

# Fair Funding Review – relative needs assessment Consultation response

12 March 2018



The Local Government Association (LGA) welcomes the opportunity to respond to the Government's consultation on the relative needs assessment as part of the Fair Funding Review.

The LGA is here to support, promote and improve local government. We will fight local government's corner and support councils through challenging times by making the case for greater devolution, helping councils tackle their challenges and assisting them to deliver better value for money services.

This response has been approved by LGA Leadership Board and Executive.

We continue to work closely with the Ministry for Housing, Communities and Local Government on the Fair Funding Review to ensure that the Review is objective and transparent and that there is extensive engagement with the local government family. This joint working, and the fact that all papers of the technical working group have been made publicly available, is welcome and we intend to continue this approach.

### General comments

Since the General Election, we have called for the Government to clarify its intentions regarding the Fair Funding Review and the confirmation that the Government is committed to the Review and that it will be implemented in 2020 is welcome. This consultation, focussing on the design of the relative needs assessment, is an important milestone, but we look forward to the work of the Review continuing at pace.

It is positive that the consultation shows the Government is listening to representations from all parts of local government. In particular, there is a consensus among local authorities that the outcome of the Review should build a simpler, more transparent system of assessing relative needs and resources. Above all, it is important that the Review delivers a fair outcome. It is welcome to see the Government's thinking attempts to reflect this view.

However, there is more to do, and our responses provide some suggestions on making the relative needs assessment more transparent while ensuring that the result has the best possible chance of being accepted as 'fair' by as many members of the local government family as possible.

# Submission

We recognise that this focusses on the relative needs assessment, but we look forward to the Government's discussion papers on treatment of resources, such as council tax, fees and charges, and any further technical papers as necessary. These issues are just as important in determining local authority funding baselines.

It is important that the work of Review continues at pace. The current Spending Review period and four-year settlement offer both expire from April 2020. The Government also intends to implement greater business rates retention, improvements to the retention system and the results of the Fair Funding Review at the same time. The financial uncertainty facing local authorities makes financial planning meaningless without some guidance from Government on what could be expected. We continue to call for the Government to provide exemplifications of the impact of the Review, and details of the transition mechanism – in particular in the 2020-2022 period – as soon as possible.

Ultimately, the Review will not be successful and lead to a sustainable outcome if it is not introduced alongside additional resources. We estimate that councils face a funding gap of over £5 billion by the end of the decade, on top of a £1.3 billion pressure to stabilise the adult social care provider market today. One way to help meet this gap is for the sector to collectively retain 100 per cent of business rates collected in England. If current plans to roll in grants and increase the share retained by councils to 75 per cent are implemented, the remaining 25 per cent should also be retained to fund pressures. These additional resources could also help to make the transition process smoother.

#### Simplification and the foundation formula

The current system of distributing funding is no longer fit for purpose.

Prior to April 2013, formula funding was distributed on the basis of a relative needs assessment made up of at least 15 formulae and 120 different indicators. This was only one of the blocks in the so-called four block model, which added other unintended consequences and complications. Since April 2013, the impact of business rates retention, and then the new methodology for calculating reductions in the four-year settlement, added further layers of opacity.

In this context, it is welcome that the Review started from a blank sheet of paper. It is positive that the Government is attempting to reduce the number of cost drivers and formulae used in the relative needs assessment. It is important that complexity is only added where it is unavoidable and where it has a material positive impact on fairness.

However, the right number of formulae and cost drivers must ultimately be driven by evidence or the outcome will not be seen as 'fair'.

The complex and diverse landscape of local government, including many different types of authorities delivering different services in different local circumstances, means that the final result will have an inevitable level of complexity although there may be ways in which the presentation and explanation of the formula can be improved.

As a result, we do not think using a single formula to estimate relative needs for the totality of local government services is feasible or appropriate. For reasons set out above, it is highly likely to be too crude to deliver an equitable result. It is welcome the Government has recognised this by proposing service-specific formulae as an element of the assessment.

However, we would support the Government to continue to explore a 'foundation formula' for services which are not driven by unique cost drivers and where need to spend can be shown to be most closely correlated to factors used in the foundation formula. This assessment has to be based on evidence and the Government's tests for service-specific formulae as set out below.

The Government's starter list of cost drivers to be used in such a formula is population, deprivation, sparsity and area cost. We believe this is a good starting point and note that it matches the proposals of the Association of Local Authority Treasurers' Societies subgroup of the technical Fair Funding Review working group.

