Update on the Fair Funding Review, September 2016

Introduction:

Over the past few months you have been provided with a number of verbal updates about the work of the technical working group for Needs and Redistribution. The aim of this paper is to expand on these updates to give you a more detailed picture of the progress that has been made on the Fair Funding Review to date, the immediate next steps and broader programme timetable.

Programme Design:

The Fair Funding Review will need to cover a wide range of issues and interactions. As was broadly described at last month's Steering Group, to manage this work we have identified 4 core questions to focus on, these are:

1. Defining Need
2. Features of the system
3. Treatment of resources
4. Incentives

We discussed the details of these work streams and the timetable at which these issues will be tackled in the September meeting of the technical working group. The high level timetable that supported that discussion is attached at Annex A.

The timetable that was presented delivers a new assessment of needs and resources in time for the potential introduction of 100% Business Rates Retention in 2019/20. This timetable is tight but we are on track to meet it, subject to securing a coherent view from the sector on their preferred approach in the near term to inform ministerial decisions on the key principles for the Review and the options to develop further.

Progress so far:

Since May, a significant number of papers have been presented to the technical working group. One of the initial papers the Technical Working Group discussed was the key questions that the Review needed to address. This discussion played a key role in influencing the contents of the Fair Funding Review: Call for evidence.

The group have also arrived at agreed positions on a number of important issues that have helped shape the direction of the Review. A summary of the papers the group have considered is at Annex B.

Defining Need:

This is the largest, most significant and therefore, the most challenging area that the Review needs to address. It is therefore the area that DCLG and the technical working group have dedicated the most time to so far.

The group has been presented with a series of papers which have outlined different options for measuring need. These have included:

- The variation in current spending per head
- The current approach to measuring relative need
- Outcome based needs assessments
- The availability of the current indicators associated with need

Having considered these papers the group have agreed the following:

- Population, while a key driver, does not capture on its own enough of the factors that drive local authorities need to spend. Other drivers should be included

- While we should not discard all of the current approach to measuring need, the reliance on historic patterns of spending does not incentivise efficiency and that it entrenches variable patterns of unmet need. Alternative statistical approaches should therefore be considered

- Instead of thinking about potential outcome measures, the Review could focus on cost drivers that are likely to drive future need, potentially (but not necessarily) with a view to simplifying the formulae.

Features of the system

One of the key issues for the Review is how the needs assessment interacts with the wider reforms to business rates and in particular how we find the balance between incentivising growth and ensuring funding is fairly distributed according to the needs of local authorities. To support this discussion the technical working group has considered a number of papers about how we can find this balance when resetting the system. The group has agreed the following:

- A system based on partial resets appears to offer the best approach to balancing the growth incentive with distributing funding according to need

- The group have asked DCLG to explore options around rolling resets which they thought would help reduce the incentive for gaming the system and would also help stabilise income from business rates.

Treatment of resources

ANEC presented a paper to the group that illustrated the variation in councils' ability to raise funding through Council Tax. This paper led to a discussion about how the ability of local authorities to raise resources locally should be taken into account when assessing where to set the baseline funding levels in the new system. The group agreed the following:

- It was very important that the ability to raise income from council tax, and possibly fees and charges, is taken into account and that this was an important issue for the technical working group to consider

- However, the fact that good data was already held about local authorities' ability to raise income suggested that this work stream could become the focus of the group after the approach to defining and measuring need has been further developed

Next steps:

Analysing the Call for Evidence:

The first priority at the moment is to process and analyse the 217 responses the department received to the Fair Funding: Call for evidence. These responses will inform ministerial decisions on the key principles for the review and so narrowing down the options to consider and the technical working group will have a chance to see and discuss a summary of the responses at the earliest possible meeting.

Identifying Key Cost drivers

Collecting the data for the indicators for a needs assessment has been the most time consuming element of the previous reviews of local government funding formulas. The current needs assessment is based on over 120 factors as indicators for need to spend across all the services that local government delivers. It is therefore important that the group focuses on identifying the cost drivers to be used in the formulae, and the appropriate data for them, over the next few months.

