Ministry of Housing, Communities & Local Government

Title:	Technical Working Group
Paper:	**NR TWG 18/03 Summary of potential analytical options**
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POLICY DEVELOPMENT: NOT A STATEMENT OF GOVERNMENT POLICY

Introduction

1) This paper summarises an appraisal of the analytical options for assessing the relative need of local authorities in relation to several specific service areas.

2) For each service area, the Ministry of Housing, Communities and Local Government (MHCLG) has identified a 'short list' of feasible analytical options that will be the focus of initial analytical work. We would welcome feedback on these options which will be used to inform the work of the review and considered alongside the responses we receive through our current consultation on relative needs.

Background

3) A 12-week consultation on the assessment of relative needs was published on 19 December, which sets out the Government's approach to the fair funding review of relative needs and resources and seeks wider views on what factors should be included in a new funding formula, or formulas.

4) The consultation considers the potential structure of the needs assessment and the merits of simplicity and complexity. This is an important consideration for the review because, whilst the Government is committed to implementing an approach with enhanced levels of simplicity and transparency, it recognises that this should not be achieved at the expense of accuracy and fairness.

5) The consultation paper therefore proposes an approach that begins with a transparent foundation formula based on a small number of common cost drivers to allocate all, or at least a proportion, of the available funding to each type of local authority. However, as there may be specific service areas where a more sophisticated approach is required, we are also considering the case for going further and allocating a proportion of the available funding based on the particular cost drivers for those services.

6) The potential services that may require such an approach are outlined in Chapter 4 of the consultation where we invite views, supported by evidence, on whether these are the most appropriate service areas, and what the most important 'service specific cost drivers' might be. The potential service areas are as follows:

- Adult social care,
- Children's services,
- Highways maintenance and public transport,
- Waste collection and disposal,
- Fire and rescue services, and
- Legacy capital financing.

7) Given that even a foundation formula is likely to reflect more than one cost driver, Chapter 5 of the consultation then considers potential analytical approaches to determining the relative importance (or weighting) of different cost drivers within a formula.

Overview of analytical option appraisal

8) For each of the service areas discussed in the consultation document, MHCLG identified a 'long list' of potential analytical options which broadly consisted of changes in the data used in the current set of relative needs formulas (RNFs), and / or changes in the methodology used to measure local authority need.

9) The 'long list' was assessed by looking at the degree to which each option met the principles of the review (set out in Annex 1), and consideration was also given to practicalities, such as data availability. Even though the principles already cover some measures of analytical robustness, it was decided that options that would fail on a measure of analytical robustness should be excluded, regardless of whether they met the other principles.

10) For each of the service areas, a 'short list' of options was developed which will go on to be the focus of further analysis by the department. These include a 'do nothing' option and a 'do minimum' option, which were identified for each service area for comparison purposes. The former effectively maintains the status quo, whilst the latter would broadly consist of a data update to the underlying indicators and potentially updated formula.

11) The options MHCLG have shortlisted will form a starting point for further analytical work, in order to maintain the availability of a service-specific approach to a new relative needs assessment. However, these will not be the only options we consider; this will be determined by responses to the current consultation which includes a section on how to weight cost drivers and construct funding formulas, and by comments on this paper from the Technical Working Group.

Summary of 'short listed' analytical options

- A **'do nothing'** option represents the status quo and would mean a continuation of current service areas and RNFs with no update to the data or methodological changes. The table below summarises the current approach to assessing relative need for the service areas concerned.

Table 1 – Current approach to weighting cost drivers

RNF	Current treatment
Adult's Personal Social Services (adult social care)	Small area modelling approach
Children's Services	Multi-level modelling approach
Highways maintenance	Local authority level regression
Environmental, Protective and Cultural Services (includes waste services)	Judgement
Fire and Rescue	Local authority level regression

- A **'do minimum'** option represents a continuation of current service areas and RNFs but with an update, where possible, to the data currently used. It may also involve re-running regressions to derive new weightings (or coefficients) for the current set of cost drivers in a particular service area.

- As well as the above two options, at least one **additional analytical option** will be carried forward for further analysis and these vary by service area. These options are summarised in table 2:

Table 2 – Summary of initial analytical options carried forward for further analysis

