

# Fair Funding Review Away Day

27 November 2017

# Agenda

Time	Session
11 40	Introductions
11 55	Plenary session: Overall progress update
12 40	Lunch
	<u>Parallel Workshop 1</u>
	Relative resources <u>OR</u>
13 30	Design of the relative needs assessment
	<u>Parallel Workshop 2</u>
14 35	See above
15 40	Refreshments
16 00	Workshop feedback, common themes, differences
16 45	Wrap-up
16 50	End

# Fair Funding Review Away Day

Progress update

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# Fair Funding Review: objectives / terms of reference

## The Fair Funding Review will...

- Set new **funding baselines** for local authorities in England
- Replace the **current methodology** which is considered **out-of-date and complex**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 distributing funding for services currently funded through the settlement
- Be developed through close collaboration with local government

# Fair Funding Review principles and the structure of our work

## Principles of the Review

- **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
- **Robustness** - taking into account the best possible objective analysis
- **Stability** - including transitional arrangements and alignment with multi-year settlements



## Measuring relative need

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

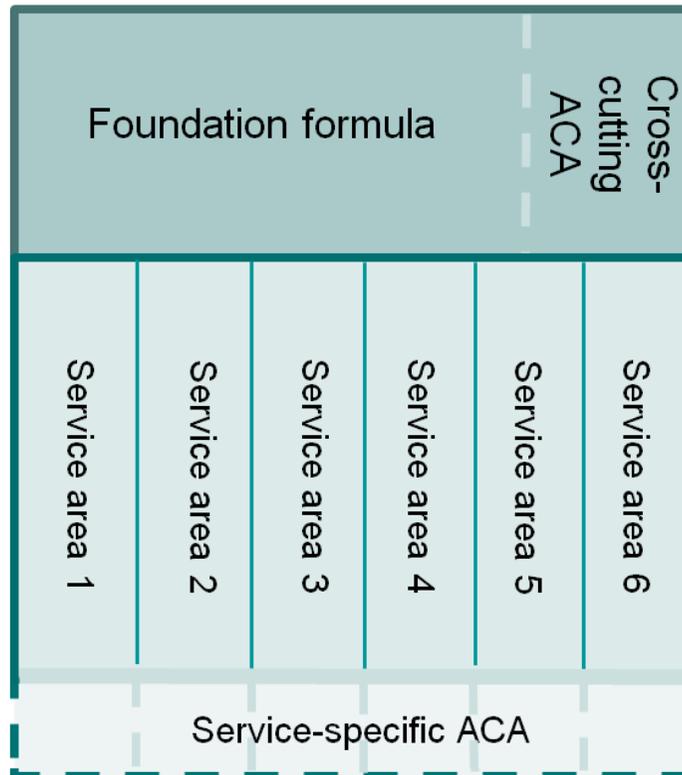
## Treatment of resources

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

## Approach to transition

- Avoids unmanageable changes in allocations
- Provides a clear path to the target allocations

# Two primary models under consideration



This diagram depicts a potential relative needs assessment approach which incorporates a foundation formula approach along with several service specific formulas, and both a service-specific and cross-cutting Area Cost Adjustment (ACA). (The diagram is for illustrative purposes and no inference should be drawn from the size of individual block elements)