In addition, the Government should consider if and how costs of service delivery differ in more densely populated areas (or if this is dealt with through deprivation measures) as well as rural areas. This should be based on evidence rather than assumption. Large student and daytime populations are often cited as contributing to the cost of service delivery – these factors should be considered as well.

Perhaps a more important concept than simplicity, however, is transparency. Even with the simplest formulae, the process of combining the results with other parts of the assessment and turning them into actual funding allocations has a significant potential to add unnecessary complexity such as the four-block model. Councils should be able to see why their allocations are what they are as easily as possible. We look forward to working together with Government on this.

#### Service specific formulae

We support the Government's two key principles to consider whether services require a specific formula to assess relative spending needs. Spending should be material for many local authorities, and the cost drivers for the service should be materially different from the single 'foundation' formula.

However, the Government must be transparent in arriving at its final decisions after analysing the cost drivers of services, to demonstrate how the services ultimately chosen for specific formulae match those tests. This could be a subject of a separate discussion paper. If any of the Government's proposed service-specific formulae are found to significantly overlap with the foundation formula, it could provide an opportunity to reduce the number of formulae used overall, and to adjust the weightings accordingly.

With this in mind, in addition to the starter list in the consultation, the Government should explore non-HRA housing support as a service to be assessed under a specific formula. Homelessness and temporary accommodation services represent a significant demand-led pressure for district and unitary authorities. Cost drivers should be tested to see how much overlap there is with a foundation formula as set out above. If there isn't a lot of overlap than a separate formula is probably required.

The list of service-specific formulae currently omits public health. The Government must make clear that this will in effect be a 'service specific formula' within the proposed structure, unless the cost drivers used in the formula match the 'foundation' formula. Funding for public health will be part of the 75 per cent retention system, so the formula should be reviewed within the context of the Fair Funding Review rather than separately to the Review. Treating public health as a matter outside the Review could add an unnecessary degree of complexity.

In terms of cost drivers used in the formulae, our responses to detailed questions provide a small number of suggestions. However, we would draw attention to contributions of individual councils, representative bodies and service directors such as the Association of Directors of Adult Social Services (ADASS), Association of Directors of Children's Services (ADCS) and the Association of Directors of Environment, Planning and Transport (ADEPT).

We believe that the cost drivers used in the formulae should avoid 'actual units of delivery' such as the number of people receiving various services. Instead, we support an approach that focusses on the drivers of demand and cost that cannot be affected by local policy choices such as numbers of people with a particular type of need. This would preserve the incentive to invest in prevention and manage demand effectively. It would also ensure that the system would not be seen as creating perverse incentives.

Social care continues to see the highest levels of council spending as well as further demand and inflation pressures. We need to ensure enough effort is put into finding suitable cost drivers for these areas of spending. One example would be adult social care for persons with learning disabilities, where the costs are likely to be lifetime costs and the number of working age adults does not necessarily correlate with level of demand. The impact of the adult social care green paper should also be reflected.

We welcome the Government's attempts to establish an evidence base on costs of children's services, but it is important that this is done at pace to ensure that results can feed into the formulae as soon as possible. One source of continued concern by our members is the financial sustainability of schools. While schools are funded through the Dedicated Schools Grant, councils carry the financial responsibility for any maintained schools that might find themselves with insufficient funding to carry on day-to-day services such as home to school transport and for supporting special needs services and school building requirements for all schools irrespective of status.

The consultation asks the question about how to treat service pressures which have a material impact on individual local authorities but a small impact at a national level. The consultation mentions flood defence spending as an example. We would draw the Government's attention to responses of our member authorities for further examples of such pressures, but examples that could be used for exploration include persons with no recourse to public funds, Unaccompanied Asylum Seeking Children and revenue costs of flood defence. Any recommendations, as with other parts of the formulae, should be the subject of further work and be discussed in the Fair Funding Review Group.

The Government must be transparent about which services it believes sit outside the overall funding formula system to ensure appropriate accountability for Ministerial decisions on council funding levels. This assessment should be based on a clear process of testing, with reference to cost materiality and whether cost drivers match one of the other formulae.

Once the Government assesses a cost pressure to be highly localised, these costs should be dealt with outside of this system, with the Government providing specific funding on a case-by-case basis.

### Statistical analysis

Assigning weightings to cost drivers is just as important as the choice of the drivers used. Our members would like to minimise ministerial judgement and for these weightings to be based on robust evidence and analysis.

