Leaders' Committee

London Councils' finance lobbying strategy - update

Item 5

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Summary

This report updates Leaders' Committee on the latest developments and lobbying activity in relation to the finance lobbying strategy agreed by Leaders' Committee in June 2018. It includes updates on the major events that will shape the local government finance system from 2020: the Spending Review 2019, the Fair Funding Review and 75 per cent Business Rates Retention reforms. It also provides an update on 2019-20 provisional local government finance settlement.

Recommendations

Leaders' Committee is asked to:

- note the progress on finance lobbying with respect to the key events outlined in the report; and
- consider and endorse the proposed lines in response to the current consultations on the Fair Funding Review and 75 per cent business rates retention.

London Councils' Finance lobbying strategy - update

Introduction

1. In June 2018, Leaders' Committee agreed a finance lobbying strategy covering the period to the end of 2019. This report updates Leaders' Committee on the latest developments and activity with regard to the strategy in relation to the major events due to occur before the end of 2019 that will shape the medium term funding outlook for local government into the mid-2020s, namely: the Spending Review, Fair Funding Review and 75 per cent Business Rates Retention reforms. It also provides an update on the 2019-20 provisional local government finance settlement.

2. In November 2018, London Councils' Executive agreed to increase the level of media and communications activity with regard to both the Fair Funding Review and Spending Review. It was recognised that as part of this it would be important to address points made in other parts of the sector that sought to portray London as being treated in an overly generous way by the current system. The launch of the "Investing in the future" Spending Review lobbying campaign in November signalled a deliberate change in this regard. It particularly drew attention to the need for more resources for the sector as a whole, but also set out the key priorities for London local government. The latest consultations on Fair Funding and 75 per cent business rates retention provide a further challenge, and highlight the continuing need to make the case for a funding system that appropriately reflects the needs of urban authorities in general and for London local government in particular.

Provisional LGF settlement 2019-20

Budget lobbying

3. The 2019-20 provisional local government finance settlement was published on 13 December 2018. By the time of the Leaders' Committee meeting, the final settlement may have been published. A verbal update will be provided.

4. The headlines for London local government from the provisional settlement were that:
    - Settlement Funding Assessment (SFA) will fall by 6.5 per cent in 2019-20 for London Boroughs, confirming real terms cumulative cuts to core funding of 63 per cent across London between 2010 and 2020.
    - Core Spending Power will increase by 2.3 per cent for London Boroughs (compared with 2.8 per cent nationally) in 2019-20.

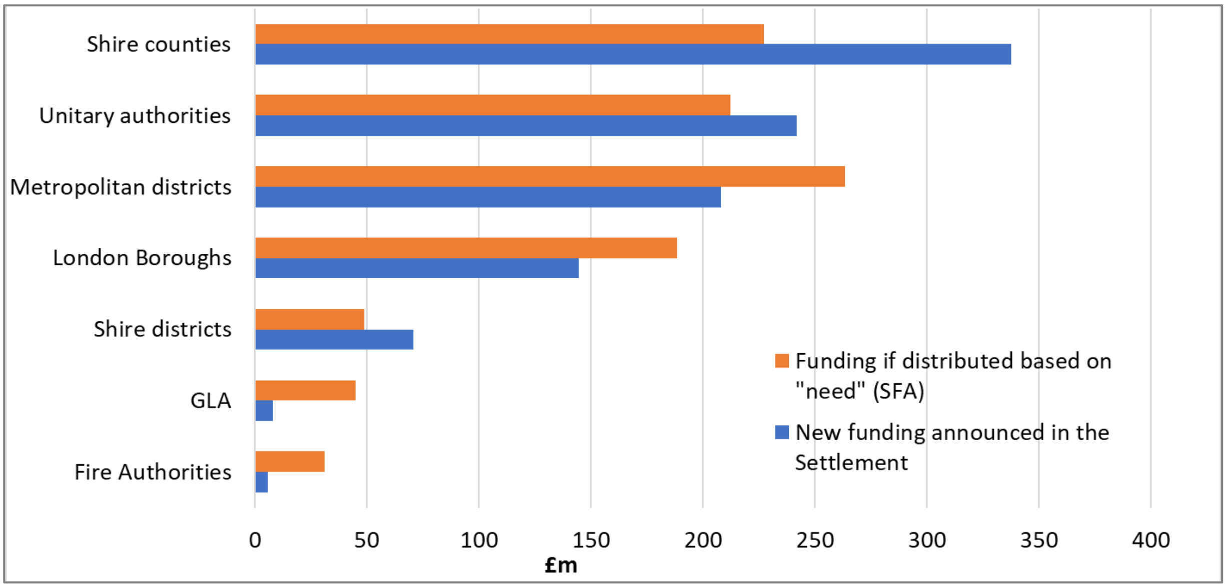
- The Council Tax referendum threshold will remain at 3 per cent in 2019-20 (the Police precept can be raised by £24).
- There will be no change to the Adult Social Care precept principle of a maximum of 6 per cent over the three years to 2019-20.
- £240 million of new funding will be provided in 2019-20 for adult social care “winter pressures” London’s share will be £37 million (15.5 per cent of the England total).
- £410 million of new funding will be provided in 2019-20 to be spent on adult and children’s social care, distributed using the adult social care relative needs formula. London boroughs’ share will be £63 million (15.5 per cent of the England total).
- £180 million of business rates levy surplus will be returned to local government in 2019-20, distributed to local authorities based on relative need. London boroughs will receive £33 million (18.5 per cent of the England total).
- No authority will be subject to “Negative RSG” in 2019-20 at a cost of £152.9 million in foregone business rates nationally (three London boroughs will benefit by a total of £12 million).
- An additional £16 million will be allocated to councils in rural areas through the Rural Services Delivery Grant in 2019-20.
- The threshold at which New Homes Bonus is triggered will remain at 0.4 per cent, and the Government will provide an extra £18 million of central funding for NHB.
- The London 75 per cent business rates retention pilot were confirmed alongside 15 new 75 per cent business rates retention pilots for 2019-20, and the 5 existing pilots will continue in devolution deal areas.