Service area	Analytical options	Overview
Adult Social Care	1) Use the new 2012/13 Department of Health small-area based RNF with updated data. 2) Local authority level regression using 2016/17 Revenue Outturn expenditure data as a proxy for local authority need.	The new 2012/13 DH RNF uses a small-area regression methodology, which is similar to the existing 2005/06 RNF. The DH RNF employs regressions at lower level geographies (LSOA), on usage rather than spending and uses England-average cost weighting to reflect that some usage types cost more than others. An approach based on local authority level regressions would not account for the same level of variance as a multi-level approach because the RNF would only exploit variation between different councils rather than within each council area. However in this instance, an RNF using local authority level regressions could utilise more up-to-date expenditure data (potentially Revenue Outturn from 2016/17) than the DH RNF. Some demographic data (other than the population multiplier) would however still originate from the 2011 Census, and claimant data would also have to remain from 2013 due to the on-going rollout of Universal Credit.
Children's services	1) New multi-level modelling exercise to develop new coefficients for new cost drivers with respect to children's services. 2) Local authority level regression using 2016/17 Revenue Outturn expenditure data as a proxy for local authority need.	A multi-level model would use regression against past spending based on lower level geographies, which means that spend and service use data is collected at a LSOA level. As a result, key drivers can be used to explain variance of spend with cost drivers within a local authority, as well as between local authorities. MHCLG has recently commissioned a multi-level modelling study into children's services.

Service area	Analytical options	Overview
Highways maintenance and public transport	1) An option (with several sub-options) is to review the number of variables used in the current RNF, update the underlying data, and derive new weightings by undertaking a local authority level regression using 2016/17 Revenue Outturn expenditure data as a proxy for local authority need.	This option would involve changing some cost drivers to make better use of data sources and account for need more effectively. Examples of the existing variables being reviewed include the flow of all motor vehicles, population and snow/grit days. The sub-options relate to the treatment of concessionary travel and bus support. Both services could be maintained within an Environmental, Protective and Cultural Services (EPCS) RNF, or in a new foundation formula. Alternatively, given the overlap between relevant cost drivers, concessionary travel could be reflected with an adult social care RNF and bus support could potentially be included within any rurality adjustment within an Area Cost Adjustment (ACA). A further option is to combine highways maintenance, concessionary and bus support into a single highway maintenance and transport RNF.
Waste services	1) Local authority level regression using 2016/17 Revenue Outturn expenditure data as a proxy for local authority need. 2) A per capita or per household distribution which could also form part of a new foundation formula.	As waste is currently part of EPCS, there is no standalone 'do nothing' or 'do minimum' option for waste services. Several sub-options are being considered with respect to potential top-ups for flood defences, environmental agency levies and coastal protection. Including waste services within a foundation formula approach is also a potential option that is being carried forward for further analysis.

Service area	Overview
Fire and Rescue services	The National Fire Chiefs Council Fire Finance Coordination Committee is leading on the fire sector's input into the review. The Committee has commissioned analysis from the Police and Crime Commissioners Treasurers' Society's Technical Support Team, which will include an analysis of the current fire funding formula and consideration of possible new indicators. We intend to focus on this service area in more detail in May's technical working group meeting. In the meantime the analytical option that will be carried forward for further analysis is a new local authority level regression using 2016/17 Revenue Outturn expenditure. As a sub-option we will also consider the practicality, feasibility and analytical robustness of a possible multi-level model approach using regression against past spending on lower-level geographies.

Questions for the group

- **Do you have views about which statistical techniques we should consider when deciding how to weight individual cost drivers?**

- **What are the group's views on the short listed options set out in this paper?**

Annex 1 – Guiding principles of the review

1) Based on the responses received to our Call for Evidence on needs and redistribution, we identified a set of principles to guide the work of the fair funding review. These represent the framework which the Government will use in designing a new relative needs assessment methodology, having considered the responses to this consultation:

   i) **Simplicity** – the overall number of formulas used within the current methodology, along with the layers of complexity contained within them, means that they are little understood and may no longer hold the same relevance as when they were first introduced. This is an opportunity to identify the most important factors that drive the 'need to spend' on local services, and we will aim to produce a relative needs assessment that is as simple as is practicable,

   ii) **Transparency** – it should be straightforward for those affected by the relative needs assessment to understand what factors have influenced the levels of funding received by a local authority so that they can hold their local representatives to account for the decisions that they make. To support this we will make the link between local circumstances and funding allocations more visible,

   iii) **Contemporary** – the new relative needs assessment will be based on the most up-to-date data that is available. To facilitate more frequent updates, as far as practicable the funding formula will be based on data that can be regularly updated at planned intervals. If the collection of data or other technical requirements means that desirable changes cannot be made at the point of implementation, the Government will consider whether and how to phase these in at a later date whilst providing councils with financial certainty,

   iv) **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,

   v) **Robustness** - the new funding formula should take into account the best possible objective analysis, and

   vi) **Stability** – the funding formula should support predictable, long-term funding allocations, ideally as part of a multi-year settlement. Local authorities' long-term financial planning and service delivery will also be assisted by temporary transitional arrangements to their new relative needs baseline to ensure there are no undue year-on-year changes in funding.

2) In addition to these principles, a key objective of the review is to work in conjunction with wider reforms to local government finance and help provide a strong incentive for councils to grow their local economies and to use their resources as efficiently as possible.