# Taking area costs into account, including rurality

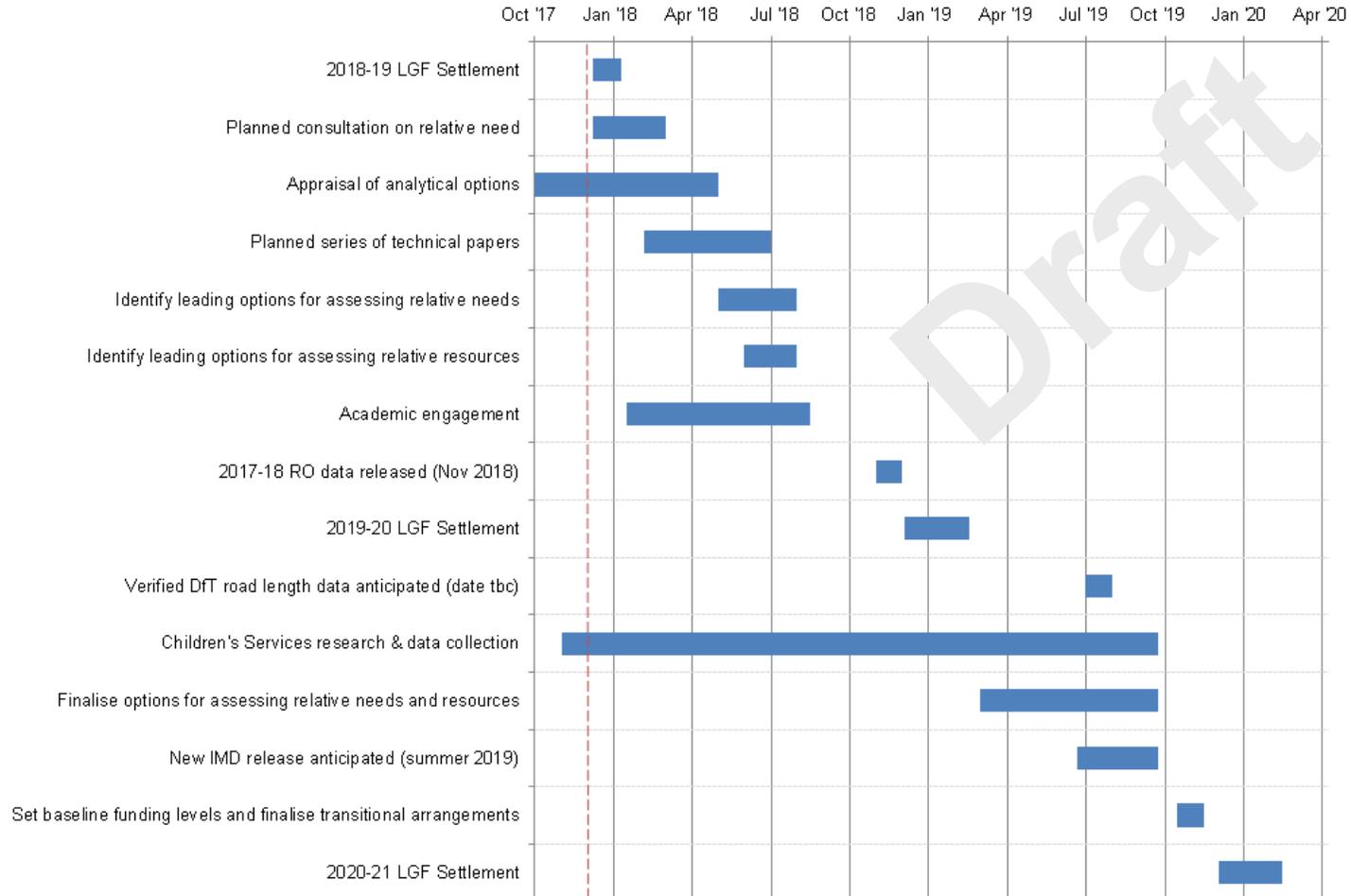


- The **cost of providing the same set of public services** varies between local authorities for a number of reasons – including the costs of inputs. Area Cost Adjustments (ACA) account for this.
- There are a number of **candidate inputs** to consider e.g. labour costs, business rates, other non-labour expenditure. Those included must meet key criteria: significance, variation, data availability and avoiding perverse incentives.
- We also need to settle the **geography** of the ACA (e.g. 1991 county level or upper tier).
- Additional unit costs in service delivery faced by **rural areas** (and perhaps coastal areas and islands) could be reflected in the ACA. This requires a measure of rurality (e.g. sparsity or journey times) and a method of relating this measure to the cost of delivering services.
- We then need to **weight** the various factors involved.

- **Relative levels of deprivation** are a crucial determinant of ‘need’ for many services.
- At present, deprivation is generally included as a ‘top-up’ within RNF formulas.
- Deprivation should be considered an **additive cost driver** (i.e. a variable that determines the number of services provided), as opposed to a multiplicative cost-adjustment (whereby deprivation increases the cost of delivering services).
- As such, deprivation is treated as a **cost driver** within one or more RNFs.
- The **Index of Multiple Deprivation** (IMD) is a good candidate for assessing local authority deprivation in the FFR.
- We then need to **weight** the cost drivers involved.

