Discussion 1:
The progress of the Fair Funding Review
Fair Funding Review – overview and terms of reference

The Government will implement a fair and stable approach to allocating business rates under 100% business rates retention…

…reflecting both relative need and resources and providing support for key services for all authorities.

• The Fair Funding Review will set new funding baselines for every authority alongside the introduction of 100% business rate retention in 2019-20.

• It will not consider the overall quantum of funding available for local government which is a matter for the Spending Review. With the introduction of 100% business rates retention will be an estimated £25 billion of business rates available to the sector in 2019-20.

• It will design a needs assessment methodology in support of these wider reforms, replacing the current approach which was designed over 10 years ago and has not been updated since 2013: there have since been demographic and other changes.

• The Review will consider how the relative needs and resources of local authorities should be assessed in a world where local government spending is driven by local resources, not central grant, looking again at the factors that drive costs.

• The Review will produce solutions that are sustainable for the duration of a reset period (“future-proofed”) for every council. It will also define appropriate transitional arrangements.

• It will focus initially on the services currently funded through the settlement, considering new grants such as the Public Health Grant on a case-by-case basis.
The Government has heard the response to the Call for Evidence. The new needs assessment methodology will be guided by the following:

**Principles of the Review**

- **Incentivise growth** — to support the reforms around 100% business rates retention and help councils grow their local economies
- **Simplicity** — an opportunity to identify the most important factors that drive need to spend
- **Transparency** — for councils and the public to understand local allocations
- **Contemporary** — using the most up-to-date data available
- **Sustainability** — an evidence-based approach to respond to current and future demand
- **Stability** — including transitional arrangements and alignment with multi-year settlements
- **Speed** — work to deliver optimal solution in 2019/20

**Measuring need**

- A less complex methodology
- Focused on up to date key cost drivers
- That reflects ‘future need’ as well

**Treatment of resources**

- A more transparent approach
- That does not undermine the growth incentive

**Approach to transition**

- Minimises losses in year one
- Provides a clear path to the target allocations
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<tr>
<th>Year</th>
<th>Event</th>
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<tr>
<td>April 2016</td>
<td>A local government Technical Working Group is established, co-chaired by DCLG and LGA</td>
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<td>July 2016</td>
<td>A call for evidence was published yielding 209 responses to questions ranging across the scope of the Review</td>
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<td>Spring 2017</td>
<td>A consultation on how to measure need will be published along with a response to the call for evidence</td>
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<td>From Spring 2017</td>
<td>A series of technical papers will be published on other areas within the scope of the Review i.e. how to take into account relative resources; transition; new responsibilities as well as further papers on measuring need</td>
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<td>Spring 2018</td>
<td>Second consultation on approach to measuring need and resources</td>
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<tr>
<td>Autumn 2018</td>
<td>Transition arrangements and baseline allocations confirmed – provisional 2019-20 Local Government Finance Settlement consultation</td>
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<tr>
<td>April 2019</td>
<td>The new needs assessment methodology is implemented</td>
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Context – how funding is allocated at settlements today
Measuring relative need is a part of the 4-block model

The use of formulas to measure relative need can be traced back to the nineteenth century…

• … though were based on a large degree of judgement. Since the 1970s computers have allowed statistical analysis to offer a more objective way of constructing funding formulas.

• Funding formulas have become increasingly complicated in an attempt to capture the many factors believed to influence need. The current system has 15 formulas with over 120 indicators – as well as 17 other formulas with bespoke distributions for grants which have been rolled in over the last seven years.

• Measuring relative need is one part of the 4-block model, which was introduced in 2006/07 and is still the basis of today’s allocation. In addition to the positive relative need sum, the model includes the following blocks:

  • A negative Relative Resource sum reduces a council’s allocation by taking into account their relative ability to raise council tax

  • A positive Central Allocation sum is allocated to each authority on a per head basis based on an average minimum calculation of need and resources

  • Finally, a Floor Damping block adds or removes funding to ensure that all authorities receive at least the ‘floor’ percentage change occurring each year: this occurs separately for four groups of authority (PSS, police, fire, shire districts).
Context - measuring relative need
How funding formulas work in more detail

Socio-economic and demographic factors which are predictive of the cost of delivering services form variables in these funding formulas...

• … for example the adult social care relative needs formula includes variables that reflect the number of older people, while the formula for highways maintenance includes variables which measure road length and usage.

• The formulas allocate proportionally more money to areas where data indicates they have relatively more older people, relatively more roads, etc.

• For most services there is more than one indicator of ‘need to spend’. For example the adult social care formula reflects the number of older people in an area, the number of older people with complex health problems and the wealth of those older people.

• Once cost drivers are determined, statistical techniques provide an evidenced-based approach to determine the weightings of each variable. They can also be used to determine which variables to use in the first place. Expenditure-based regression models are the most widely used technique across Government, removing the level of judgement in funding formulas.
  o The consultation aims to outline some of the techniques available and seek feedback.

• As reflected in the 4-block model, a needs assessment must also take into account councils’ varying resources and the pace at which authorities are moved to the new allocations. These are also issues for the Fair Funding Review.
Measuring need is the focus of the next consultation
The Government will explore moving to a single formula

It may be possible to move to a single formula based on common cost drivers:

- A large degree of variance in funding allocation across local government using the current formulas can be explained by population, and there are significant overlaps between many of the other variables.

