowing costs;

(b) the retention of sums to provide against inflation and pay awards being in excess of the assumptions made within the budget;

(c) the retention of sums to provide for contingent liabilities; or

(d) to meet unforeseen events

7.2 In taking a decision on the level of balances, it is important to take into consideration current and future budget pressures and recognise that in order to set a balanced budget over the next four years there is a need for significant net reductions in the budget which inevitably will mean that there is very little room for manoeuvre in determining the level of balances.

7.3 The recent National Audit Office report on financial sustainability in local authorities published following the crisis at Northamptonshire County Council indicates that there is a heightened risk of more councils over the next four years falling into special financial measures as a result of not reconciling the pressure on budgets. The establishment and planned use of a suitable level of reserves will be a key part of financial resilience going forward.

7.4 The movement and planned use of reserves, both revenue and capital, over the MTFS period is currently being reviewed and there will be a full update to Cabinet in February.

8. SUMMARY

8.1 Following the changes discussed in this report arising from the Provisional Local Government Finance Settlement, the gap in the MTFS (Appendix 1) has changed to the following:-

	2019/20 £'000	2020/21 £'000	2021/22 £'000	2022/23 £'000
Gap remaining (cumulative)	0	2,873	7,352	8,779

9. **CONSULTATION UNDERTAKEN OR PROPOSED**

9.1 There will be extensive consultation as the business plan process develops. This will include the Overview and Scrutiny panels and Commission, the Financial Monitoring Task Group, business ratepayers and all other relevant parties. The consultation meeting with Business Ratepayers is arranged for 13 February 2019.

9.2 Feedback on scrutiny of the Business Plan proposals will be provided by the Overview and Scrutiny Commission on 23 January 2019.

10. **TIMETABLE**

10.1 The business planning timetable for 2019/20 has been reported to and agreed by Cabinet previously.

11. **FINANCIAL, RESOURCE AND PROPERTY IMPLICATIONS**

11.1 All relevant implications have been addressed in the report.

12. **LEGAL AND STATUTORY IMPLICATIONS**

12.1 All relevant implications have been addressed in the report.

13. **HUMAN RIGHTS, EQUALITIES AND COMMUNITY COHESION IMPLICATIONS**

13.1 Not applicable

14. **CRIME AND DISORDER IMPLICATIONS**

14.1 Not applicable

15. **RISK MANAGEMENT AND HEALTH AND SAFETY IMPLICATIONS**

15.1 Not applicable

APPENDICES – THE FOLLOWING DOCUMENTS ARE TO BE PUBLISHED WITH THIS REPORT AND FORM PART OF THE REPORT

Appendix 1	Medium Term Financial Strategy - Update
Appendix 2	Business Rates Retention Reform – Summary of key points in the Consultation Paper
Appendix 3	Fair Funding Review – Summary of key points in the Technical Consultation Paper

BACKGROUND PAPERS

Budget files held in the Corporate Services department.

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DRAFT MTFS 2019-23:				
	2019/20 £000	**2020/21 £000**	**2021/22 £000**	**2022/23 £000**
Departmental Base Budget 2018/19	**149,808**	**149,808**	**149,808**	**149,808**
Inflation (Pay, Prices)	4,244	7,094	9,945	12,796
Autoenrolment/Nat. ins changes	0	0	0	0
FYE – Previous Years Savings	(4,464)	(6,070)	(6,185)	(6,185)
FYE – Previous Years Growth	(2,506)	(2,006)	(2,006)	(2,006)
Amendments to previously agreed savings/growth	206	0	0	0
Change in Net Appropriations to/(from) Reserves	766	909	1,065	1,002
Taxi card/Concessionary Fares	450	900	1,350	1,800
Adult Social Care - Additional Spend	1,054	0	0	0
Growth	0	0	0	0
Other	2,479	4,566	4,846	4,922
Re-Priced Departmental Budget	**155,932**	**159,097**	**162,718**	**166,032**
Treasury/Capital financing	9,806	10,873	12,294	12,324
Pensions	3,552	3,635	3,718	3,801
Other Corporate items	(20,676)	(20,601)	(20,549)	(20,125)
Levies	607	607	607	607
Sub-total: Corporate provisions	**(6,711)**	**(5,486)**	**(3,930)**	**(3,393)**
Sub-total: Repriced Departmental Budget + Corporate Provisions	**149,221**	**153,611**	**158,788**	**162,639**
Savings/Income Proposals 2018/19	(2,577)	(8,171)	(9,550)	(9,655)
Sub-total	**146,644**	**145,440**	**149,238**	**152,984**
Appropriation to/from departmental reserves	(2,017)	(2,160)	(2,316)	(2,253)
Appropriation to/from Balancing the Budget Reserve	(2,597)	(3,427)	0	0
BUDGET REQUIREMENT	**142,030**	**139,853**	**146,922**	**150,731**
Funded by:				
Revenue Support Grant	(5,076)	0	0	0
Business Rates (inc. Section 31 grant)	(35,903)	(37,726)	(38,286)	(38,501)
Adult Social Care - Improved Better Care Fund	(1,054)	0	0	0
PFI Grant	(4,797)	(4,797)	(4,797)	(4,797)
New Homes Bonus	(2,108)	(1,304)	(1,008)	(800)
Council Tax inc. WPCC	(92,350)	(94,629)	(96,955)	(99,330)
Collection Fund – (Surplus)/Deficit	(742)	0	0	0
TOTAL FUNDING	**(142,030)**	**(138,456)**	**(141,046)**	**(143,428)**
GAP including Use of Reserves (Cumulative)	**0**	**1,397**	**5,876**	**7,303**

Potential Unfunded ASC commitments due to Loss of Better Care Funding	0	3,218	3,218	3,218
GAP assuming no new ASC Government Grant (Cumulative)	**0**	**4,615**	**9,094**	**10,521**
Possible Offset if 2019/20 ASC CT hypothecation can be used to replace Better Care Funding	0	(1,742)	(1,742)	(1,742)
GAP assuming no new ASC Government Grant but 2019/20 CT hypothecation can be used(Cumulative)	**0**	**2,873**	**7,352**	**8,779**

Business Rates Retention Reform - Sharing risk and reward, managing volatility and setting up the reformed system

Consultation – December 2018

The consultation seeks views on options for the reform of elements of the business rates retention system in England from 2020-21 onwards. It will last for 10 weeks from 13 December 2018 to 21 February 2019.