5. In total, the provisional settlement confirmed around £1 billion in direct funding for local government (around £145 million of which will go to London Boroughs) that councils would not have been planning to receive prior to Budget 2018, plus the potential to benefit from greater retention of business rates growth for 16 areas piloting 75 per cent retention next year.

6. London Councils’ consultation response welcomed the announcement of new funding, but raised concerns over its sufficiency, given the cumulative real terms cut to core funding over the decade of 63 per cent and set against the requirement for boroughs to make over £500 million of savings in 2019-20. It also raised concerns over the distribution of some of the new funding that was announced and, in light of the upcoming decisions that the Government will make as part of the Fair Funding Review, the recent trend for the distribution of new funding favouring rural rather than urban areas.

7. While individually these decisions seem small, their cumulative impact is to see a significant shift in resources away from urban areas - where there are significant needs - towards rural areas. For example, Figures 1 and 2 below show the distribution of the £1 billion of new funding by authority type (blue) compared with if it had been distributed purely based on relative needs (orange) - using the distribution that was last calculated in 2013-14. Urban areas (London boroughs, the GLA and metropolitan districts) would have received £136 million more and shire areas (counties and districts) would receive £132 million less.

Figures 1 and 2 - £1bn of new funding in the 2019-20 provisional settlement – distribution by authority type compared with distribution based on relative need



	New funding announced in the Settlement	Funding if distributed based on "need" (SFA)	Difference
Fire Authorities	5.8	31.2	-25.4
GLA	8.0	45.0	-37.1
Shire districts	70.9	48.9	22.0
London Boroughs	144.7	188.5	-43.8
Metropolitan districts	208.1	263.4	-55.3
Unitary authorities	241.8	212.4	29.4
Shire counties	337.6	227.4	110.2
England	**1,016.8**	**1,016.8**	**0.0**

8. With regard to the specific funding streams announced, London Councils' consultation response raised concerns about the weak evidence base underpinning the decision to award more funding to the rural services delivery grant, and the decision to distribute the £410 million of new funding for social care based solely on the adult social care Relative

Needs Formula (RNF), rather than also using the children's social care RNF. London boroughs' share of the adult social care RNF is 15.5 per cent, while their share of the children's social care RNF is 25.5 per cent. If both formulas were used with equal weighting, London would receive £20 million more and county councils £17 million less than is being proposed.

9. A further example, while outside of the main finance settlement, can be seen in the decision announced in December by the DfE to award £250 million of extra revenue funding for children with Special Educational Needs and Disabilities (SEND) over the next 2 years. While welcome, this is being distributed on a per capita basis, using the 2-18 year old population, rather than using the existing High Needs block formula. London boroughs will receive £42 million (17 per cent of the national total). Had the existing high needs formula been used, they would have received 20 per cent of the national total yielding an additional £9 million, while county councils would receive £8 million less.