- This suggests it may be possible to simplify the needs assessment to a single formula that will be easier to understand, however there may be areas where a more specific approach may be required: high cost areas (Social Care) or services of a distinct nature (Highways Maintenance) may not fit in a single formula.

- The proposal is to explore using a single formula based on common cost drivers, by comparing it against an approach which uses multiple specific formulas to assess the impact of simplifying the needs assessment.

- The consultation aims to receive feedback on this approach and the cost drivers that should be considered.

- The Government’s analytical plan between now and 2019 will continue to shortlist and refine options for measuring need and resources (into which response to the consultation will feed-in) and consider other issues such as how frequently “need” changes and what Area Cost Adjustments may be required.
Getting the right cost drivers
The variables in the funding formula need to be the right ones

Criteria for cost drivers

- Relevant – with evidence to show that it has a significant impact on the cost of providing services
- Objective – measurable using robust data that is collected on a consistent basis across England
- Distinct – must explain a good degree of unique variation in the need to spend and not overlap
- Stable – should not exhibit unpredictable or large changes year on year
- Future proof – expected to drive the ongoing costs of providing services; not one-off events.

Common cost drivers

Although specific cost drivers may be required in particular approaches for certain services, the Government has identified 3 cross cutting cost drivers:

- Population – the number of people to provide services for is universally identified as the single most important predictor of costs, although it is often necessary to distinguish subsets
- Sparsity – determining how the cost of providing different services varies in rural or urban areas is a very sensitive issue
- Deprivation – past funding formulas reflect the tendency that areas with income deprived individuals are more likely to access certain services
Grants being rolled into 100% BRR

A number of grants will be rolled into the settlement to make the move to 100% business rates retention fiscally neutral.

The Fair Funding Review will focus initially on how to measure need for services currently funded through the settlement...

- …and will turn to new responsibilities on a case-by-case basis thereafter.

- So far, the Government has announced that Revenue Support Grant, Rural Services Delivery Grant, Public Health Grant and the Greater London Authority Transport Grant are to be funded through retained business rates from 2019-20 onwards.

- There are three broad approaches to take towards these grants:
  
  - **Become part of the new formula.** This will likely result in a significant change from the grant’s current distribution.
  
  - **Include in the assessment but with a bespoke needs based formula.** This will mean the funding is distributed according to the specific need it is designed to address but would still be different from the current distribution.
  
  - ** Maintain the existing distribution.** This may be appropriate in some circumstances and may help the overall transition to the new system.

- The consultation aims to receive feedback on the different approaches.
Structure of work
The Fair Funding Review is split into 3 broad work streams

Measuring need has been the main focus, but there are two equally important strands…

• **Resources:**
  • As mentioned earlier in the presentation, and as evident in the current settlement distribution methodology, the assessment of the relative resources of local authorities is just as important as that for relative need.
  • There are different ways to take council tax into account. Other resources such as fees and charges will also be considered.

• **Transition:**
  • A new methodology and demographic changes could introduce discontinuities. There is a question over how new allocations are implemented.
  • The Review must also design an approach to ‘needs resets’ which is compatible with the design of the new system.

The Government will publish **a series of technical papers** between now and the completion of the Review. These will set out the options the Government is considering for the above work streams as well as updates on the approach to measuring need and other areas, like how to structure funding formulas between tiers of government, or Area Cost Adjustments.
Local Government Engagement

As well as through formal consultation, the Government will continue to engage directly…

…with a wide range of stakeholders across Whitehall and externally who will help to shape and progress this review, including foremost from within Local Government:

- The Needs and Resources Technical Working Group is co-chaired by DCLG and the LGA and is attended by representatives from across the country, including…:

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<tr>
<td>DCN</td>
<td>Sally Marshall (Dacorum)</td>
<td>CCN</td>
<td>Dave Shipton (Kent)</td>
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<td>SIGOMA</td>
<td>Geoff Winterbottom</td>
<td>SMT</td>
<td>Nikki Bishop (Trafford)</td>
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<td>RSN</td>
<td>Dan Bates</td>
<td>SCT</td>
<td>Sean Pearce (Worcs.) / Chris Tambini (Leics.)</td>
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<td>North East CA</td>
<td>Paul Woods</td>
<td>SLT</td>
<td>Duncan Whitfield (Southwark)</td>
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<td>SUT</td>
<td>Alan Cross (Reading)</td>
<td>GLA</td>
<td>Martin Mitchell</td>
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- The Government is also further engaging with individual local authorities to discuss the key issues including what drives costs and how the Government might incentivise and reward outcomes.
Recap – Fair Funding Review next steps

- Publish a response to the call for evidence along with a technical consultation on measuring need which looks at how to structure a needs assessment, cost drivers, statistical techniques and approaches to new responsibilities rolling into the settlement.

- Direct engagement with local government, Other Government Departments, academics and other parties to help shape the analytical approach.

- Publish a series of technical papers including on the Review’s approach to the treatment of council tax and other resources, and on transitional arrangements.