The Government is currently in the process of reviewing the components of the business rates retention system, both individually and in aggregate. This reform of the system is consistent with the Government's aim to introduce 75% business rate retention in 2020, in a way that is fiscally neutral.

The Government's ambition for business rates retention remains two-fold:

- to give local government greater control over the money it raises, recognising that local authorities are best placed to decide local priorities; and
- to incentivise local authorities to support local economic growth.

The Government acknowledges that:-
- the business rates retention system is complex and has not always been flexible.
- that there is a level of disproportionate volatility in the current system and is committed to reducing the impact on local authority income of factors outside of an authority's control.

It is the Government's aim to introduce reform of the business rates retention system in 2020-21.

The Government's proposals in the consultation paper are in three main areas:-

1. proposals to update the balance of risk and reward to better reflect the wider context for local authorities in 2020.
2. proposals designed to mitigate volatility in income and simplify the system
3. proposals about how to set up the new business rates retention system in 2020

The balance of risk and reward
The Government believes that if local authorities are going to keep a share of the benefits of growth through the business rates retention system then they should also take on a share of the risk.

This section of the consultation covers:-

- how the system should be reset on a regular basis;
- the tier split between district and county councils;
- proposals to reform the levy; and
- the level of the safety net.

How the system should be reset on a regular basis
At a reset, Business Rates Baselines are re-calculated for the forthcoming reset period for all local authorities. During this period, growth in the authority's locally raised business rates (and so income) can be retained above its Baseline Funding Level (currently at 50%, which is the local share under 50% business rates retention).

The Government intends to carry out a full reset of Business Rates Baselines in 2020-21.
This will allow:-

- full implementation of reforms to the business rates retention system;
- the findings of the review of relative needs and resources; and
- the Spending Review.

The approach to the reset in 2020-21 and for the future resets after this point need not be the same; the way the system is set up to facilitate optimal implementation will not set a precedent for resetting Business Rates Baselines in the future.

This consultation seeks views on resets after 2020-21 and not what happens at the transition to the reformed system, which will be consulted on later.

Types of Reset

Partial Reset	Under a partial reset: Business Rates Baselines and Baseline Funding Levels are held constant for a set number of years and at a reset a percentage of the growth achieved over the previous period is redistributed, with the remaining percentage retained by individual local authorities. This percentage is yet to be determined and the Government welcomes views on this. It is not expected that authorities experiencing decline in their rates would retain this entering a new reset period. The advantage of this type of reset is that it would help to smooth out 'cliff-edges' and could offer improved stability and certainty for authorities, whilst still allowing them to benefit from local growth.
Full Reset	Under a full reset: no growth is retained into the forthcoming reset period. This creates 'cliff-edges' at the end of each reset period and creates a perverse incentive for authorities to control when growth comes 'on stream'. The Government has ruled out full resets at the end of every reset period.
Phased Reset	Under a phased reset: authorities retain each year's growth (or loss) in rates for a set number of years and thereafter that growth (or loss) is redistributed. Under this option it would not matter when growth came 'on stream' as all growth would count equally, regardless of timing.

This consultation seeks views on:

a. The most desirable type of reset; and
b. The time period that a reset should cover

Time period between resets
The Government has previously proposed a 5-year time period between resets which it says received support as it "struck a good balance between incentivising growth and providing for redistribution to meet need."

The Government has announced that business rates revaluations will happen every three years. Aligning resets and revaluations could have some benefit because it reduces, marginally, the scale of the disruption to tariffs and top-ups in any year.

The government ask respondents to consider whether the frequency of resets aligned with the frequency of revaluations are desirable (i.e. multiples of three years).

The Government is continuing to work to understand how reset options interact with future pending review periods and the output of the review of relative needs and resources.

The Safety Net
The safety net is the mechanism that ensures that the risk of experiencing a decline in business rates income is proportionate and sustainable at an individual local authority level when shocks to the system occur, such as the closure of a major ratepayer. It ensures that no authority falls below a minimum level of their assessed need, currently expressed as a percentage of Baseline Funding Level.

It is proposed to continue with the current approach to the safety net: that it should continue to function as a 'simple' safety net whereby local authorities bear some of the risk but will receive help when business rates income reduces below a certain level. It is the level at which the safety net should be set that remains to be decided. The likelihood that an authority will require a safety net payment is very much a function of other elements in the system (e.g. appeals and other valuation change).

Within the current system the safety net is funded through two sources: the levy and a top slice of Revenue Support Grant (RSG). The Government expects that the safety net will continue to be funded through the levy account and a top-slice, this time on business rates income (as opposed to RSG). The Government believes that funding more of the safety net through a top-slice is fairer because the cost will be shared by all authorities – effectively a form of collective mutual insurance for all local authorities – and not just those who have achieved growth.