10. Other concerns raised in the consultation response included the:
    - unfortunate delay in publication of the settlement (but welcoming the broader ambition for it to be published earlier);
    - continued lack of transparency in the finance system;
    - continuation of council tax referendum cap principles;
    - reduction in scale of the London 75 per cent Business Rates Retention pilot; and the
    - changes to the business rates tax base.

11. With regard to communications and media engagement, on settlement day a factual briefing was produced for finance officers, a press release was published[1], and Cllr John gave a reactive interview to BBC London. Further policy briefings were sent to members and London MPs the following day.

Spending Review 2019

12. The date, process and timeline for the Spending Review (SR) remains unknown but is now unlikely to be before the summer. London Councils' officers have been engaging with civil servants as our Spending Review lobbying, and will continue to do so regularly as departmental discussions progress with HMT.

[1] https://www.londoncouncils.gov.uk/node/34887

13. The “Investing in the future” lobbying campaign was launched at the London Councils summit in November 2018, with the publication of a detailed briefing and set of key facts and FAQs[2]. The aims of the campaign are to:
    - achieve an overall increase in funding for local government in next year’s Spending Review;
    - ensure funding for children’s services, adult social care and homelessness that matches the scale of demand from residents;
    - target investment in value-for-money local government services – by setting out he investment case for local government; and
    - make the case for reform and devolution of local taxes.

14. A further briefing was published on 17 January, specifically aimed at engaging the business community to ensure they are aware of our lobbying messages and to seek support for the common issues on which to lobby government ahead of the Spending Review, for example through joint documents, letters, or Ministerial meetings.

15. The briefing, titled “Investing in the future: Protecting London’s Economy”[3], was launched at an event with London First attended by London Councils’ senior officers, Executive members and London First members. It focused on the potential threats to London’s economy if austerity continues in the 2019 Spending Review, calling for London’s local public services to be put on a sustainable financial footing. In particular, it called for London’s housing crisis, creaking transport infrastructure and significant skills gaps to be addressed to safeguard not only London’s economy but the UK’s.

16. The next briefing in the campaign, aimed at engaging voluntary and community sector partners, will be launched at a joint event on 20 February at The Guildhall with London Funders. The aim is to raise awareness of the Spending Review and its importance to London and Londoners, develop a coalition between the voluntary sector and boroughs to influence the Review, and share ideas on how we can best work together to meet Londoners needs.

17. Further briefings will be published at regular intervals between now and the Spending Review on key service areas including: children’s service; adult social care; housing; transport; and criminal justice.

[2] https://www.londoncouncils.gov.uk/download/file/fid/23689
[3] https://www.londoncouncils.gov.uk/investing/business

18. On 14 February the Chair of London Councils is attending a meeting of the Mayor of London and other combined authority Mayors, which will provide an opportunity to raise further awareness of the overall Spending Review campaign messaging, with a particular focus on the role of urban areas. It will also represent an opportunity to develop alliances with regard to the distributional impact of the Fair Funding Review.

Fair Funding Review update

19. The Fair Funding Review, will set new funding baselines for all local authorities from 2020-21 onwards, determining the distribution of an estimated £20 billion across England. The Government published its second consultation on the Review in December 2018. As expected, the Government has used the consultation document to outline its leading options for the structure of the relative needs assessment, covering the suggested funding formulae, the likely cost drivers, and techniques used to weight cost drivers and its preferred approach to the Area Cost Adjustment. It also sets out how the approach to relative resources deduction could be calculated, and high-level principles for transition to the new baselines.

<u>Relative Need</u>

20. With regard to relative need, the consultation proposes an overall structure of the Relative Needs Formula that would include an overarching "foundation formula", split into upper and lower tier services, based only on a measure of population adjusted for area costs. Measures of deprivation and rurality, which had previously been considered to be part of the overall formula, are not proposed to be included. Seven service-specific relative needs formulae are proposed, in addition to the foundation formula (see Figure 3 below).