- The Review will examine how council tax should be taken into account when redistributing business rates at local government finance settlements, and will also consider other sources of income.
- In particular, it will consider:
  - the varying levels and capability of local authorities to raise council tax,
  - the effects of council tax discounts, from nationally set exemptions (e.g. students) to those with local discretion (e.g. LCTS),
  - how net expenditure is used, and how to take account of sales, fees and charges (e.g. parking revenue), and
  - and the equity and incentive effects of the various options.

# Potential timeline working towards 2020/21 (subject to final decisions and ongoing review)



# Planned consultation and research on CSC relative need

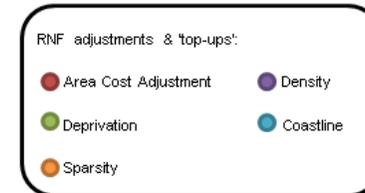
- We are currently progressing a technical consultation on relative need, based on input from the technical working group. This is an important milestone, providing the framework for our future work and further collaboration with the sector.
- We envisage that the consultation will include the following key areas:
  - An overview of funding formulas, including potential future approaches, and the Review's criteria for considering cost drivers,
  - The 'common cost drivers' for local government that have been identified so far through earlier engagement with the group and wider sector,
  - The potential 'service specific cost drivers' for local government that have also been identified, and
  - The potential statistical methodologies that could be used to 'weight' funding formulas and cost drivers.
- Planned DfE/DCLG research project to develop an improved understanding of the drivers of need within the sector and collect data on cost pressures for Children's Services at a low geographical level.

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Design of the relative needs  
assessment



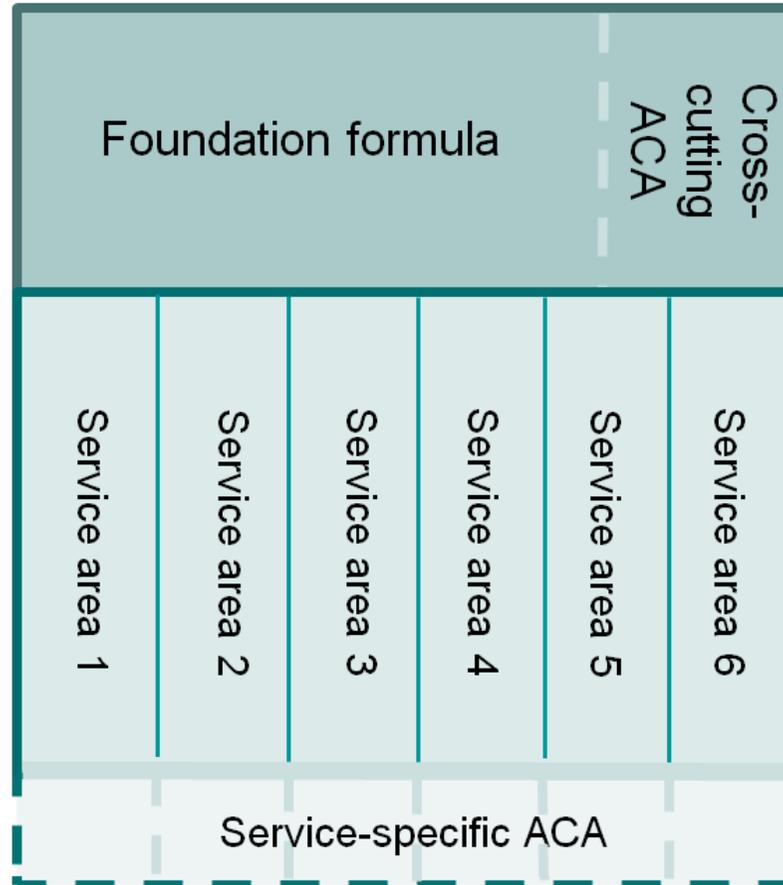
At present, 15 relative need formulas and several tailored distributions for services previously supported by specific grants are used to determine annual funding allocations for each local authority across England.



These formulas involve over 120 indicators of 'need', reflecting factors previously identified as driving the costs of service delivery.

- A key principle of the Review is to work towards simplification.
- Foundation formula using common cost drivers?
- Potential service-specific formulas:
  - Adult social care
  - Children’s services
  - Highways maintenance and public transport
  - Waste collection and disposal
  - Fire and rescue services
  - Legacy capital financing
  - Others?

