

DERBYSHIRE COUNTY COUNCIL

CABINET MEMBER FOR STRATEGIC, POLICY AND BUDGET

9 September 2014

Report of the Director of Finance

**INDEPENDENT COMMISSION ON LOCAL GOVERNMENT FINANCE –
RESPONSE TO “CALL FOR EVIDENCE”**

1 Purpose of the Report

To note the details of the Independent Commission on Local Government Finance’s “Call for Written Evidence” and the Council’s response.

2 Information and Analysis

Local government faces unprecedented financial challenges. There are upward pressures on services and downward pressures on budgets and local taxes.

The Independent Commission on Local Government Finance (ICLGF) is tasked with making recommendations for the reform of local government finance and finding better ways to fund local services and promote economic growth in England. ICLGF was established by CIPFA and the LGA to impartially examine:

- The current position of the local government finance system.
- A potential new system that enables better public services and encourages economic growth.
- Practical options for changing the system that could be implemented by an incoming government.

ICLGF has requested written evidence from business and business organisations, the faith and voluntary sector, public sector organisations and local government on:

- the strengths and weaknesses of the current local government finance system;
- the problems and opportunities it creates in tackling the challenges above;

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- potential reforms that would make it easier to tackle these challenges; and
- specific practical solutions for changing the system that can be implemented by an incoming government from May 2015.

ICLGF will analyse the evidence to form a view on the current local government finance system and the ways in which it could be reformed.

The call for evidence will be complemented by a research and engagement programme.

Interim findings will be published in Autumn 2014, with a final report published in early 2015.

ICLGF's final recommendations on the future of local government finance will be presented to all of the main political parties with the aim of shaping the debate on the future of local government and influencing the next government.

Consultation Response

The Council's response to ICLGF's "Call for Written Evidence" is included in this report at Appendix One.

3 Considerations

In preparing this report the relevance of the following factors has been considered - financial, legal and human rights, human resources, equality of opportunity, health, environmental, transport, property and prevention of crime and disorder considerations.

4 Background Papers

Papers are held in Technical Section, Room 146, County Hall.

5 OFFICER'S RECOMMENDATION

To note the Council's response to ICLGF's "Call for Written Evidence".

PETER HANDFORD

Director of Finance

20 August 2014

Derbyshire County Council response to the 'Call for Written Evidence'

Dear Sirs

The Council welcomes the opportunity to respond to the ICLGF's call for written evidence. The Council has set out some of its concerns regarding the current system of local government finance which we trust will be considered by the Independent Commission.

1. Business Rates Retention Scheme and Existing Grant Arrangements

- 1.1. Prior to the introduction of the scheme, the Council argued that local authorities needed a period of financial stability and a period of certainty. At the time, the economic climate was delicate and therefore, the Council was of the opinion that it was not the right time for such a radical change to the Local Government Finance System. The Government's proposal for the localisation of Council Tax benefit, which was also introduced alongside the introduction of the Business Rates Retention Scheme (BRRS), together with the offer of one-off funding for Council Tax Freeze Grant, provided additional challenges in the first year of the BRRS.
- 1.2. These concerns have been borne out as we have seen further offers of the Council Tax Freeze Grant for local authorities, which effectively gives local authorities a 'cliff edge' in their funding levels as there is no guarantee that the funding will be paid beyond 2015/16. As part of the 2014/15 Final Settlement, the Government announced that it intends to continue paying freeze grants through base funding to help with the potential 'cliff edge' effect. This will only benefit local authorities if it is not matched by a further cut in Revenue Support Grant.
- 1.3. Furthermore, the BRRS has become just as complicated to explain to Officers and Members as its predecessor, the Formula Grant system, particularly as the BRRS still retains an element of the Formula Grant system in the baseline funding which is used to calculate an authority's share of business rates. Local authorities also have the option of forming business rates pools which may benefit them financially. However, to date many authorities have been reluctant to form pools, due to their complexity and burdensome administrative arrangements.
- 1.4. The system has become further complicated with the decision to use 'holdbacks' for the New Homes Bonus, safety net and capitalisation, all of which do little to aid local authorities in setting their budgets, as they are unable to estimate the amount which is likely to be returned in the form of a s.31 grant. We are disappointed that the Government's estimates to meet the demands of the safety net were inaccurate and the Council does not agree that Revenue Support Grant is reduced to fund this error. It is