The levy
The Government believes that providing a credible growth incentive should be a feature of reformed rates retention. Scrapping the levy would require primary legislation. However, the Government remains strongly committed to rewarding

growth and is minded to reform this element of the system within the current legislative framework. This would mean raising the threshold at which the levy falls due.

The Government proposes that the level at which an authority becomes eligible to pay the levy should be raised so that only growth that could be considered ‘extraordinary’ would be subject to it. After this point the levy should be 100% and therefore function as a cap. This would be a simpler approach, with greater predictability for authorities and would provide a stronger growth incentive, as authorities would be able to retain all growth that can reasonably be attributed to their management of their local economy.

(‘Extraordinary’ is used here in its literal sense to describe growth outside of the ordinary, for example as a function of provisions made and released. As this growth cannot be attributed to an authority’s management of their local economy it is reasonable and proportionate that the levy be used as an inverse of the safety net to limit gain.)

It would be possible to use the existing legislative framework to reform the function of the levy to address ‘extraordinary growth’. Reform can also be designed to simplify this element of the system. The higher the threshold at which the levy fell due, the smaller the number of affected authorities. For example, using 2016-2017 data, setting the levy at 150% Baseline Funding Level would have meant 18 authorities would have been subject to it, at 200% it would have affected 7 authorities and at 250% it would have seen only 4 authorities subject to the levy. The consultation paper seeks views on the level at which the levy should fall due (e.g. 150%, 200%, 250%, or another level).

The levy is currently calculated as follows and is paid only by tariff authorities:

Levy rate = 1 - (Baseline Funding Level/Business Rates Baseline) or 0.5, whichever is lesser
Levy payment = (retained rates – Baseline Funding Level) * levy rate, if retained rates > Baseline Funding Level.

<u>Tier splits</u>
The Government is minded to retain a national tier split as an appropriate mechanism to distribute business rates income in multi-tier areas between billing and precepting authorities. Determining an appropriate level for the tier split between counties and districts is a decision that will need to be made later in the process, following decisions on other elements of the system.

The consultation paper does not seek views on an appropriate tier split between London boroughs and the Greater London Authority. The Government currently makes this decision separately, in consultation with London authorities, and this will continue to be the Government’s approach.

It is expected that Fire and Rescue Authorities will continue to retain 1% of business rates across the area they cover.

Pooling
The Government believes that pooling is desirable and offers many benefits. For example:-

- It allows better planning across a functional economic area,
- It facilitates joint decision making on the strategic spending of business rates growth.
- It facilitates opportunities for collaboration and friendly scrutiny.

If the levy were to be reformed, a key incentive to pool will be lessened and therefore, the consultation paper seeks views on how pooling can be incentivised and improved.

The Government will also consider how best to encourage pooling as part of its wider approach to devolution policy.

Simplifying the system and reducing volatility

This section of the consultation paper covers:

- a review of hereditaments on the central and local lists;
- the options available to deliver the Government's commitment to address volatility caused by appeals and valuation loss; and
- a proposal to simplify the administration of the business rates retention system.

The central and local lists
The central list is a list of hereditaments that pay business rates directly to central government, as opposed to a local billing authority. Under the Local Government Finance Act 1988, the Secretary of State has the power to designate hereditaments to the central list. Criteria to assist in this decision are also already in existence. The Government re-affirms its view that the reform of the central and local lists should create a rational and transparent system which is uniform throughout the country and that the central list should be used to list hereditaments which by their nature are unsuitable for listing in local lists.

Baselines will need to be adjusted where there is movement between lists, so that any movement will not impact on an authority's income. The Government therefore proposes that the most suitable time for hereditaments to move between lists is at a reset. Once a decision has been made on what type of reset will be implemented in the reformed system, options can be considered for how often it is appropriate to consider reallocating classes of hereditaments between the non-domestic rating lists.

Appeals and other valuation change
The Government remains committed to addressing the impact of appeals and other valuation change on local authority income and has previously stated its intention to centralise this risk.
Authorities are required, under international accounting standards, to make provisions against valuation change. Both overestimating and underestimating these provisions can cause volatility in income at a local level. It is therefore necessary to reform how provisions are addressed alongside centralising appeals and other valuation change.

In order to address volatility caused by valuation change and associated provisions, MHCLG has worked with the Chartered Institute of Public Finance and Accountancy (CIPFA) to scope options to answer two central questions:

a) How to measure the compensation due to local authorities, if business rates losses due to valuation change were to be centralised; and,

b) How to mitigate the impact of provisions on authorities' ability to spend on services in-year using accounting adjustments.

The Government is seeking solutions that don't exacerbate complexity of the business rates retention system. The consultation paper proposes a change to the administration of the system as the best way to mitigate the impact of appeals and provisions for appeals.

<u>Change to the administration of the system:</u>

This change would work by having floating tariffs and top-ups, compared to fixed ones. Local authorities' own estimates of income - after provisions - would be used each year (through NNDR1s) to set top-ups and tariffs.

- The date that NNDR1 forms are submitted would have to be brought forward to around September each year.
- There would need to be a change to the information that is requested through NNDR forms. Specifically, local authorities would have to provide figures, posted to individual years, covering prior-year adjustments incorporating appeals and valuation change for "gross rates payable".

It is the Government's view that any additional effort required to implement these changes to NNDR forms would be offset by the outcomes the reform would deliver.

The Government is committed to ensuring local authorities see the benefit of all their growth. A separate baseline could be used to measure growth from, based on either gross rates payable or net rates payable. This could be recalibrated annually to take account of backdated appeals.

Such a change to the administration could bring significant benefits such as providing predictability of income from business rates, allowing local authorities to retain all the growth they achieve and a more responsive and flexible system.

