

Executive

Fair Funding Review - update

Item No 5

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Summary: This report updates the Executive on the Government's progress with regard to the Fair Funding Review, and includes an overview of the key themes that are likely underpin London Councils' response to the Government's technical consultation on relative need, which has a deadline of 12 March.

Recommendation: Executive is asked to consider and comment on:

- the progress of Fair Funding Review; the direction of travel of London Councils' response to the technical consultation on relative need; and the planned future work programme.

Fair Funding Review – update

Introduction

1. This report provides an update on the Government's progress with regard to the Fair Funding Review of relative needs and resources. It sets out the aims, principles, planned work streams and overall timeline for the Review.
2. It includes a summary of the current technical consultation on relative need and the key themes that will underpin London Councils' response, due on 12 March. It also sets out the next steps for London Councils' work in this area between now and the summer of 2018.

Background

3. Funding baselines for local authorities are based on an assessment of local authorities' relative needs and resources. The methodology behind this assessment was introduced over ten years ago, and has not been updated since the introduction of the 50% business rates retention system in 2013/14.
4. The methodology is very complex and involves 15 relative need formulae and several tailored distributions for services previously supported by specific grants, which determine annual funding allocations for each local authority across England. These formulae involve over 120 indicators of 'need', reflecting factors previously identified as driving the costs of service delivery.
5. In February 2016, in the 2016/17 Local Government Finance Settlement, the then Secretary of State for Communities and Local Government, Greg Clark, first announced the Government's intention to review the way local authorities are funded via a "Fair Funding Review". At the time, this was part of the plans for 100% business rates retention that were expected to be implemented in April 2019.
6. In the summer of 2016, alongside the main consultation on 100% retention, the Government published a call for evidence on the principles of the Fair Funding Review. London Councils responded jointly with the GLA (alongside the joint response to the 100% retention proposals), setting out high level principles that the assessment of need and redistribution should become simpler, more transparent, fairer and more responsive under the new system than currently.

7. Since then, the 2017 general election triggered the fall of the Local Government Finance Bill, that would have made 100% retention possible. Following a period of uncertainty over the summer and autumn, the Government recommitted to further business rates retention for the sector, which will be implemented a year later than originally planned, in April 2020, and will be 75% rather than 100% retention.
8. The Government has confirmed that it intends to implement the new funding baselines, that will be determined by the Fair Funding Review, at the outset of the 75% retention scheme in 2020-21.
9. Work is therefore continuing in parallel to implement these separate but interlinked parts to the local government finance system. Since 2016, this has included a series of technical working groups jointly chaired by the LGA and MHCLG. The Fair Funding Review technical working group has been considering and advising on how the new needs and resources assessment may be undertaken. London Councils is represented on this group, which meets roughly every 6 weeks.

Aims, principles and timeline

10. The Government has stated that the aims of the Review are to:
 - **set new funding baselines** for local authorities in England, aiming for implementation in 2020/21;
 - **replace the current methodology** for determining funding baselines, which is considered out-of-date and complex;
 - design a new '**relative needs assessment**' methodology by considering factors that drive the costs of service delivery and how to put these together analytically into new funding formulas;
 - consider how to make a fair **adjustment for 'relative resources'** (e.g. council tax), and how to **transition to new allocations** quickly;
 - focus primarily on services currently funded through the settlement (rather than those outside of it, such as Public Health); and
 - be developed through close collaboration with local government.
11. The principles by which the Government will undertake the work of the review are:
 - **Simplicity** - an opportunity to identify the most important factors that drive need to spend in a way that is simple and practicable.

- **Transparency** – it should be straightforward for those affected by the relative needs assessment to understand local allocations so that they can hold their local representatives to account for the decisions that they make.
- **Contemporary** - using the most up-to-date data available and data that can be regularly updated at planned intervals.
- **Sustainability** - an evidence-based approach will be deployed to identify the factors which drive costs for local authorities today *and* in the future. The new funding formula must, as far as is practicable, anticipate future demand for services.
- **Robustness** - taking into account the best possible objective analysis; and
- **Stability** - the funding formula should support predictable, long-term funding allocations, including transitional arrangements and alignment with multi-year settlements.

12. To achieve these objectives, the Review will cover three broad work streams - the measurement of relative need, the treatment of relative resources, and the approach to transition to the new funding baselines.

13. The Government's overall timetable, working toward publication of final baselines in the 2020/21 Local Government Finance Settlement, is set out below.

Table 1 – Fair Funding Review timetable

Date	Milestone
March 2018	Technical consultation on relative need closes
Spring/Summer 2018	MHCLG issues series of technical papers on relative need, resources and transition
Summer 2018	Finalise overall structure and leading options for needs and resources assessments
Spring 2019	Finalise options for needs and resources
Summer 2019	Conclusion of detailed research project into Children's Services
Summer 2019	Indices of Deprivation data sets updated
December 2019	Provisional 2020/21 Local Government Finance Settlement
April 2020	75% retention scheme begins and with new funding baselines

14. This is an ambitious timetable with a lot of complex work to be completed in a relatively short period of time, including a detailed research project looking into what

drives the costs of children's services and the updating of the Indices of Deprivation by the summer of 2019.