understood that the increase in safety net holdbacks is due to concerns over the impact of successful rates appeals in some authorities. The Council fails to see why local government should fund an issue that is created by a protracted process for appeals by a Government agency. Due to the unpredictable nature of these grants, the Council has no option but to treat this funding as one-off in nature as there is no guarantee that a similar amount will be paid in future years.

- 1.5. Furthermore, decisions made in the Autumn Statement 2013 regarding the capping of the business rates multiplier, have added a further level of complexity to the BRRS, and again have brought a degree of uncertainty to the system. The decision to cap the business rates multiplier has also made it difficult for local authorities to account for the funding received, as the payment made is an interim payment pending the final figure which will be published once the final NNDR outturn is established. Guidance will have to be provided to local authorities on the accounting treatment of this.
- 1.6. The Council agrees that the BRRS provides an incentive for growth in its area; however we are concerned that the incentive effect is reliant upon existing infrastructure to promote business rates growth. Those councils who are in areas where the infrastructure exists, such as the South East and inner cities, will already have an advantage over the more rural areas of the country, where it will take time to build the necessary infrastructure to allow areas to grow. Whilst, the Council welcomes support from Government to help with the development of Local Enterprise Partnerships, such as D2N2 in Derbyshire/Nottinghamshire, the benefits of growth will take time to develop, but the costs associated with the growing demographic, particularly older people in Derbyshire, will far outweigh the business rates growth required to fund the costs. Whilst we can, to some extent, understand the incentive for local growth, we are concerned that there is no correlation between the service needs of a local authority and its ability to grow its business rates growth and would argue that there needs to be a finance system which reflects need. The proposals for funding the baseline were based on the levels of Formula Grant as at 2012/13. We suggest that the system needs to be reviewed and assess the changing levels of service need over time. If the Government waits until the reset, which is not due until 2020, the baseline funding level will be 7 years out of date. This creates further safety net issues due to changes the freeze has masked and damped.
- 1.7. If the BRRS is to continue, we would expect a substantial period of consultation to take place with local authorities, prior to the reset, to ensure that local government understands the implications of any reset and the way that needs have been re-assessed. A full set of exemplifications should be provided. During the consultation period for the BRRS scheme the Government failed to provide exemplifications which made it difficult for local authorities to understand the full financial impact of the proposed changes.

PUBLIC

- 1.8. We would also request that local authorities are given two to three years notice of any reset in order to aid medium term financial planning. We would request that the timing of any resets are fixed, say, every five years in line with business rates revaluations.

2. Formula Grant/Four Block Model

- 2.1. The previous method of grant distribution, the Four Block Model, lacked transparency, was unstable and unpredictable. It was a highly complex and technical model, with only a handful of officers in local government able to fully comprehend all its elements. This convoluted system made it difficult for officers to explain to both Members and the electorate. Furthermore, the data used to determine funding allocations was often out of date.
- 2.2. The change to the Four Block model from the previous Formula Spending Shares was a relatively quick transition with a short consultation period with local government prior to implementation.
- 2.3. We would like to see any new system of local government to be well-thought through and developed in partnership between central and local government. There needs to be an open and honest debate from both sides and a mutual agreement on a system that is robust, long-lasting and addresses the long-standing concerns of local government.
- 2.4. It is pleasing to see that the Government has commissioned research on whether rural authorities face additional unavoidable costs. The Council is looking forward to see the outcomes of the research, and we would expect the findings to be reflected in the local government finance system.
- 2.5. Resource equalisation has been an established debate amongst local authorities. We would expect this issue to be researched and addressed in any new local government finance system.