How resets, tier splits, the safety net and levy will work from 2020 are all decisions that would still need to be taken regardless.

<u>Summary</u>
This consultation will not be testing how we transition into the new system. The Government will consult further in 2019.

- There will be a full reset of the business rates system in 2020/21. This will allow full implementation of both reforms to the business rates retention system and the outcome of the review into relative needs and resources.
- The outcome of the review into local authorities relative needs and resources together with the Spending Review will give all local authorities new funding allocations.
- MHCLG will continue to work with the sector on the design of the future business rates retention system through 2019.

Summary of questions

Question 1:	Do you prefer a partial reset, a phased reset or a combination of the two?
Question 2:	Please comment on why you think a partial/ phased reset is more desirable.
Question 3:	What is the optimal time period for your preferred reset type?
Question 4:	Do you have any comment on the proposed approach to the safety net?
Question 5:	Do you agree with this approach to the reform of the levy?
Question 6:	If so, what do you consider to be an appropriate level at which to classify growth as ‘extraordinary’?
Question 7:	What should the fall-back position be for the national tier split between counties and districts, should these authorities be unable to reach an agreement?
Question 8:	Should a two-tier area be able to set their tier splits locally?
Question 9:	What fiscally neutral measures could be used to incentivise pooling within the reformed system?
Question 10:	On applying the criteria outlined in Annex A, are there any hereditaments which you believe should be listed in the central list? Please identify these hereditaments by name and location.
Question 11:	On applying the criteria outlined in Annex A, are there any listed in the central list which you believe should be listed in a local list? Please identify these hereditaments by name and location.
Question 12:	Do you agree that the use of a proxy provides an appropriate mechanism to calculate the compensation due to local authorities to losses resulting from valuation change?
Question 13:	Do you believe that the Government should implement the proposed reform to the administration of the business rates retention system?
Question 14:	What are your views on the approach to resetting Business Rates Baselines?
Question 15:	Do you have any comments at this stage on the potential impact of the proposals outlined in this consultation document on persons who share a protected characteristic?

A review of local authorities' relative needs and resources

Technical consultation on the assessment of local authorities' relative needs, relative resources and transitional arrangements (December 2018)

This consultation seeks views on the approach to measuring the relative needs and resources of local authorities, which will determine new baseline funding allocations for local authorities in England in 2020-21. The current methodology has not been updated since the introduction of the 50% business rates retention system in 2013/14.

The aim of the review is "to enable the Government to reconsider the drivers of local authorities' costs, the resources available to them to fund local services, and how to account for these in a way that draws a more transparent and understandable link between local circumstances and resource allocations."

The Current Needs Assessment

At present, 15 different relative needs formulas and several tailored distributions for services previously supported by specific grants are used to determine annual funding allocations through the settlement. These formulas involve over 120 cost drivers and were last updated in 2013-14 (although the underlying statistical modelling which determined the cost drivers and weightings given to them can be traced back even further).

Adult's Personal Social Services
- Social Services for Older People RNF (Relative Needs Formula)
- Social Services for Younger Adults RNF

Fire and Rescue Service
- Fire and Rescue RNF

Capital Finance
- Capital Financing RNF

Children's Services
- Children's Social Care RNF
- Local Authority Central Education RNF
- Youth and Community RNF

Environmental, Protective and Cultural Services RNF
- Upper-tier EPCS RNF
- Lower-tier EPCS RNF
- Concessionary Travel RNF
- Fixed Costs RNF
- Flood Defence RNF
- Continuing EA Levies RNF
- Coastal Protection RNF

Highways Maintenance
- Highways Maintenance RNF

Proposed Relative Needs Formulas

The Government has proposed a simplified approach to the relative needs assessment by reducing the number of formulas and focusing on the most important cost drivers. The starting assumption has been that all council services are included in the Foundation Formula, and the Government have considered on a case-by-case basis whether a standalone funding formula is merited for particular service areas. The Review of Local Authorities' Relative Needs and Resources consultation proposes a per capita foundation formula for upper and lower-tier authorities, alongside seven service-specific funding formulas.

Foundation Formula[1,2]

Adult Social Care RNF[1]
Children Services RNF[1]
Public Health[1]
Highways Maintenance[1]
Fire and Rescue[1]
Legacy Capital Finance[1,2]
Flood Defence and Coastal Protection[2]

Terms of Reference
The terms of Reference of the review of local authorities' relative needs and resources are to :-

- set new baseline funding allocations for local authorities
- deliver an up-to-date assessment of the relative needs of local authorities using the best available evidence.
- examine the relative resources of local authorities.
- focus initially on the services currently funded through the local government finance settlement, with subsequent consideration of additional responsibilities devolved to local government under further business rates retention,
- consider appropriate transitional arrangements
- develop the approach through close collaboration with local government

Guiding Principles
- Simplicity
- Transparency
- Contemporary
- Sustainability
- Robustness
- Stability

[1] Indicates an Upper-Tier authority RNF
[2] Indicates a Lower-Tier authority RNF

Implementation

The Government aims to implement as part of the 2020-21 local government finance settlement :-

- the outcome of the review,
- increased business rates retention,
- a full business rates baseline reset, and
- the 2019 Spending Review.

The Government recognise that early notification of final funding allocations in particular would help councils' medium term financial planning and service delivery. Given that final confirmed allocations will be subject to the timing and outcome of the planned Spending Review, the Government's current aim is to publish indicative allocations through a further stage of formal consultation before the 2020-21 provisional local government finance settlement.

Focus of the Review

Three main areas:-

i) relative needs,
ii) relative resources, and
iii) transitional arrangements.

