LG Group Executive
13 January 2011

Item 1

Local Government Finance Settlement 2011-12 and 2012-13

Purpose of report

For decision

Summary

This paper summarises the proposals in the Provisional Local Government Finance Settlement for 2011-12 and 2012-13. These proposals implement at individual local authority level the decisions on future CLG grant levels made in Spending Review 2010. The paper reports on the action the LGA has taken since the Spending Review to pursue the agreed lobbying objectives and seeks Members' approval of the broad outline of the LGA response to the statutory consultation on the settlement, for which the deadline for responses is 17 January 2011.

Recommendations

Members are asked to:
1. note the work done to pursue the principal Spending Review lobbying objectives;
2. approve the outline response to the 2011-12 settlement consultation;
3. note that the LGA Leadership Board will be asked to approve the full LGA response to the settlement consultation.

Action

Group Finance Director

Contact officer: Stephen Jones
Position: Group Finance Director
Phone no: 020 7664 3171
E-mail: stephen.jones@local.gov.uk

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Local Government Finance Settlement 2011-12 and 2012-13

Background

1. Last November's Group Executive discussed the outcome of the Spending Review 2010 (SR10) and agreed further lobbying action to ensure that:

   1.1 the impact of the loss of Working Neighbourhoods Fund, on top of significant reductions in general grant, was fully understood by government;
   1.2 the impact for individual authorities of the depth of the cuts and in particular of the front loading of cuts was fully understood by government;
   1.3 mitigation of the impact of front loading was fully explored and progress made on that to the maximum extent possible;
   1.4 clarity on the levels of all new specific grants and the transition from existing grants was obtained; and
   1.5 decisions about the distribution of grant in the settlement were made as fairly and equitably as possible, recognising the difficulty of this issue.

2. Following the Group Executive, the Chairman and Group Leaders issued an open letter to the Secretary of State for Communities and Local Government on 29 November. This was followed up with a meeting with the Secretary of State on 30 November, at which five practical proposals to mitigate the risk to local services from the settlement were discussed. These five proposals were, in summary, for the government to:

   2.1 reduce the impact of front loading;
   2.2 increase the size of the proposed £200m capitalisation to be allowed;
   2.3 clarify the position on all 'missing' grants;
   2.4 allow councils more flexibility to raise income locally; and
   2.5 avoid unfair grant distribution.

Outcome for local government

3. The Provisional Local Government Finance Settlement was published on 13 December. The LGA issued an on the day briefing summarising the contents of the settlement and setting out key messages. As our briefing noted, the government had responded positively to some of our lobbying, for example in the creation of the new £85m transition grant to mitigate the level of cuts faced by authorities with the largest reductions in their 'spending power'. Against that, the level of cuts imposed on councils was greater than the average 10.7% number

announced in SR 2010, and there was no movement on capitalisation.

4. A large number of authorities have contacted the LGA to express their concern that the size of the cuts announced presents them with significant difficulties. A number of authorities, particularly larger authorities, have told us that it would be particularly helpful for them if additional flexibility on capitalisation could be obtained.

5. The Settlement offered both local authorities and representative associations an opportunity to meet with CLG Ministers to make representations. The LGA has sought a meeting as, no doubt, have many local authorities.

6. LGA officers have, in the meantime, been carrying out a detailed analysis of the Settlement and obtaining feedback from member authorities. This has suggested a number of points that might profitably be pursued. These are summarised in paragraphs 7-13 below and it recommended that all these points are incorporated in the LGA's response to the formal consultation on the 2011-12 settlement.

Business Rates

7. The Formula Grant that CLG distribute to authorities is made up of revenue support grant from CLG, formula police grant from the Home Office and redistributed business rates. The amount of business rates income that can be distributed is set by the Secretary of State in the Settlement each year. For 2011-12 the amount is £19bn, considerably lower than LGA officers were expecting.

8. The Settlement material includes an explanation and a detailed calculation of this amount. The detailed calculation is based on what CLG describe as 'provisional outturn' figures for 2009-10 that record a <u>deficit</u> on the business rates account of £900m as at 31 March 2010. However, the audited accounts for the business rates pool, published in July 2010, record a <u>surplus</u> on the account of just over £200m. CLG have in addition introduced a new 'calibration adjustment' into their calculations. They say that this is based on historic experience of differences between the local authorities' estimates of business rates expected to be received and the outturn figures. This 'calibration adjustment' reduces the amount available for distribution in 2011-12 by around £1,200m.

9. In summary, therefore, these adjustments reduce the amount of business rates that might be expected to be distributed to English local authorities by more than £2bn. LGA officers have asked CLG officials to provide more information to demonstrate that their calculation of the distributable amount is not over-pessimistic. This is a particularly important issue for local government given the severity of the front loaded cuts. Whilst there is no difficulty with a prudent approach to management of the business rates pool that seeks to avoid the pool going into deficit, authorities would rightly be very unhappy if by March 2012 a

substantial surplus had built up in the pool that might otherwise have been applied to ease front loading problems. At the time of preparation of this paper, no reply had been received to the LGA's enquiries. An update will be given at the meeting, and it is recommended that this issue be explored fully.