However, some of our members have expressed concern over using statistical techniques which seek linkages to past expenditure levels on services as a way to derive these weightings, such as past expenditure-based regression. We recognise that this technique has strengths, such as the ability to explain how the analysis is carried out, but our members would like to avoid the possibility that the result of the analysis only reinforces the previous patterns of spending. We believe the Government should consider producing an in-depth explanatory paper on how this statistical technique could be used in a way that does not simply perpetuate historic spending patterns to provide further information to stakeholders, especially those without a deep understanding of statistics. This could form one of the set of technical papers planned as the work progresses.

Small-area modelling, which looks at population characteristics at ward level within a local authority as well as between local authorities, minimises this effect. We note that the level of detail required for small-area modelling to work can often be unavailable without bespoke data collections, which can carry significant cost. It is positive that the Government is considering using this technique for developing the social care formulae and we welcome the Government's research into the costs of looking after children as the basis for this technique on the children's services formula.

Furthermore, we strongly support:

- A 'sense check stage' of any statistical analysis with the use of expertise of finance officers and service directors. This has been discussed at the officer-level Fair Funding Review technical working group which came to the same view and we would support the consensus reached by local authority representatives in the meeting.
- Independent assurance of any options that likely to be implemented.

Please see below for detailed answers for specific consultation questions.

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## Responses to specific questions

Our responses to each of the questions in the consultation document are set out in detail below.

### General

#### **1) What are your views on the Government's proposals to simplify the relative needs assessment by focusing on the most important cost drivers and reducing the number of formulas involved?**

It is positive that the consultation shows the Government is listening to representations from all parts of local government. In particular, there is a consensus among local authorities that the outcome of the Review should build a simpler, more transparent system of assessing relative needs and resources. Above all it is important that the Review delivers a fair outcome. It is welcome to see the Government's thinking attempts to reflect this view.

However, the right number of formulae and cost drivers must ultimately be driven by evidence or the outcome will not be seen as 'fair'.

The complex and diverse landscape of local government, including many different types of authorities delivering different services in different local circumstances, means that the final result will have an inevitable level of complexity although there may be ways in which the presentation and explanation of the formula can be improved. A relative needs assessment on the basis of a single formula is highly likely to be too crude to deliver an equitable result.

However, we would support the Government to continue to explore a 'foundation formula' for services which are not driven by unique cost drivers and where need to spend can be shown to be most closely correlated to factors used in the foundation formula. This assessment has to be based on evidence and application the Government's tests for service-specific formulae.

### Single 'foundation' formula and constituent cost drivers

#### **2) Do you agree that the Government should use official population projections in order to reflect changing population size and structure in areas when assessing the relative needs of local authorities?**

We support this proposal. Using projections to reflect the potential future changing pattern of relative needs could minimise the degree to which the relative needs and funding baselines diverge from one another over the years between system resets.

#### **3) Do you agree that these population projections should not be updated until the relative needs assessment is refreshed?**

We believe there needs to be further analysis of the effects of this on the design of the business rates retention system, in particular the balance between needs and incentives. This has to include consideration of how to deal with unexpected significant divergence in needs that are measured by the formulae. To explore this, we are developing analysis on the extent to which population characteristics diverge over time and will share this with our members and the Government later this spring.

**4) Do you agree that rurality should be included in the relative needs assessment as a common cost driver?**

**5) How do you think we should measure the impact of rurality on local authorities' 'need to spend'? Should the relative needs assessment continue to use a measure of sparsity or are there alternative approaches that should be considered?**

Our members in rural areas, or with pockets of rurality in within their areas will welcome the inclusion of rurality (sparsity) as a cost driver for consideration in the 'foundation formula'. There should be an evidence-based process in determining the weighting of this, and any other, cost driver.

**6) Do you agree that deprivation should be included in the relative needs assessment as a common cost driver?**

Our members in more deprived areas, or with pockets of deprivation within their areas, will welcome the inclusion of deprivation as a cost driver. There should be an evidence-based process in determining the weighting of this, and any other, cost driver.

**7) How do you think we should measure the impact of deprivation on 'need to spend'? Should the relative needs assessment use the Index of Multiple Deprivation or are there alternative measures that should be considered?**

The IMD process can provide data to be used in the assessment, however the three-year pause between releases, and the 'ranking' nature of the end result of the calculations, means that the indices themselves should only be seen as a 'backstop' if no other reliable means to measure deprivation emerge. There should be an evidence-based process in determining the weighting of this, and any other, cost driver and consideration of how up to date the data is in the IMD.