Four Key Areas of the Consultation

- To present proposals to simplify the assessment of local authorities' relative needs by introducing a simple Foundation Formula, alongside several 'service-specific' formulas. The majority of these formulas will be subject to a service-specific Area Cost Adjustment.
- To consider the type of adjustment that will be made to an authority's relative needs assessment to take account of the relative resources available to them to fund local services, such as council tax
- To propose a set of principles that will be used to design transitional arrangements and examine how the baseline for the purposes of transition should be established
- To seek views on the potential impact of the options outlined in this consultation document on persons who share a protected characteristic.

Relative Needs

The relative needs of local authorities are determined by the use of funding formulas, which incorporate relevant local demographic or other data, thought to predict the relative demand councils face when delivering different services.

In order to strike a balance between simplicity, transparency and precision, the Government has taken a number of factors into consideration when settling the number and type of relative needs formulas required, and the cost drivers included in them.

The needs assessment separates factors between those which drive demand for the number of services or interventions required (e.g. the number of people living in a local authority area), and those which affect the cost of delivering those services or interventions (e.g. the cost of employing staff which will vary across the country, or the impact of providing services across congested or sparsely populated areas)

To minimise the use of judgement in the needs assessment, statistical techniques offer the best available empirical basis for determining which cost drivers are most significant in driving authorities' need to spend on particular services, and the relative importance (or weighting) of cost drivers included in a formula.

It will be necessary to decide what proportion of the overall funding that is available through the settlement will be allocated by each formula.

A key consideration for the Government is how to future-proof the formula and still offer funding certainty for authorities.

<u>Structure of the Relative Needs Assessment</u>
The general consensus was that deploying several service-specific formulas, alongside a Foundation Formula, would help to ensure an appropriate balance between simplicity, transparency and precision. However, many argue that the needs assessment should take account of specific factors that are relevant to their circumstances or those of a particular group of authorities and a large number of additional cost drivers have been suggested, along with several service areas that might warrant a specific funding formula. However, the Government say that the level of consensus around many of the suggestions that were made was not high but those that receive a reasonable level of support are discussed in the consultation paper.

The Government is minded to deploy a per capita Foundation Formula for upper and lower tier authorities, alongside seven service-specific funding formulas.

1) Adult Social Care
2) Children and Young People's Services
3) Public Health
4) Highways Maintenance
5) Fire and Rescue
6) Legacy Capital Finance
7) Flood Defence and Coastal Protection

The Government state that the overall level of funding available for redistribution at the 2020-21 local government finance settlement will be subject to the outcome of the 2019 Spending Review. Further consideration will be needed before the Government establishes what proportion of the overall funding is to be allocated by each formula.

In order to illustrate where specific council services are captured in the proposed relative needs assessment, the Government has ‘mapped’ expenditure lines from local authority general fund revenue account outturn forms to specific areas of the needs assessment.

Overview of Proposed Relative Needs Formulas

Upper or Lower Tier Formula:	Separate upper and lower tier formulas
Cost drivers included in the formula	– Total population
Analytical technique used:	Per capita basis
Will an Area Cost Adjustment apply?:	Yes
Example service areas included in formula:	<u>Upper tier:</u> Waste disposal Public transport Libraries Leisure Planning Central services <u>Lower tier:</u> Waste services Environment Homelessness Sports and recreation Central services

In the case of London, separate funding is provided to the Greater London Authority for the functions that it provides. These are upper tier functions which include public and other transport planning, local bus support, rail support, other transport support and public transport co-ordination. It will be necessary to take account of this to avoid an overestimation of relative needs for London authorities. Therefore in line with past settlement methodologies, a ‘London adjustment’ will be used to reflect that there is no ‘need to spend’ on these service areas for London authorities.

As well as population, the Government has also looked at the potential of rurality and deprivation as cost drivers for the Foundation Formula. It notes, however, that in the upper tier Foundation Formula, population alone explained 88.1% of all variation in past expenditure and population alone explained 84% of variation in past expenditure included in the lower tier Foundation Formula.

Adult Social Care
As a targeted service with strict eligibility criteria, adult social care is a complex area that accounts for the largest proportion of expenditure for upper tier authorities. The

Government believes that the best available option for adult social care is to deploy the most up-to-date, service-specific formula available, which offers appropriate levels of analytical robustness. The Government's leading option is to base an adult social care relative needs formula on work by LG Futures (a specialist consultancy firm), together with the Personal Social Services Research Unit at the University of Kent and the London School of Economics and Political Science, using data collected in 2012-13.

Children and Young People's Services
Children and Young People's services is a complex area with unique cost drivers. A significant proportion of expenditure is on services for the most vulnerable children, which are relatively low incidence, but high cost. Children and Young People's services represents the second largest area of expenditure for upper tier authorities and the Government believes that the best available option is to develop a new service-specific formula which offers appropriate levels of analytical robustness. To do this the Government has commissioned a children's services data research project.

Public Health
Public health is a significant area of expenditure for upper tier authorities and includes a wide range of services, some of which are universal (e.g. health visitor programmes) and others which are targeted at specific population groups (e.g. drug misuse treatment services). In addition, some public health activity is currently prescribed in regulations, which local authorities are legally required to provide. Given the complexity and size of this service area, the Government believes a service-specific approach would be required for public health if it falls within the scope of the review. On this basis, the leading option would be based on a new public health formula that was developed by the Advisory Committee on Resource Allocation. This formula was the subject of formal consultation in 2015.

Highways Maintenance
There is broad agreement that the two cost drivers - road length and traffic flow – are the most significant. The Government is therefore minded to implement a straightforward formula for this service area that incorporates these two cost drivers.

