Report of the Director of Finance

Agenda Item No:
Meeting: 27 September 2011

NORTH LINCOLNSHIRE COUNCIL

CABINET

CONSULTATIONS ON PUBLIC SERVICE FINANCIAL REFORMS

1. OBJECT AND KEY POINTS IN THIS REPORT

1.1 The report introduces a series of consultations which are part of the government's reform agenda. Each has implications for the funding and delivery of local services.

1.2 There are three covered here:

i. Business rates
ii. Council tax benefit
iii. The school funding formula

1.3 The paper outlines the proposals, the key issues and implications for councils, and a proposed outline response.

2. BACKGROUND INFORMATION

2.1 The government has an ambitious legislative programme which includes a radical redesign of public services. The principles which underpin the new vision include

- Decentralisation of power to individuals and communities
- Freeing front-line service providers to innovate and encouraging diverse provision
- To make public services responsive to those who need them;
- And ensuring fairness through equality of access.

2.2 The consultations covered in this paper address three specific proposals:

- The retention of business rates income by local authorities
- The transfer of responsibility for council tax benefit to local authorities as part of a wider reform of the benefits system
- A new formula for government funding of schools

2.3 These separate consultations invite responses from all interested parties.

3. OPTIONS FOR CONSIDERATION

3.1 This report highlights key issues, evaluates the benefits and risks associated with each proposal, and indicates a line of response. A précis of each proposal with commentary is included in the appendices to this report.

4. ANALYSIS OF OPTIONS

4.1 Where the consultation offers a choice of options a preferred option is indicated.

5. RESOURCE IMPLICATIONS (FINANCIAL, STAFFING, PROPERTY, IT)

5.1 Financial, staffing and property implications are likely to arise if these proposals are enacted. At this stage the proposals only have consultative status, therefore the assessment of impact can only be provisional.

6. OTHER IMPLICATIONS (STATUTORY, ENVIRONMENTAL, DIVERSITY, SECTION 17 - CRIME AND DISORDER, RISK AND OTHER)

6.1 There may be indirect implications

7. OUTCOMES OF CONSULTATION

7.1 This paper reflects the professional view of appropriate officers of the council.

8. RECOMMENDATIONS

8.1 That the consultations and comments on them be noted, and responses to each of the consultations finalised in consultation with cabinet members.

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Background Papers used in the preparation of this report

Local Government Resource Review: Proposals for Business Rates Retention
Localising support for council tax in England
A Consultation on School Funding Reform: Proposals for a Fairer System

Appendix 1

Local Government Resource Review: Proposals for Business Rates Retention

Proposal

The DCLG has recently issued a consultation paper as part of the Local Government Resource Review, on proposals for Business Rates (NNDR) retention by Local Authorities.

Currently, councils collect business rates due in their area, which are paid over to central government. They are then pooled and redistributed to councils as the largest element of formula grant, but distributed according to relative resources and relative needs of different local authorities as measured by a range of socio-economic indicators and the size of the council taxbase.

Letting councils retain business rates raised locally would, government argues, create a link between local government finance and the economic success of an area, encouraging councils to attract development to their area. This would happen, for example, through greater incentives to grant planning permissions in appropriate cases.

However the scheme proposed aims to offer some protection for areas with relatively low resources and/or high need by formalising a baseline entitlement. There would therefore continue to be some redistribution of business rates between areas and the consultation focuses on how this should work. The government would also continue to set a national rate in the pound, and determine the system of reliefs to business that are available. So businesses would see no change in the way their bills are calculated.

The consultation proposes:

1. At a national level, to deliver a fiscally sustainable system and avoid putting the government’s deficit reduction programme at risk, the business rates retention scheme will be managed within the expenditure control totals for 2013/14 and 2014/15 which were set out in the spending review
2. Current legislation requires all business rates income to be returned to local government. On current trends business rates will soon exceed the total value of formula grant. The government intends to pass this surplus back to local government via the New Homes Bonus and other specific grants. So local government will only benefit from any growth in NNDR receipts over and above that already assumed by government
3. To establish a ‘fair’ starting point for all councils by taking the formula grant distribution for 2012/13 as the baseline
4. A system of tariffs (payable by councils that collect more business rates than they receive back in formula grant) and top-ups (payable to councils that receive more than they collect) will ensure that no council is initially worse or better off as a result of the change. These tariffs and top-ups may be fixed in future years, or could be uprated using, for example, RPI.

5. Councils will be able to retain a significant proportion of any growth in business rates that takes place above the current level, and similarly would face reduced receipts in cases of low or negative growth.
6. A levy is proposed to recoup a share of 'disproportionate growth' to fund significant negative volatility in other areas and provide a degree of protection, described as a safety net, against significant losses, such as from major plant closures or appeals. Various ways of calculating disproportionate growth are suggested
7. Councils would keep any increase in business rates due to renewable energy projects, which would be discounted in the calculation of any levy
8. Adjustments would take account of changes in business rate yield resulting from five-yearly valuations, and the government could reset the system if it was felt that resources no longer met changing service pressures within individual council areas.
9. Pooling arrangements could be entered into in local areas (eg LEPs) to smooth volatility over a wider area, on a voluntary basis but subject to agreed governance arrangements
10. Tax Increment Financing is proposed to be introduced alongside existing Business Rate Supplement and Business Improvement District arrangements. Such a scheme would allow councils to borrow against future growth in business rate revenues and so provide, for example, infrastructure that would support future development. Local retention of business rate income starts to facilitate such schemes. Separate proposals to allow LEPs to retain business rates income from Enterprise Zones would not be affected as the government would exempt such income from the calculation of top-ups and tariffs.