3. Damping

- 3.1. The Council has previously made contributions to various Government reviews of local authority finance systems during which we have emphasised the need for fairness and stability within any grant system. The approach to floor damping adopted by the government reflects these concepts by guaranteeing minimum increases for all councils.
- 3.2. The Government was committed to some form of floor damping mechanism in the previous Formula Grant model as it provided an element of stability of year-on-year increases, as well as providing an element of transparency within the Funding Formula. The removal of floor damping would likely give rise to turbulent grant increases which does not aid the financial planning process.

- 3.3. The vagaries associated with the Formula Grant system were such that the method of allocation was reviewed on a regular basis and produced different distributions of grant with alarming regularity. This gave rise to the potential for a local authority to gain from a change in one year and lose from a further change a few years later. If the grant system didn't damp these results the potential volatility would be extremely difficult to manage.
- 3.4. From 2008/09, the Government moved to multi-year settlements. At the time, the Council (which was heavily damped), had a clear expectation over the period of multi-year settlements, that the damping would fully unwind. This never transpired and the move to the Business Rates Retention Scheme from April 2013, resulted in a loss of funding of £12m through the damping mechanism, which was effectively 'locked in' and the Council will never have the opportunity to recover this funding.

4. New Homes Bonus

- 4.1. The New Homes Bonus Scheme was introduced in April 2011 with the expectation that it would provide a financial incentive to local authorities to help overcome known barriers to the building of new homes. The Government has funded the New Homes Bonus (NHB) from £250m set aside and a further £700m which was top-sliced from Revenue Support Grant. The allocation of the NHB favours those councils with lower-tier responsibilities. If the £700m top-slice was allocated as Revenue Support Grant rather than the New Homes Bonus the Council would have been significantly better off by around £6m in 2014/15.
- 4.2. The National Audit Office (NAO) has recently conducted an examination of the NHB to ascertain whether the Government is meeting its objective and whether local authorities are being incentivised to encourage the building of new homes locally. It concluded by stating that it was too early for the NHB to have had a discernible influence on the number of new homes. It also stated that there is no evidence to suggest that there has been a measureable change in local authorities' behaviour. The reality is that many local authorities are using the funding to support budget pressures which is not how the Government intended the funding to be utilised.
- 4.3. The NAO report also raised concerns that through the redistributed Formula Grant, by 2016/17, some local authorities may face substantial financial risks from the overall effect of the NHB on their funding because of the redistributive nature of the scheme, confirming the issue raised above.
- 4.4. The report also stated that the Government was planning to undertake a post-implementation review of the NHB in 2013/14 but had not yet decided its scope or methodology. To date, there has been no indication from Government as to when the review will take place, despite further

PUBLIC

confirmation that there would be a review announced alongside the 2014/15 Finance Settlement.

5. Early Intervention Grant

- 5.1. In 2012, the Government took the decision to top-slice £150m from the now defunct Early Intervention Grant with the commitment that the distribution of the £150m would be left to ministerial judgement. Therefore, there is no guarantee that the £150m will be paid to local authorities. In the first two years following the top-slice, the funding has been made to local authorities in the form of Adoption and SEN Reform grants; however the decisions around the funding allocations did not come until early or during the financial year, which makes it difficult for local authorities to plan and budget for the funding provided.
- 5.2. The Government needs to provide local authorities with advance notice of the funding available to them in order that they can formulate appropriate budget plans.

6. Local Government Finance Settlement

- 6.1. The last two financial years have seen a late publication of the Local Government Finance Settlement. The 2014/15 Settlement was published shortly before Christmas, despite requests from local government to publish the information in line with the longstanding timescales that had been followed. However, the Council acknowledges that the information could not be published until the Chancellor had announced his Autumn Statement. The Council acknowledges that 2014/15 has seen an added complexity to the funding methodology as a result of the Chancellor's decision to cap the business rate multiplier.
- 6.2. The Council was also disappointed that the Council Tax referendum principles were not published alongside the Provisional Settlement. Many local authorities need to make decisions regarding Council Tax level early in the New Year and the publication of the principles in December would have aided local authority decision making.
- 6.3. The Council would expect any new Government to commit to the revaluation of Council Tax bands. The current council tax system is based on valuations from 1991.