**8) Do you have views on other common cost drivers the Government should consider? What are the most suitable data sources to measure these cost drivers?**

We would refer the Government to responses by local authorities. The following includes a selection of proposals, where evidence of impact could be sought.



The Government could consider whether there should be adjustments to reflect the extra pressure on services caused by population density, daytime visitors and students. These would have to be tested to see if there is an impact over and above that reflected through other cost drivers.

**9) Do you have views on the approach the Government should take to Area Cost Adjustments?**

Areas facing higher labour and input costs will welcome the consideration of area costs as a cross-cutting cost driver. We note the Government is planning a separate technical discussion paper on this element of the assessment and look forward to discussing this, and how it links to the needs element, in more detail within the technical working group over the coming months.

As a general principle, it is important to avoid duplication between various cost drivers – the same should apply to the components of the Area Cost Adjustment.

**10a) Do you have views on the approach that the Government should take when considering areas which represent a small amount of expenditure overall for local government, but which are significant for a small number of authorities?**

**10b) Which services do you think are most significant here?**

We would draw the Government's attention to responses of our member authorities for further examples of such pressures, but examples that could be used for exploration include persons with no recourse to public funds, Unaccompanied Asylum Seeking Children and revenue costs of flood defence. Any recommendations, as with other parts of the formulae, should be the subject of further work and be discussed in the Fair Funding Review Group.

The Government must be transparent about which services it believes sit outside the overall funding formula system to ensure appropriate accountability for Ministerial decisions on council funding levels. This assessment should be based on a clear process of testing, with reference to cost materiality and whether cost drivers match one of the other formulae.

Once the Government assesses a cost pressure to be highly localised, these costs should be dealt with outside of this system, with the Government providing specific funding on a case-by-case basis.

Service-specific formulae and proposed cost drivers

**11a) Do you agree the cost drivers set out above are the key cost drivers affecting adult social care services?**

**11b) Do you have views on what the most suitable data sets are to measure these or other key cost drivers affecting adult social care services?**

Social care continues to see the highest levels of council spending as well as further demand and inflation pressures. We need to ensure enough effort is put into finding suitable cost drivers for these areas of spending. One example would be adult social care for persons with learning disabilities, where the costs are likely to be lifetime costs and the number of working age adults does not necessarily correlate with level of demand.

We would draw attention to responses of individual local authorities as well as ADASS in populating the 'long list' for the research to consider. The impact of the adult social care green paper should also be reflected.

**12a) Do you agree that these are the key cost drivers affecting children's services?**

**12b) Do you have views on what the most suitable data sets are to measure these or other key cost drivers affecting children's services?**

We believe that the list of cost drivers must be driven by further research. The evidence base is currently limited and must be expanded. We welcome the Government's attempts to establish an evidence base on the costs of children's services, but it is important that this is done at pace to ensure that results can feed into the formulae as soon as possible. The results of this in-depth research should suggest the list of cost drivers to be used in this formula.

We would draw attention to responses of individual local authorities as well as ADCS in populating the 'long list' for the research to consider.

One source of continued concern by our members is the financial sustainability of schools. While schools are funded through the Dedicated Schools Grant, councils carry the financial responsibility for any maintained schools that might find themselves with insufficient funding to carry on day-to-day services such as home to school transport and for supporting special needs services and school building requirements for all schools irrespective of status.

**13a) Do you agree that these are the key cost drivers affecting routine highways maintenance and concessionary travel services?**

**13b) Do you have views on what the most suitable data sets are to measure these or other key cost drivers affecting routine highways maintenance or concessionary travel services?**

This seems like a sensible starter list of cost drivers but we would draw attention to responses of individual local authorities and ADEPT. On highways maintenance, it is important to look at both road length and usage and it is welcome the Government recognised this in its starter proposal.

**14a) Do you have views on what the most suitable cost drivers for local bus support are?**

**14b) Do you have views on what the most suitable data sets are to measure the cost drivers for local bus support?**

We would draw attention to responses of individual local authorities and ADEPT.

**15a) Do you agree that these are the key cost drivers affecting waste collection and disposal services?**

**15b) Do you have views on what the most suitable data sets are to measure these or other key cost drivers affecting waste collection and disposal services?**

This seems like a sensible starter list of cost drivers but we would draw attention to responses of individual local authorities, ADEPT and other relevant organisations. It is important for analysis to consider whether waste collection and waste disposal services are driven by the same cost drivers.