Figure 3 – proposed structure of the relative needs formula

RELATIVE NEED FORMULAS		SHIRE AREAS			METROPOLITAN AREAS	LONDON	OTHER
		Unitaries	Counties	Districts	Metropolitan Districts	London boroughs	Fire authorities[4]
Foundation Formula	Upper tier	●	●		●	●	
	Lower tier	●		●	●	●	
1) Adult Social Care		●	●		●	●	
2) Children and Young People's Services		●	●		●	●	
3) Public Health		●	●		●	●	
4) Highways Maintenance		●	●		●	●	
5) Fire & Rescue[5]		●	●				●
6) Legacy Capital Finance		●	●	●	●	●	●
7) Flood Defence and Coastal Protection		●		●	●	●	

21. It also proposes that the Area Cost Adjustment includes additional factors reflecting travel times and remoteness, to reflect the variation in the cost of some inputs due to the size of local markets or isolation from major markets. Both are likely to disbenefit London boroughs.

Relative Resources

22. With regard to how to measure relative resources, the consultation proposes using a notional council tax level rather than actual council tax levels. It does not, however, indicate the Government's preferred notional level of council tax. It is proposed that this would be multiplied by a measure of council tax base, including treatment of discounts, exemptions, premiums and local council tax support. The Government proposes to adjust in full for all mandatory discounts, exemptions and premiums, including the pension age element of local council tax support and is consulting on how to treat discretionary discounts and premiums. The consultation asks for views on how to adjust for the working-age element of council tax support, given its mixed mandatory/discretionary nature. It also seeks views on how to take council tax collection rates into account in the resources adjustment and whether to project changes in the council tax base over a number of future years.

23. The Government is minded not to include an assessment of fees and charges in the resources deduction, but is still considering whether to adjust specifically for parking income. Again this would likely disbenefit London boroughs who generated over £650 million (41 per cent of the national total) in parking fees and charges income in 2017-18, and is statutorily ring-fenced to be spent on highways and transport.

Transition

24. With regard to transition - the Government has set out the overarching principles for transitioning to the new baselines (that they ensure stability, transparency, are time limited, and offer a degree of flexibility), and has indicated that the baselines from which the funding will transition should be "a measure of funding in 2019-20", but has not specified a preferred measure, instead it is asking for views on which measure would be appropriate.

25. As yet, it is unclear what the impact of the specific proposals in the consultation will be on London boroughs, but there are some areas of particular concern that suggest the review might result in funding being moved from London to other parts of the county – notably to shire counties.

London Councils' response

26. London Councils' consultation response is likely to raise a number of these concerns. Whilst not an exhaustive list, the key lines that are likely to be developed include:

- The need for sufficient funding for the system overall from the Spending Review.
- Disagreement that the review must be fiscally neutral, in line with the LGA's "levelling up" proposals that no authority receives less funding than the current system by using the remaining 25 per cent of business rates.
- Concern over the lack of progress of the review since the last consultation, and lack of indication of the potential scale of the impact of the proposals on funding levels, with less than a year until implementation.
- Concern about the potential undercounting within ONS population projections (while welcoming the overall principle of using projections over static figures).
- Significant concern about the proposal not to include deprivation within the foundation formula, which means that around 30 per cent of London boroughs' funding within the formula will not have any deprivation factor.
- Concern about the omission of a service-specific formula for homelessness, and the inference that, as it will be funded through the foundation formula, levels of homelessness are not linked to deprivation.
- Concern about the omission of a service-specific formula for concessionary fares as London spends over £300 million per annum (around 30 per cent of the national total) on this – but has only 16 per cent of the population that would be the main driver of the foundation formula.
- Concern about the omission of specific formulae to reflect the disproportionate cost borne by London boroughs of Unaccompanied Asylum Seeking Children (UASC) and people with No Recourse to Public Funds (NRPF). London boroughs spend a combined £100 million in these two areas each year, while local government *as a whole* spends only around £90 million on flooding and coastal defences, both of which have their own separate formulae under the proposals.
- Concern about the evidence base for the inclusion of journey times and remoteness within the ACA, which will likely have the impact of "watering down" the benefit of the ACA to London boroughs.

- Concern about the exclusion of residential property costs from the ACA (were homelessness not to have its own specific formula) which partly drive the higher costs of housing the homeless through temporary accommodation.
- Concern over the lack of detail about the notional council tax level or its potential distributional impact.
- Concern about the potential implications of using a notional council tax level for low council tax areas – specifically highlighting the need for fundamental reform of the tax and calling for the removal of the council tax referendum limit which prevents these areas from ever "catching up" to a notional average.
- Concern about the proposal to consider the inclusion of parking fees and charges income within the measure of local resources, highlighting that this funding is statutorily ring-fenced to be spent on highways and transport, and that this would add further complexity to the formula.
- Concern about the lack of detail on the proposals for transition (although indicating general support for the principles), and specifically the lack of indication over the proposed length of the reset period.