7. Proposals for a New Government

- 7.1. The call for evidence specifically asks for practical solutions for changing the system that can be implemented by an incoming Government from May 2015. Below, we have set out our proposals.

New Homes Bonus Scheme

- 7.1.1. The Government has made a commitment to review the Scheme, but to-date there has been no indication of when this review will take place. The Council would like to see a commitment from Government setting out a timetable for the review.
- 7.1.2. Alternatively, we would strongly urge Government to consider abolishing the scheme and rolling the funding into Revenue Support Grant to enable local authorities to make decisions about its priorities. As indicated in the recent NAO report, the scheme does not appear to be meeting its objective.

Early Intervention

- 7.1.3. The Council would urge Government to roll in the £150m top-slice into Revenue Support Grant, so that local authorities can plan and prepare on how to spend the funding. Local authorities are best placed to decide on local priorities.

Local Government Finance Settlement

- 7.1.4. The Council would like to see a return to the Local Government Finance Settlement being announced in late November/early December to aid the budget setting process. There was a commitment made by the current Government earlier this year to have multi-year settlements and we would request that the new Government in 2015 upholds this commitment. Multi-year settlements will help local authorities with their budget setting and medium term financial planning, providing some certainty in the finance system, which has been eradicated with the austerity measures taken in recent years.
- 7.1.5. A commitment that the Council Tax referendum principles are published alongside the *Provisional* Local Government Finance Settlement, and not left until as late as January/February.
- 7.1.6. We would like to see a Comprehensive Spending Round published by Government as soon as is practicable following the General Election. Local Government has borne the brunt of the austerity measures in recent years and only has some certainty around funding levels up until the end of 2015/16. The expectation is that the austerity measures will continue on the same trajectory as those seen over the last four years, but local authorities need to have some certainty on the finances they will receive in the

medium term if they are to develop robust plans that deliver and shape the services they provide as we move into the next decade.

- 7.1.7. A quick decision on whether the Council Tax Freeze and Business Rates Compensation will be paid beyond 2015/16.

Spending Power

- 7.1.8. More recently, the Government has introduced the Spending Power figures to describe how an authority's funding has reduced. This has done little to help local authorities, as it fails to reflect the substantial cuts made to Revenue Support Grant. It only serves to mislead the public and does not reflect the true position. A prime example was seen following last summer's Technical Consultation when the Government stated that the cuts represented a 2.3% reduction in local government funding. The reality was that the Council will see its Revenue Support Grant reduced by 27% in 2015/16 and its Settlement Funding Assessment reduced by 14%.
- 7.1.9. We would like to see the Spending Power figures abolished and an agreement reached between central and local government on information that provides the electorate with easily understandable data in respect of local authority funding.

Accountancy

- 7.1.10. There has been a lot of debate recently amongst accounting professionals in local government regarding the presentation of the final accounts produced by local authorities. The debate rests around whether the Statement of Accounts produced by local authorities provides meaningful information to the electorate. The introduction of IFRS accounting for local government from April 2010 has resulted in accounts being convoluted and over complicated. The proposal to bring forward the statutory deadline for publication of the Statement of Accounts is an ideal opportunity to examine the requirements of the Code of Practice and for local authorities to challenge the requirements of the Code and whether the publication of substantial disclosures adds value to the reader of the accounts. We are pleased that the Government has made a commitment to work with CIPFA to reduce the current reporting requirements in the Statement of Accounts, as we consider that there are substantial elements of the statement of accounts which are surplus to the needs of the electorate in terms of helping them understand where authorities are spending money.

Yours faithfully

Peter Handford
Director of Finance