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Dear Stephen

Calculation of the Distributable Amount National Non-Domestic Rates

Thank you for sending me the papers relating to the Secretary of State's determination of the Distributable Amount of NNDR for 2001-12. Whilst this is a relatively arcane area of law, I am able to come to some clear conclusions, as follows -

1 The Secretary of State is required to determine the Distributable Amount so as to produce a Zero Balance on the NNDR account, and has no legal power to plan for a surplus

The process which the Secretary of State is required to undertake in calculating the Distributable Amount is defined in Paragraph 9 of Schedule 8 to the Local Government Finance Act 1988. This provides that he must estimate the amounts which will be credited into the account during the year, and the sums which will be debited to it (i.e. the balance of relevant cash payments which will be made during the coming year). He is allowed to make any reasonable assumptions in order to come to such estimates, but the estimates which he has made for 2011-12 are described in the CLG paper "the Distributable Amount for 2011-12" and set out in the spreadsheet which you provided to me, as Receipts of £2 22,012 million, with Payments totalling £2,909 million. Paragraph 9(3) then provides that, where the Receipts exceed the Payments, the Secretary of State shall calculate the amount equal to the difference (£19,102 million) and Paragraph 9(4) provides that this difference shall be the Distributable Amount.

In this instance, the Secretary of State has not set the Distributable Amount as a sum equal to the difference, but has chosen to "budget for a surplus" and set the Distributable Amount some £102 million lower, at £19,000 million. That is simply unlawful. Having made his estimates of the likely payments into and out of the account, he is required to set the Distributable Amount simply as the difference between the two sums.

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I advise that, if the issue were tried, a Court would have to find that, on those estimates, the Secretary of State was required to set the Distributable Amount at £19,102 million. Further, having made his estimates for 2011-12, it is not now open to the Secretary of State to review these estimates in order to come up with a balance of £19,000 million.

It is another matter whether there is any merit in actually litigating this point. The Secretary of State has now determined the total amount of grant payable to local authorities for 2011-12, and then calculated the proportion of this sum which is to be distributed as Revenue Support Grant by deducting the Distributable Amount from that total. So, if the Secretary of State were now to have to increase the Distributable Amount and so pay more money to local authorities in 2011-12 as redistributed NNDR, it would be difficult for the Secretary of State to make an adjustment in RSG claw back this sum in the same year. So the effect would be simply to increase the actual year-end deficit on the NNDR account, and so reduce the Distributable Amount for 2012-13.

However, it must be said that the Secretary of State's casual and unlawful decision to "budget for a surplus" of £102 million is the equivalent of approximately 5,000 front line jobs in local authorities.

2 In determining the Distributable Amount for any year, the Secretary of State is entitled to take account both the actual cash deficit in the account from the previous year and any anticipated receipts and payments to and from the account which arise from the previous year.

The NNDR account is prepared on a cash basis – notional receipts of NNDR from billing authorities and compensation payments in lieu of NNDR, less notional payments by CLG to billing authorities where the amount of NNDR for which businesses in their area were actually liable proved to be lower than the billing authority's original estimate, and the Distributable Amount. The sums which may be credited and debited to the account for any one year are defined by Paragraph 2(1) and (2) of Schedule 8, and include payments made under Paragraphs 5(10) [the unaudited surpluses or shortfalls in cash payments from billing authorities below their estimates for the previous year] and (14) [any further surpluses or shortfalls determined following audit of each authority's NNDR account, for the previous year].

Accordingly, such actual surpluses and shortfalls, which can only be determined after the year-end, fall to be received or paid into the national NNDR account in the year following the year to which they relate. Thus, where the actual NNDR collected in Year One proves to have been £100 million less than the estimates of the billing authorities, which informed the Secretary of State's estimates and therefore the Distributable Amount for Year One, that £100 million not only can legitimately, but must, be carried forward and taken into account in determining the Distributable Amount for Year Two, thus ensuring that, over a period of years, the Distributable Amount paid to local authorities does accurately reflect the amount of NNDR actually collected..

3 The Secretary of State has failed to provide other than summary supporting information to validate the figures which he has used in his determination. This does not invalidate his determination, but it is radically at odds with the transparency on public expenditure which the Secretary of State requires of local authorities

Whilst the Secretary of State has set out in the paper “The Distributable Amount for 2011-12” an explanation of the assumptions which have informed his estimates of receipts and payments into and out of the NNDR account for 2011-12, he has done this only in very broad terms –

- The 2010-11 deficit of 2,270 million is not supported by a tabulation of estimates and actual collection for individual billing authorities, although this information is collated within CLG and must be readily available;
- There is no explanation of why transitional relief, small business relief and empty property relief have proved not to be cost neutral to billing authorities, despite the Government’s intention that they should be so. These reliefs account for some £910 million of the deficit and the reasons for these deficits, and whether these reasons will endure into 2011-12 are fundamental to the Secretary of State’s assumptions which underlie his determination of the Distributable Amount for 2011-12;
- The Secretary of State reports baldly that a review of the difference between NNDR 1 (estimate) and NNDR3 (outturn) forms has led him to make the assumption that there will be shortfall of £237 million, but no supporting data is provided. This review has also led to his including a provision (the “Calibration Adjustment”) of £625 million for 2011-12. Incidentally, the fact that the Secretary of State is making these provisions for any such shortfall means that there is less need to “budget for a surplus”.

The total absence of detail to support figures of hundreds of millions is in striking contrast with the Secretary of State’s strictures to local authorities to provide total transparency for all payments of £500 or more and is equally at odds with the requirement on local authorities to disclose the Chief Finance Officer’s Background Papers which informed the preparation of the draft Budget.

4 Where NNDR reliefs which were supposed to be cost-neutral prove to reduce the amount of NNDR collected, and so result in a deficit which reduces the Distributable Amount in the following year, the Secretary of State should make equivalent provision in the Block Grant calculation to ensure that the Government meets the actual cost of such legislative burdens.

Whilst I appreciate that the determination of the total amount of support for local authorities is essentially a political decision, the Government has undertaken to identify the financial impact of legislative change on local authorities and make equivalent

contribution. In this instance, there were in-year changes to the level of Small Business Rate Relief in October 2010 resulting in an additional cost of £195 million. But the same principal should apply where it is clear that reliefs which were supposed to be cost-neutral have proved to be costly. In such circumstances, the Government's assessment of the total amount of support to local authorities (to be split between the Distributable Amount and the RSG) should be predicated on an explicit statement of the current level of local authority expenditure extrapolated to the next year to take specific account of the consequence of demographic and inflationary pressures, and setting out the impact of legislative changes. Only once that aggregate sum has been determined should the Government identify its assumptions as to efficiency savings, and then its "political" cut in support to local authorities.

This calculation should exist within CLG and it would be interesting to try an FoI request to secure its disclosure, hopefully leading to its automatic publication in subsequent years.

I hope that this is clear, but please do come back to me if you need amplification of any part of this advice.