Legacy Capital Finance
A separate Legacy Capital Financing relative needs formula is required to ensure that local authorities with borrowing commitments that were agreed to be funded through the local government finance settlement, prior to the introduction of the Prudential Capital Finance System, have that cost recognised in their relative needs assessment. Legacy Capital Finance remains a pressure on authorities and the Government believes that the unringfenced funding distributed by the settlement provides local authorities with the greatest flexibility to service this historical debt.

Flood Defence and Coastal Protection
Upper-Tier authorities: The Government believes that it is proportionate to incorporate upper tier flood defence and coastal protection within the upper tier Foundation Formula, on the basis of the overall scale of expenditure and the distribution of relative needs.

Lower tier authorities: Spending patterns suggest separate flood defence and coastal protection relative needs formulas could be introduced for lower tier authorities. The government believe the following cost drivers are the most significant for flood defence and coastal protection:

Flood defence: length of ordinary watercourse, properties at risk, and agricultural land at risk.
Coastal protection: properties at risk, and length of coast.

The Government will use local authority level expenditure based regression as the basis for further analytical work to determine whether these are the most appropriate cost drivers, before taking a view on the best approach.

Fire and Rescue
Further work is required to identify an appropriate approach to develop the new funding formula for this service area. As this work progresses the Government will sense-check the results of the analysis with experts in the sector, including the National Fire Chiefs Council. Subject to the outcome of this consultation and additional analytical work the Government will form a view on the best approach.

AREA COST ADJUSTMENT

The cost of delivering the same services may vary between local authorities for a number of reasons - for example:

- the costs of employing staff or renting non-domestic properties can vary considerably between different places, and
- some local authorities face unique pressures related to their geography; such as the costs associated with conducting business from isolated or peripheral communities or providing services to widely dispersed or densely concentrated populations.

The Government believes that it is important to include an Area Cost Adjustment in the assessment of relative needs and has identified the following criteria to determine which factors are taken into account:

i) significance
ii) variation
iii) data availability
iv) appropriate incentives - the Area Cost Adjustment should maintain incentives for local authorities to design services which deliver at the lowest possible cost.

The Government is minded to incorporate the factors set out below:

i) a rates cost adjustment, including rents, to reflect the variation between areas in the cost of using equivalent premises due to differences in local supply and demand factors,
ii) a labour cost adjustment, including accessibility, to reflect the fact that authorities will need to compete with other potential employers to secure and retain suitably skilled staff, and
iii) a remoteness adjustment, to account for variation in the cost of some inputs due to the size of local markets or isolation from major markets.

<u>Proposed Area Cost Adjustment methodology</u>
Whilst a consistent approach to Area Costs will be adopted across the relative needs assessment, the Government intends to tailor the Area Cost Adjustment for the Foundation Formula and each service area it is applied to, in order to reflect the different impact of these costs.
The factors set out above (a Labour Cost Adjustment (inclusive of accessibility), a Rates Cost Adjustment (inclusive of rents), and Remoteness) will be weighted together into a single index for each funding formula, using evidence-based weights which are appropriate for the relevant service(s).

<u>Weighting of funding between services</u>
The Government intends to introduce several funding formulas, which means that it will be necessary to decide the proportion of overall funding that is allocated by each one.
Some support has been expressed previously around using the proportion of spending that local government as a whole currently commits to different services as a basis for this, potentially supplemented with trend analysis or time series modelling to set control totals that reflect the pressures that local government are expected to face in the coming years. The Government intends to further explore the approach to determining control totals, and will ensure that any assessment of the future

pressures local authorities may face is aligned with the wider 2019 Spending Review, which will determine the overall level of funding available for redistribution at the 2020-21 settlement.

Weighting cost drivers in a relative needs formula
Statistical techniques offer an evidence-based way to determine funding allocations by minimising the use of judgement in constructing funding formulas. The use of statistical techniques would enable the Government to determine which cost drivers have the most significant impact on an authority's need to spend, and the relative importance (or weighting) of one cost driver against another within a formula.

The Government have considered the merits of a range of techniques that could be used. Alongside the principles of the review, a number of other considerations were taken into account, including:

i) the analytical robustness offered by a technique,
ii) the level of sophistication employed by a technique (and the trade-off between complexity, robustness and transparency), and
iii) practicalities, including the availability of appropriate data sources.

The two leading statistical techniques identified for the review are 'multi-level' modelling and expenditure based regression.

Multi-level models
Local authority level expenditure based regression models aim to account for variances in relative needs between local authority areas. Multi-level models do the same thing, but also aim to account for variances in relative needs inside an individual local authority area. This has the advantage of helping to eliminate any undue impact that individual council expenditure decisions may have had on the pattern of relative needs identified. However multi-level models are more complex than simple regression models and rely on a large amount of detailed information related to the level and distribution of spending within local authorities.

As multi-level models are recognised as a more robust approach for services which represent a significant proportion of expenditure and where future levels of need are more challenging to predict, the Government proposes the use of this technique in relation to Adult Social Care and Children and Young People's Services.

Local authority level expenditure based regression models
A significant challenge in determining the relative needs of local authorities is that there is no objective measure of 'need'. The most commonly used proxy of need in the past has been past spending per head (of relevant population), which is considered by Government to be reflective of the relative cost and importance of a service for local government. Such local authority level expenditure based regression models measure and compare the relationship between the 'need to spend' on council services and independent data sets which drive the cost of service delivery. The model attaches a 'weighting' to each cost driver included in a funding formula, and the greater the extent to which a cost driver explains the pattern of past expenditure, the more weight is attached to that cost driver. The model estimates the average relationship between each cost driver and past expenditure across all

local authorities. This makes it possible to understand how much, on average, an additional unit of a particular cost driver represents a change in the need to spend – and therefore how much of the funding available for distribution should be allocated. Allocations are therefore determined by the value for each cost driver in each authority.