Next steps

27. London Councils will respond to the consultation by the deadline of 21 February. Sign off will be via Group Leaders. A draft officer response will be circulated to boroughs in early February to ensure alignment of key messages.

28. A set of common lobbying lines on the Review will be sent to all boroughs for inclusion alongside any individual lobbying points when engaging with any print or broadcast media on the Fair Funding Review.

29. A briefing will be sent to all London MPs setting out the main lobbying lines. This follows a meeting of the Chair and Chief Executive of London Councils with the Chairs of the London APPG on 17 January which discussed how London MPs could be more widely engaged on these issues to support London Councils' lobbying.

30. The launch of the "Investing in the future" has signalled a phase of more active campaigning and media activity with regard to funding. This will include building stronger alliances with other areas of the country on particular issues, most notably (but not

exclusively) with other major urban areas. The meeting with the Mayor and other CA mayors on the 14 February represents an opportunity to do this.

75 per cent Business Rates Retention

31. Alongside the provisional finance settlement and Fair Funding consultation, the Government published its third consultation since 2016 on further business rates retention[4]. It sets out more detail about the parameters of the 75 per cent business rates retention scheme that will begin in April 2020. The consultation covers three broad areas:
    - The balance of risk and reward
    - Proposals for simplifying the system and reducing volatility
    - Setting up the system.

The balance of risk and reward

32. The consultation indicates that the reset of the system in 2020 will be a full or "hard" reset in which business rates baselines will be recalculated and any growth that authorities had accumulated since 2013-14 (the last reset) will be removed. Thereafter, it sets out options for a either a phased or partial reset (the latter is seen as the most desirable option) where authorities retain growth for a number of years rather than experiencing a sharp "cliff edge" of a full reset. It does not specify preferences for the length of the reset period but suggests that full resets should be kept as an option perhaps once every fifteen years.

33. The consultation indicates that the government expects a 'simple' safety net to continue, without taking account of the position over more than one year. It does not specify a level but notes that the 75 per cent pilots will use a level that is 95 per cent of baseline funding.

34. With regard to the levy on growth, the Government had previously planned to remove this under the original 100 per cent retention plans, but notes this would require primary legislation. It therefore proposes to continue to have a levy on "extraordinary growth", and seeks views
on what level should be regarded as extraordinary. The examples it gives are 100 per cent, 150 per cent, 200 per cent and 250 per cent of baseline funding.

35. The consultation proposes to allow two tier areas to be able to decide their own retention splits but indicates that some sort of default level would be required where local

[4] Available here: https://www.gov.uk/government/consultations/business-rates-retention-reform

agreement cannot be reached. The tier split in London between boroughs and the GLA will continue to be determined separately in consultation with London authorities.

36. The Government view is that business rates pools are a desirable element of the system and allow better planning and decision making and a joint approach. The consultation asks for views on how to incentivise pooling, but it includes no specific suggestions.

Proposals for simplifying the system and reducing volatility

37. With regard to the movement of properties between the central and local lists, the Government has ruled out placing hereditaments on the central list purely based on risk. It no longer mentions “area lists” (an idea which previously only London had expressed an interest for).

38. The consultation reaffirms the Government’s commitment to address the issue of the impact of appeals on council budgets. It sets out four options which have been considered but ruled out due to a number of issues including complexity and being counter to legally required accounting practice. The consultation proposes a new approach to the administration of the system which it is calling “the alternative approach” – and regards this as the only viable method of addressing the volatility caused by appeals.

39. In short, the proposal seeks to simplify the retention scheme by separating out the baseline element from the calculation of any growth reward. The impact of appeals would be removed by having “floating” tariffs and top-ups, that would change every year rather than being fixed. Certainty is to be provided by ensuring that authorities receive their income, net of provisions for appeals, equal to their needs assessment plus or minus any growth or decline in business rates and the safety net and levy. The Government states that under this alternative system local authorities would still keep 75 per cent of growth in business rates. Appendix A sets out how the system would work in detail and how it differs from the current system.