To facilitate this, DCLG are arranging for other government departments to attend the technical working group to outline their views on the key factors affecting costs in their policy areas. DH presented to the group in September and DfE are due to attend the October meeting of the technical working group.
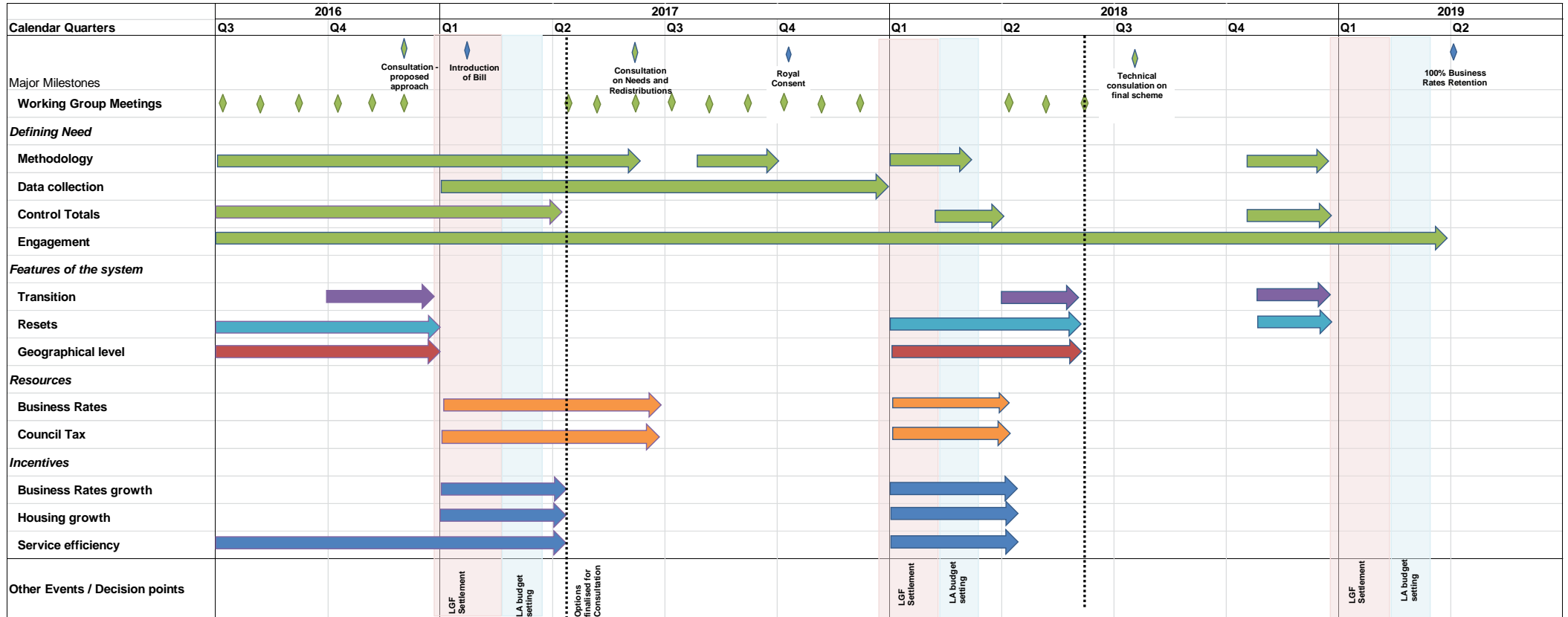
The Association of Local Authority Treasurers (ALATS) have organised a sub group of the technical working group to develop a local government view of what the key cost drivers to be used in a new needs assessment should be. We hope this group will present a paper on their work so far to the October meeting of the technical working group.

Exploring alternative statistical methodologies

One of the main areas of agreement within the group so far has been the need to consider alternatives to the current approach for measuring relative needs which relies on regressions against past expenditure. However there has been less agreement about what methodologies we could use instead.

To progress this conversation, analysts in DCLG have been exploring alternative methodologies ranging from normative modelling to factor analysis and other data reduction techniques such as principle component analysis. DCLG is in the process of assessing the strengths and limitations of these different approaches and will present a paper on this to the October meeting of the technical working group.

Annex A: Fair Funding Review Work plan

Calendar Quarters	2016		2017				2018				2019	
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2

Major Milestones
- Consultation - proposed approach
- Introduction of Bill
- Consultation on Needs and Redistributions
- Royal Consent
- Technical consulation on final scheme
- 100% Business Rates Retention

Working Group Meetings

Defining Need
- Methodology
- Data collection
- Control Totals
- Engagement

Features of the system
- Transition
- Resets
- Geographical level

Resources
- Business Rates
- Council Tax

Incentives
- Business Rates growth
- Housing growth
- Service efficiency

Other Events / Decision points
- LGF Settlement
- LA budget setting
- Options finalised for Consultation
- LGF Settlement
- LA budget setting
- LGF Settlement
- LA budget setting

Annex B: Papers considered by the Technical Working Group

May

Terms of reference (DCLG)

Initial questions (DCLG)

Discussions shaped the contents of the Call for Evidence (closed 26 Oct)

June

Comparison of 2014/15 Revenue Expenditure per head (DCLG)

Cost drivers of local government services (DCLG)

The group agreed that population was a key driver but also need to consider characteristics of places.

July

Current approach to measuring need – Relative Need Formulas (DCLG)

Alternative approaches – Outcome measures (CIPFA/Grant Thornton)

The group agreed that we should explore alternative methodologies to the current methodology which is based on regressions against past expenditure. They did not think it was feasible to consider outcome based measures.

August

Needs and Resets of the System (DCLG)

Drivers of Need – EPCS (ANEC)

Taking ability to raise council tax income account (ANEC)

The group supported further thinking around partial resets and asked for rolling resets to be modelled. The group also agreed that the needs assessment should take account of ability to raise income but agreed to consider how best to do this when the approach to measuring need was more advanced.

September

Fair Funding Review – Work plan (DCLG)

The Group noted the importance of working at speed and consulting on final needs assessments as early as possible ahead of the year of introduction.

Approach to measuring relative need – Adult Social Care (DH)

The group noted the interaction between the work of the Fair Funding Review and other assessments of need being undertaken by government in the shorter term.

Needs and Resets of the System – full and partial resets (DCLG)

The Group expressed an interest in exploring a rolling system of needs resets further.