Although some criticisms have been raised against use of local authority level expenditure based regression, the Government believes it is still the best statistical approach in certain circumstances for the following reasons:
- It does not allocate more funding to councils that have spent more in the past
- It does not penalise efficiency.

Future proofing the needs assessment

The Government recognises that the impact of population and demographic changes over time is a particular concern for many in local government. The rate and nature of population change is likely to vary from one local authority area to another, which means a key consideration is the balance to strike between futureproofing the formula and offering funding certainty for authorities.
There is a strong consensus around using official population projections to reflect changing population sizes when assessing the relative needs of local authorities, and the Government is minded to agree that using Office for National Statistics population projections to calculate allocations for each year of a forward funding period, at the outset of the period, and updating these when the needs assessment is refreshed, is the most appropriate way to reflect future population changes, while giving authorities certainty over their income for the duration of the funding period.

Relative Resources

In addition to funding allocated through the local government finance settlement, councils raise resources locally. Authorities' capacity to fund the services they provide through local resources varies across the country depending on both their relative levels of needs and the resources they can raise, due to a number of factors, such as local circumstances and priorities, central Government policy and the legal framework in which they operate.

Local resources include:
• Council tax and
• Sales, fees and charges

The Government believes that it is important to continue to take account of councils' relative ability to raise resources.

For each local authority:-	
Final Funding =	Relative Needs share – Resources Adjustment +/- Possible Transitional arrangements + Actual resources income

<u>Supporting principles relating to the Resources adjustment</u>

- there will be no redistribution of council tax or sales, fees and charges resources between authorities
- the Government do not intend to reward or penalise authorities for exercising local discretion, and
- local authorities with a lesser capacity to fund services through locally raised resources will receive a smaller reduction to their relative needs share.

<u>Council Tax</u>
In line with one of the principles set by the Government, authorities would retain their actual council tax income no matter how the relative resources adjustment is assessed.

The amount of council tax income that local authorities raise varies depending on the size of their council tax base and the council tax level that they set each year, subject to collection rates. To reflect councils' varying ability to raise local resources, the Government will need to determine a measure of council tax income for the purposes of the relative resources adjustment.

In determining a measure of council tax resources, there are several factors which need to be accounted for

i) A measure of council tax base, including a treatment of discounts, exemptions, premiums and local council tax support,
ii) A measure of council tax level,
iii) A measure of the council tax collection rate,
iv) An approach to council tax tier splits in multi-tier areas.
v) an approach to council tax in successive years.

Tax Base

In relation to non-discretionary discounts and exemptions the Government is minded to:-

- continue including the effect of all non-discretionary discounts and exemptions in its measure of the tax base for the purposes of the resources adjustment, using data captured by local authority council tax base returns.
- To ensure consistency, to also take account of the impact that the pension-age element of local council tax support has on an authority's ability to raise council tax income.

As a result, a smaller resources adjustment would be applied to those authorities that have a greater number of properties in their area subject to mandatory discounts or exemptions.

In relation to discretionary discounts and premiums the Government is minded to:-

- continue with an assumption-based approach to take account of the second homes discount, the empty homes discount and the empty homes premium in its measure of council tax base.

The Government wishes to explore options for taking account of the working age element of local council tax support when determining the measure of authorities' council tax base.

Council Tax Level

The Government is minded to use a notional assessment of council tax levels when making the relative resources adjustment. This is an approach that has precedent in previous local government funding settlements, including the 2013-14 methodology.

Using a notional council tax level, as part of a notional measure of council tax resources, would mean that two local authorities with similar tax bases and a similar assessment of relative needs would receive broadly similar baseline funding levels, irrespective of their actual council tax levels.

Consistent with its aim to adopt a simple and transparent approach, the Government is minded to set a uniform notional council tax level for all areas (although work will continue on this).

Collection Rate
In 2017-18, the average England-level council tax collection rate was 97.1%, ranging from 90.0% to 99.5% at individual local authority level. The Government is inviting views on how it should determine the measure of council tax collection rate in the resources adjustment.
One approach would be to use councils' actual collection rates. However, this would mean that for two authorities that are identical aside from their collection rate, the one with the higher collection rate would receive a lower baseline funding level. Another approach is to apply a single, uniform collection rate to the measure of each local authority's council tax income. This uniform collection rate could be set at various levels (e.g. at the minimum, average, or maximum collection rate); however, it would have the same effect for all authorities in the relative resources adjustment irrespective of their actual collection rate.

Tier splits
Council tax is collected by a billing authority and in multi-tier areas the income is split between each tier and/or fire and rescue authorities. Once an assessed measure of council tax is agreed, the Government will need to determine how to split or allocate the resources adjustment for areas where upper tier, lower tier and/or fire responsibilities are carried out by different local authorities. This approach would not pre-judge the split of growth in business rates between tiers.

Council tax in successive years
In the case of a multi-year settlement from 2020-21 onwards, it will be necessary to consider the treatment of council tax income in successive years as part of a resources adjustment.

The Government is minded to fix a single measure of council tax resource over the period. This approach has the advantage of rewarding authorities for growth in their council tax receipts whilst not linking the methodology to a measure of projections of council tax resources that may be uncertain.

Sales, Fees and Charges

Sales, fees and charges are another source of income for many local authorities, which - like council tax – vary by local authority.

- Local authorities can charge for **statutory services**, where the power to charge is prescribed by legislation.
- Local authorities also have the power to charge for **discretionary services** up to full cost recovery where there is no pre-existing legislation governing the charging regime. However if authorities wish to charge above cost recovery for services, they may do this commercially via a trading company.