Setting up the system

40. This consultation also covers how the business rate baseline would be set if the alternative system is not adopted and business rates retention continues to operate as it does now with fixed tariffs and top ups. It proposes baselines would be based on 2018-19 outturn returns (known as NNDR3s) uprated by inflation, as 2019-20 NNDR3s would not

be available, with averages for appeals and non-collection. It seeks views on how to adjust baselines for appeals provisions.

London Councils' response

41. London Councils' response is likely to:

- Reiterate London Government's long-term ambitions for London to retain 100 per cent of its business rates in future, and disappointment that the new scheme is only 75 per cent.
- Support the LGA view that the remaining 25 per cent of business rates be returned to local government, emphasising the need for transparency in this process.
- Raise concerns over the long- term sustainability of business rates as suitable tax to fund local government.
- Broadly welcome attempts to reduce the "cliff edge" caused by resets and indicate general support for the idea of phased resets which seem to eliminate this completely– but with the need for more illustration of the impact on authorities.
- Raise concern about the impact of a "hard reset" in 2020 - which could cause significant volatility for a number of boroughs – and call for further clarity about any transition to new business rates baselines.
- Express disappointment that the levy on growth will remain and ask for more illustration of the distributional impact of the relative proposals for the new levy on "extraordinary growth".
- Welcome the commitment to pooling but stress the need for it to have financial benefit, suggesting there is no reason that pools couldn't retain more than 75 per cent (as with the pilots in current system).
- Offer suggestions as to how pooling can be incentivised under the 75 per cent scheme – emphasising London's track record of successfully working together and our willingness to continue to develop a London business rates retention system.
- Welcome attempts to simplify the system.
- Welcome the commitment to reducing volatility through removing the impact of appeals, but continue to raise concerns about the current performance of the VOA.
- Broadly welcome the proposed alternative model – while recognising it does not eliminate volatility or complexity completely and call for further reassurances that

the reward element will remain linked to genuine growth and not changed in future by government.

Next Steps

42. London Councils will respond to the consultation by 21 February. Sign off will be via Group Leaders. A draft officer response will be circulated to boroughs in early February to ensure alignment with key messages.

43. Civil servants have indicated a further consultation is planned prior to the summer parliamentary recess to bring both sides of the system together into one set of proposals encompassing the Fair Funding Review and 75 per cent business rates retention. They have intimated that this could include illustrative indications of distributions at the individual authority level. Whether these will be indicative allocations depends on the timing of the Spending Review which would determine the overall spending control total.

Recommendations

44. Leaders' Committee is as asked to:
    - note the progress on finance lobbying with respect to the key events outlined in the report; and
    - consider and endorse the proposed key lines in response to the current consultations on the Fair Funding Review and 75 per cent business rates retention.

Financial Implications for London Councils

None

Legal Implications for London Councils

None

Equalities Implications for London Councils

None

Appendix A – The proposed alterative approach to 75 per cent Business Rates Retention

The table below summarises the similarities and differences between the current system in terms of how it would be likely to operate from April 2020 and the alternative system.

	Current system	**Alternative system**
Business Rates baseline	Top down system based local authorities share of the amount expected to be collected nationally less national provision for appeals	Business rates to be collected for the year as estimated annually by each authority
Funding baseline	Based on the outcome of the Fair Funding Review including relative needs, relative resources and transition	Based on the outcome of the Fair Funding Review including relative needs, relative resources and transition
Top-up / tariff	Business rates baseline less funding baseline Fixed between resets other than being uprated by inflation every year	Business rates baseline less funding baseline revised each year based on each authority's assessment of business rates collectable plus/minus growth or decline in business rates, the safety net and levy
Safety Net and levy	Applied according to rules and paid separately	No change to the way safety net and levy would work – but any payments would be included in top/up tariff
Treatment of appeals	Provisions for appeals reduces retained business rates growth	Provisions for appeals does not reduce retained business rates growth although actual payment for appeals does
Business rates growth retention gain / decline	75 per cent of difference between actual business rates collected and business rates baseline as adjusted by top-up/tariff and levy/safety net. Need to provide for appeals can reduce benefit of growth retained	75 per cent of difference between actual business rates and estimated business rates baseline (both adjusted to take out the effect of appeals provisions) as adjusted by top-up/tariff and levy/safety net. Need to provide for appeals is taken into account in calculation of top-up /tariff so does not impact on growth retained