Capitalisation

10. Officers are seeking to develop the case for increased flexibility on capitalisation, using information obtained from member authorities. As members may be aware, in addition to this issue being discussed at the LGA's meeting with the Secretary of State, capitalisation was explored at a recent evidence session of the CLG Select Committee of the House of Commons. The preliminary uncorrected transcript of evidence records the Secretary of State as saying:

    "I made it absolutely clear to the LGA … that if they would like me to increase the capitalisation, of course I would do that. It has to be against the context of the settlement and public expenditure, so I'd have to reduce the amount of grant that would go into local authorities, but if they would prefer to have a smaller grant and greater capitalisation, I'm open to that kind of persuasion. If they feel they need £1 billion, I'm quite happy to take £600 million out of the grant allocation to allow that to happen, but I took a view—this is how we put these sorts of things together— that it was better to put the maximum amount into the block grant than to save money for capitalisation. So it was a kind of deliberate policy. I have to say, having put that to the leaders of the political parties a few weeks ago, they didn't seem to be as keen to press the point. I might have been misjudging them."

11. Following that, the LGA Chairman has written to the Secretary of State, the Chief Secretary of the Treasury and the Chair of the Select Committee to confirm our view that allowing additional capitalisation would not work against the government's policies to reduce the deficit. The Chairman's letter sets out the Association's position in the following terms:

    "In your evidence, you said to the Committee that you had made it clear to us that it would not be possible to increase the £200m capitalisation proposed for 2011-12 without a corresponding reduction in grant. That is correct. However, you went on to refer to your impression that when you had made your views known to us we were not keen to press our argument on capitalisation.

    "I am afraid that, if that is your interpretation of our reaction, it is entirely incorrect. We do not accept that capitalisation is to be equated with additional borrowing, as you suggested in your further evidence to the Committee, or that allowing additional capitalisation would for that reason work against the government's policies to reduce the deficit. Many authorities have cash and capital reserves to fund redundancy and other costs associated with the need to make a significant reduction in spending in future years. Other authorities have assets they could sell, for example to rationalise their office estate and save money. Expecting authorities to lock up these kinds of funds and insisting that they cannot be used to cover redundancy costs may be a reflection of the current bureaucratic orthodoxy but it amounts in our view to an entirely unjustified constraint on the proper management of local public spending. We shall therefore be continuing to press our argument on this matter and look forward to discussing it with you in the New Year."

Specific grants and transfers into and out of Formula Grant

12. The detail of the Settlement and further information supplied since by CLG and other government departments has resolved most issues concerning 'missing' grants. The grant structure has been considerably simplified, which is welcome, but there are various other issues and consequences that are unwelcome, including in particular:

    12.1 **Top slice for academies' central functions** - £148m in 2011-12 and £265m in 2012-13 has been removed from formula grant to pay for academies' central functions. The reduction has been taken from education authorities on a pro rata basis irrespective of whether academies exist in their areas. Furthermore, as was noted in the Impact Assessment produced by the Department for Education in connection with the Academies Bill, the marginal benefit to local authorities in having fewer schools for which to provide central functions is likely to be close to zero in most authorities. This funding reduction is therefore not justified on the government's own evidence.

    12.2 **Early Intervention Grant** – This new grant is unringfenced, which is welcome. However, after taking into account previous unringfenced grants funded by DfE that have now ended, there is a reduction of 27% in total funding.

    12.3 **Concessionary Fares** – The methodology used to deal with the funding for concessionary fares through formula grant is regarded by many authorities as deeply unsatisfactory, because existing grant baselines are adjusted by reference to all spend net of special grant, not just spend on the statutory scheme. This has the effect of permanently depriving a number of authorities of substantial funds hitherto used for their own discretionary spending. A better approach would be the one proposed in the LGA's response on the consultation on Formula Grant, namely that concessionary fares funding is wrapped up with the Bus Service Operators Grant and put into a **local commissioning pot under the control of local authorities.** This would allow the funding to be targeted more efficiently to provide better value for the taxpayer.

Technical issues

13. Member authorities have drawn to our attention a number of more technical issues relating to the grant settlement that have significant impacts for them. These include:

    13.1 The construction of the baseline for **the new £85m transitional grant** is defective. Firstly, it includes local parish precepts, which are not controlled by the billing authority and in no sense part of its 'spending power'. Second, it treats certain grants made on a partnership basis across a number of authorities as part of the 'spending power' of the authority that receives the grant on behalf of the partnership as a whole. Third, it excludes from previous spending power certain DfE grants that have now ended. These technical defects have the impact of reducing transitional grant by modest overall but, for some authorities, individually significant amounts.

    13.2 The basis of inclusion of **Supporting People** funding as a 'tailored distribution' on an undamped basis is regarded as unsatisfactory by many authorities.

    13.3 For those authorities receiving funding for their **supported borrowing**, no account has been taken of the increase in the Public Works Loans Board interest rate.

Recommendations

14 Members are asked to:

    14.1 note the work done to pursue the principal Spending Review lobbying objectives;

    14.2 approve the outline response to the 2011-12 settlement consultation as set out in paragraphs 7-13 above;

    14.3 note that the LGA Leadership Board will be asked to approve the full LGA response to the settlement consultation.

Financial Implications

15 This is core work for the finance team and all work is contained within existing budgets.