**16a) Do you agree these remain the key drivers affecting the cost of delivering fire and rescue services?**

**16b) Do you have views on which other data sets might be more suitable to measure the cost drivers for fire and rescue services?**

We note that the Government is working with representative bodies of fire and rescue services on this formula, and that the starter list reflects the make-up of the 'current' fire and rescue formula.

This work should consider the type and nature of both domestic and commercial properties in an area, and look at ways to add sufficient flexibility to adapt to changing national resilience requirements.

**17a) Do you agree these are the key cost drivers affecting the cost of legacy capital financing?**

**17b) Do you have views on what the most suitable data sets are to measure these or other key cost drivers affecting legacy capital financing?**

We support the Government's starter list of cost drivers for this formula. However, it is important to keep in mind that the cost related to legacy capital financing is directly measurable for each individual local authority. The Government should review the pattern of these costs to see if they might be better dealt with as per Q10.

**18a) Are there other service areas you think require a more specific funding formula?**

**18b) Do you have views on what the key cost drivers are for these areas, and what the most suitable data sets are to measure these cost drivers?**

The Government should explore non-HRA housing support as a service to be assessed under a specific formula. Homelessness and temporary accommodation services represent a significant demand-led pressure for district and unitary authorities. Cost drivers should be tested to see how much overlap there is with a foundation formula as set out above. Only if there is a significant overlap would a separate formula not be necessary.

The list of service-specific formulae currently omits public health. The Government must make it clear that this will in effect be a 'service specific formula' within the proposed structure, unless the cost drivers used in the formula match the 'foundation' formula. Funding for public health will be part of the 75 per cent retention system, so the formula should be reviewed within the context of the Fair Funding Review rather than separately to the Review. This means that treating public health as a matter outside the Review would add an unnecessary degree of complexity.

#### Weightings of cost drivers and services against one another

### **19) How do you think the Government should decide on the weights of different funding formulas?**

The choice of weights for different funding formulas will have a significant impact on distribution of funding between different tiers of local government. The LGA would draw attention to responses of member authorities on this issue.

However, more generally, the control totals assigned to the formulae should be sufficient to fund services covered by those formulae at the point of transition and in the future. Local services face a funding gap of over £5 billion by the time the Fair Funding Review will be implemented – in addition to the £1.3 billion pressure to stabilise the adult social care provider market. The Review must come alongside sufficient funding; otherwise any outcome will not be sustainable.

### **20) Do you have views about which statistical techniques the Government should consider when deciding how to weight individual cost drivers?**

Assigning weightings to cost drivers is just as important as the choice of the drivers used. Our members would like to minimise ministerial judgement and for these weightings to be based on robust evidence and analysis.

However, some of our members have expressed concern over using statistical techniques which seek linkages to past expenditure levels on services as a way to derive these weightings, such as past expenditure-based regression. We recognise that this technique has strengths, such as the ability to explain how the analysis is carried out, but our members would like to avoid the possibility that the result of the analysis only reinforces the previous patterns of spending. We believe the Government should consider producing an in-depth explanatory paper on how this statistical technique could be used in a way that does not simply perpetuate historic spending patterns to provide further information to stakeholders, especially those without a deep understanding of statistics. This could form one of the set of technical papers planned as the work progresses.

Small-area modelling, which looks at population characteristics at ward level within a local authority as well as between local authorities, minimises this effect. We note that the level of detail required for small-area modelling to work can often be unavailable without bespoke data collections, which can carry significant cost. It is positive that the Government is considering using this technique for developing the social care formulae and we welcome the Government's research into the costs of looking after children as the basis for this technique on the children's services formula.

Furthermore, we strongly support:

- A 'sense check stage' of any statistical analysis with the use of expertise of finance officers and service directors. This has been discussed at the officer-level Fair Funding Review technical working group which came to the same view and we would support the consensus reached by local authority representatives in the meeting.
- Independent assurance of any options that are likely to be implemented.

**21) Do you have any comments at this stage on the potential impact of the options outlined in this consultation document on persons who share a protected characteristic? Please provide evidence to support your comments.**

It will not be possible to comment on the impact of the Review on persons who share a protected characteristic until the Government provides further details of proposals and exemplifications.

However, council services are under significant financial strain and this will only be aggravated by continued uncertainty over funding levels from April 2020.