15. The fact that the first time local authorities will see their proposed new funding baselines will not be until December 2019 in the provisional 2020/21 local government finance settlement – just four months before they are implemented – is a cause for concern as councils will have increasingly less certainty about funding allocations for medium terms financial plans. The Government has stated that it intends to introduce transitional arrangements that are fair, transparent and easily understood so that budgetary impacts can be accommodated. It is, therefore, likely that the first year of the new scheme will see heavily damped transition to the new funding baselines to reduce volatility.

Technical consultation on relative need

16. As part of the first work stream, in December, the Government published a detailed technical consultation specially looking at relative need with a deadline of 12 March.
17. The consultation sets out how the Government is planning to update its measurement of relative need across local government, identifying a preferred approach to simplifying the needs assessment by focussing on the most important cost drivers and reducing the number of formulae involved.
18. The approach put forward is to develop an overarching "foundation formula" that would include a small number of key cost drivers, such as population, deprivation, and rurality, adjusted for area costs, with a series of service-specific formulae for the major services that have more distinct cost drivers and require a more detailed approach. The consultation identifies these as: adult social care; children's services; highways maintenance and public transport; waste collection and disposal; fire and rescue; and legacy capital financing. It considers what the key cost drivers in each of these service areas are and whether any other service areas warrant their own specific formula.
19. The final part of the consultation looks at the different statistical and other techniques that could be used to calculate the relative weightings between these service specific formulae.

20. The Government plans to follow this consultation with a series of technical papers that will consider other aspects of the review, including topics such as:

- the **structure of formulae for service specific cost drivers** that may be included in the relative needs assessment;
- the **assessment of the relative resources** of local authorities, including how income from council tax will be taken into account; and
- **transitioning to the new funding distribution.**

London Councils' response and future work

21. London Councils broadly agrees with the overarching principles of the Review, and few would argue with the overall objective of balancing needs and resources in a manner that is as simple and transparent as possible. However, the means of delivering this will be much debated and will cover, as is clear from the current consultation, a lot of technical and extremely complex territory.

22. London Councils' response to the technical consultation is likely to focus on the importance of the key factors that best reflect the drivers of cost in the capital. In broad terms, these are that: London has high levels of relative deprivation; it costs more to deliver local services in the capital, because of its unique labour and property markets; and any formula should reflect the fact that London's population will continue to grow at twice the rate of the rest of the country over the next 20 years.

High levels of deprivation

23. Deprivation is the key driver of need in many demand-led services. Generally speaking, London has higher levels of relative deprivation than other areas, although this varies from borough to borough and, of course, within each borough. The response will seek to raise concerns that the higher costs of housing in London are not properly reflected in the current formulae (e.g. while average incomes in London are relatively high, average incomes after housing costs are below national average, with implications for rates of in-work poverty), and will call for any income-related data that may be used in the formula, such as the 2019 Indices of Deprivation, to reflect those higher housing costs.

Rapidly changing population

24. One of the principles set out for the Review for London is the “sustainability” principle. It is positive that the Government has set out the intention that “the new funding formula must, as far as is practicable, anticipate future demand for services”. London’s population has grown by 13% since 2010: over twice the rate of the rest of the country. It is forecast to continue to do so over the next 20 years. It is, therefore, vital that the new formulae (both the foundation formula and service-specific formulae) build in future growth through projections not static population figures. However, a caveat to this is that if projections are built into the formula they must be robust and account for “hard to count” areas better. London’s high levels of migration mean it has many of the most undercounted local authorities in the country.

Higher costs of delivering services

25. The response will also argue that any new formula must reflect an accurate and up to date Area Cost Adjustment. The current ACA reflects higher labour and business rates costs. Since 2013, when the current ACA was updated, London’s economy has grown faster than that of the rest of the country. It is, therefore, important that any new ACA continues to reflect the different costs of labour and property in the capital. London Councils will advocate the continuing of such an area cost adjustment, but that it should reflect the most up to date data as some of the data that underpin the current ACA is over 10 years old.
26. The response is likely to raise questions regarding the proposals for rurality as one of the key drivers within the overarching foundation formula. It will be important to avoid the potential to double count the impact of sparse areas that would also be reflected within deprivation measures and, potentially, an area cost adjustment.
27. It will also raise concerns about the hidden service areas that are not currently reflected in the funding formula, such as the additional costs of those with No Recourse to Public Funds (which costs £50 million per annum across London) and the disproportionate impact of Unaccompanied Asylum Seeking Children in the capital.

28. A further concern that will be raised is that the proposals do not include a separate formula for homelessness and temporary accommodation, which currently causes significant additional costs to London boroughs' general funds.

Next steps

29. London Councils' future lobbying, with regard to relative need, will focus on these key areas, which explain why differences in funding levels per head of population are the obvious outcome of a system designed to equalise local councils' ability to deliver the services their populations need.

30. London Councils will respond to the technical consultation by 12 March and will respond to the technical papers planned for publication between the spring and the summer.

31. The broader approach to lobbying, including the priorities for resource equalisation and transition, will be developed in the coming months. Discussions are planned with CELC and SLT towards the end of April, and a set of firm lines and approaches to the key issues in the Fair Funding Review will be in place for Leaders to consider and agree in June. It is also proposed that the Congress of Leaders and the Mayor agree a concerted London position on this at its meeting in July.

Recommendations

32. The Executive is asked to consider and comment on:

- the progress of Fair Funding Review; the direction of travel of London Councils' response to the technical consultation on relative need; and the planned future work programme.

Financial implications for London Councils

None

Legal implications for London Councils

None

Equalities implications for London Councils

None