# Type and number of formulas



## Relevant

- there should be evidence to demonstrate that the cost driver has a significant impact on the cost of providing services

## Objective

- the cost driver should be measurable using robust, up-to-date data that is collected on a consistent basis across England. Local authorities should not be able to directly affect the indicator (i.e. the cost drivers should not create perverse incentives to 'game' the system)

## Distinct

- the cost driver should explain significant variation in the 'need to spend' that is not covered by another cost driver

## Stable

- the cost driver should not exhibit unpredictable or large changes year-on-year

## Future proof

- the cost driver should be expected to drive the ongoing costs of providing services (i.e. they should not be one-off events)

- Population
- Deprivation
- Rurality/density
- Road length (adjusted?)
  
- Area Costs?
- Others?

## Weighting cost drivers within formulas to determine their relative importance:

- Expenditure based regression at LA level
- Multi-level modelling
- Other? (Judgement?)

## Weighting of formulas, tiers:

- Current spend ratios?
- Other?

- Should the Government continue to explore the concept of a foundation formula combining common cost drivers?
- What service-specific formulas should there be? How should they be weighted against one another?
- What cost drivers could be examined for all the formulas identified?

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Assessing relative resources

- Council tax income varies widely across England.
- As well as factors over which councils have little or no control, local decisions also determine council tax income. This includes, for example, the Band D level set, or discretionary discounts.
- This means local decisions or factors outside the local authority's control could influence settlement allocations.
- Historically, when setting baselines, the Government has used a 'notional' approach to council tax levels.

## Scenario 1:

### No account of CT resource

- The 2017-18 settlement distributed £241m of adult social care support grant using the Adult Social Care relative needs formula (RNF)
- This distribution made **no** allowance for the size of an authority's council tax resources – neither base nor Band D level.
- Such a system would benefit those areas with high levels of council tax income relative to their need.

## Scenario 2:

### Account for potential CT resource

- At the 2013-14 Settlement, it was assumed local authorities treated discretionary discounts in the same way and set the same Band D.
- Funding baselines were set so that the total of business rates and a notional council tax measure were allocated to follow the same distribution of need.
- Such a system accounts for potential local authority CT resources. This will be explored in later slides.

## Scenario 3:

### Full account CT of resource

- Settlement Core Funding was introduced in 2016-17 – a methodology which reduced an LA's business rates, RSG and council tax income (as measured in 2015) by a set percentage.
- The iBCF methodology also uses potential actual income to distribute funds.
- Such funding systems take full account of the size of an authority's council tax resources, including the actual Band D levels set.
- This benefits those areas with low council tax relative to their need.

# Council tax assessment - deprivation



- Deprivation will be reflected through relative need in the Fair Funding Review. It also interacts with the tax base.
- Deprived areas typically have a higher proportion of low band properties. They also typically have a higher proportion of dwellings eligible for council tax exemptions.
- These combined factors mean deprived areas typically have a low tax base when compared to the number of dwellings.
- Deprived areas also typically have a high need per person, as recognised by the current RNFs.

# Other income from fees and charges



- Sales, Fees and Charges (SFC) allow authorities to recoup part or full cost of a service provided. They provide a means of more specific and directed charging than council tax.
- SFC are not currently accounted for as a measure of authorities' resources in the same way as council tax. However, SFC are taken into account in the net revenue value used in expenditure based regressions.
- The Review is considering whether it is appropriate to continue to take account of SFC income as currently measured, and the implications of alternative approaches such as whether there should be no measure of SFC at all, or whether SFC should be factored in an LA-level relative resource adjustment.

The main issues associated with building a resources adjustment into a settlement allocation methodology which incorporates SFC are identified as:

- SFC is a multi-faceted source of income over which **councils have discretion**
- The income and **data sources** which map it must be stable and robust
- There are **different ways to factor SFC income** in a settlement methodology
- Availability of income and **ring-fencing**

- Should there be an assessment of relative council tax?
- On what basis should the assessment of relative council tax be made? Actual, notional, something in-between?
- Should the Review assess relative income from other sources?  
On what basis?
  - Fees & Charges
  - Investment income
  - Other income