Unlike council tax, sales, fees and charges have not previously been taken into account in a relative resources adjustment. The Government has considered whether it is appropriate to make a more direct adjustment for sales, fees and charges income when assessing local authorities' relative resources, and the practical considerations that would apply. The following considerations have been taken into account:

i) Scale
ii) Ability, choice and incentive effects
iii) Volatility
iv) Data availability

Having taken the above considerations into account, the Government recognises that there are practical challenges in taking a direct account of sales, fees and charges income through the resources adjustment and it is therefore broadly minded not to do so.

Transitional arrangements

Calculating local authorities' relative needs and resources using new relative needs formulas and updated data is likely to result in changes to the level of funding individual councils receive. Once new funding baselines have been established, the Government intends to introduce transitional arrangements that will determine the basis on which authorities reach their new funding allocations. The government's aim is that transitional arrangements will unwind over time to ensure that every council reaches their full funding allocation as quickly as practicable. T

Principles for Transition

Given the wide range of options available, the Government intends to use the principles set out below, along with the wider principles of the review in designing transition arrangements:

i) stability – the transition from the existing funding position in 2019-20 to new target allocations must be manageable and sustainable for both the sector and individual local authorities, in the context of wider changes to the local government finance system,
ii) transparency – the process must be clear and understandable to support financial planning and help explain the nature of transition to a wider audience,
iii) time-limited – support for those authorities with a reduction in settlement funding allocations using deferred gains for those authorities that see an increase in allocations should be provided over a fixed period of time to enable target allocations to be reached as soon as practicable,
iv) flexibility – the speed of change could vary across the sector to achieve greater efficiency. Considerations might include local revenue raising capacity, distances from target allocations or relative funding pressures, for example to deliver statutory services.

Establishing the baseline
The scale of transition will depend on the baseline it is measured from, and the Government propose that the starting baseline for the purposes of transition will be a measure of the funding available to each local authority in 2019-20.
However, this position may require some form of 'adjustment' in order to reflect wider considerations such as the increase in business rates retention, decisions on

the treatment of business rates growth achieved during the current spending period and due to be ‘reset’ in 2020, or so-called negative Revenue Support Grant.

There are a number of options for establishing the baseline, and further engagement with those in the sector will be required in order to define the best possible measure.

WHAT IS A FOUNDATION FORMULA (December 2017 – Government consultation)

A simple 'foundation' funding formula

There are a number of factors, such as the basic demographic characteristics of an area, which affect the cost of providing multiple services. Therefore it may be possible to use a simple foundation formula to allocate funding to each type of local authority based solely on these cross-cutting or 'common' cost drivers. This approach would make the relative needs assessment much simpler but would result in particular cost drivers for some large specific service areas being excluded, which may result in a less fair distribution for authorities that have high costs in delivering those services.

Introducing a foundation formula based on common cost drivers to allocate funding to each type of local authority would result in the most understandable and transparent system. Non-specialists would easily be able to see in the clearest possible terms how the differences in common cost drivers between areas affected the level of funding authorities received. However, such a simple approach would involve a greater degree of Ministerial judgement than the current relative needs assessment. Changing the structure of the relative needs assessment in such a significant way could lead to dramatic changes in funding allocations for some authorities, and such a simplified approach might fail to capture variation in important cost drivers. This would likely be amplified for those authorities with an exceptionally high level of demand for, or unique costs of delivering a relatively expensive service.

However, the Government also acknowledge that there may be particular service areas where a more specific approach is required, and so it will also consider the case for going further and allocating a proportion of the available funding based on the particular cost drivers for those services.

Summary of questions

Question 1): Do you have views at this stage, or evidence not previously shared with us, relating to the proposed structure of the relative needs assessment set out in this section?

Question 2): What are your views on the best approach to a Fire and Rescue Services funding formula and why?

Question 3): What are your views on the best approach to Home to School Transport and Concessionary Travel?

Question 4): What are your views on the proposed approach to the Area Cost Adjustment?

Question 5): Do you agree that the Government should continue to take account of non-discretionary council tax discounts and exemptions (e.g. single person discount and student exemptions) and the income forgone due to the pensioner-age element of local council tax support, in the measure of the council tax base? If so, how should we do this?

Question 6): Do you agree that an assumptions-based approach to measuring the impact of discretionary discounts and exemptions should be made when measuring the council tax base? If so, how should we do this?

Question 7): Do you agree that the Government should take account of the income forgone due to local council tax support for working age people? What are your views on how this should be determined?

Question 8): Do you agree that the Government should take a notional approach to council tax levels in the resources adjustment? What are your views on how this should be determined?

Question 9): What are your views on how the Government should determine the measure of council tax collection rate in the resources adjustment?

Question 10): Do you have views on how the Government should determine the allocation of council tax between each tier and/or fire and rescue authorities in multi-tier areas?

Question 11): Do you agree that the Government should apply a single measure of council tax resource fixed over the period between resets for the purposes of a resources adjustment in multi-year settlement funding allocations?

Question 12): Do you agree that surplus sales, fees and charges should not be taken into account when assessing local authorities' relative resources adjustment?

Question 13): If the Government was minded to do so, do you have a view on the basis on which surplus parking income should be taken into account?

Question 14): Do you agree with the proposed transition principles, and should any others be considered by the Government in designing of transitional arrangements?

Question 15): Do you have views on how the baseline should be constructed for the purposes of transition?

Question 16): Do you have any comments at this stage on the potential impact of the proposals outlined in this consultation document on persons who share a protected characteristic? Please provide evidence to support your comments.