The consultation period runs to 24 October, and the government has posed a set of detailed questions and more recently has issued a series of eight technical papers on particular aspects. These will be evaluated in more detail before a final response to the consultation is prepared.

Comment

Returning business rates to councils is to be welcomed as providing increased influence over a key funding stream. However the particular nature of North Lincolnshire does present some risks to the council as well as opportunities if the scheme goes ahead in the form suggested.

The council's response needs to consider the technical merits of the proposals, the balance of risk and opportunity they offer, and their essential fairness taking account of how they might impact locally. Particular issues are:

1. The council currently loses £3m formula grant as a result of damping, i.e. without this protection for authorities with reducing entitlements the formula would pay the council £3m more in recognition of its relative needs and resources. Setting the baseline at the level of the 2012/13 settlement locks in a level of funding which does not reflect the current assessment of need in the area. We should argue strongly for the new funding arrangements to start with undamped formula grant figures.

2. The government proposes to limit the potential benefit to local authorities by adhering to spending targets for NNDR already set. While the need for national expenditure control is understood, government needs to review its approach in future spending reviews to ensure that local government can benefit more fully from the opportunities the scheme presents.

3. North Lincolnshire is a net contributor to the national business rates pool. In 2012/13 the contribution is projected to be £77.1m with £57.9m returned as formula grant, a difference of £19.2m.This means that the council will be required to pay a tariff into the new funding mechanism of this order for redistribution to other authorities. These authorities receive a top-up to local resources.

4. The nature of the council's economic base brings both risks and opportunities. The high level of business rates locally reflect historical developments in the steel, chemicals and energy sectors and constitute a large element of the taxbase. Since the introduction of the National Non Domestic Rate in 1990 the council has paid over the rates collected into a national pool. The steel industry represents around 20% of business rates collected, with many related businesses in supply and distribution. Any contraction in its operations would severely reduce business rate income. The same concerns apply to the two power stations and two refineries which together represent a further 20% of the taxbase. In these circumstances the government safety net arrangements need to work effectively.

5. Future development on the Humber Bank, together with other initiatives designed to diversify the area's industrial base, could bring other significant business rates receipts which could offset losses in historical industries or provide growth. However proposals to waive business rates from new development in an Enterprise Zone or to pool receipts for use by a Local Economic Partnership could limit the ability to offset a decline in one with an increase in the other.

6. The consultation model illustrates the effects of a 10% safety net. Taking the proposed level of grant for 2012/13, £58m, this means the council would stand the first 10% of any reductions in taxbase or £5.8m per annum, equivalent to 8.7% on council tax. This would be £6.1m if we start from an undamped baseline. A fall of this magnitude is clearly a possibility and would cause severe problems locally, We should argue for the safety net to be set much lower or at zero – this would be consistent with the concern to protect councils existing grant entitlements.

Proposal

This is part of the government's radical review of the benefits system. The intention is to simplify a complex system and to ensure that people will always be better off in work than on benefits. It expects that this incentive to work will reduce the cost to the state of benefit payments.

At the heart of proposals is a single Universal Credit for working-age claimants to replace six income-related benefits: jobseeker's allowance, housing benefit, child tax credit, working tax credit, income support and income-related employment support allowance. The Universal Credit will start for new claimants in October 2013, with existing claimants migrating over the following four years.

The proposal for council tax benefit is to localize what is currently a national scheme. It would still operate as a reduction of council tax liability not a cash payment and would meet the government's localism agenda and greater local financial accountability, sitting alongside proposals for local referenda on council tax increases. It also makes clear that pensioner entitlements to council tax support will be the same under the new arrangements. The consultation proposals suggest that a transfer of responsibility to the local level will give an additional incentive to local authorities to promote economic growth.

At present billing authorities like North Lincolnshire administer housing benefit and council tax benefit and both are funded by government subsidy. From 2013 authorities will receive a grant towards a local council tax benefit scheme, 10% below the current funding level (a saving of £500m nationally, £1.3m in North Lincolnshire). Housing Benefit responsibilities will cease over a timetable which is still to be determined.

Currently around 17,000 people in North Lincolnshire receive council tax benefit, 70% of whom receive the maximum benefit. The balance of caseload is 51% pensioner/49% working age. One third of those of working age do not receive income support or job seekers allowance, but they might be in receipt of other benefits like disability or attendance allowance. The total subsidy in North Lincolnshire is £13.1m.

Comment

There are a number of key issues to cover in a response:

<u>Delivery of the ambitions for benefits reform.</u>

1. Make the benefits system less costly for the taxpayer

   The proposal would make a contribution of £500m to deficit reduction though some additional costs may arise for local authorities.

2. Better off in work than on benefits

   The proposal is to protect current pensioner entitlements; which therefore means that existing working age claimants could face an average 20% reduction. This could act to encourage claimants to return to work as the government wishes, but would also affect claimants in work on low income.

3. Simplify

   The attraction of the universal credit is that it aims to simplify a complex system. However a separate council tax benefit, while increasing local control, retains a level of complexity. Individual benefit claimants may not be able to access benefits from a single point, and entitlements may vary between local authority areas.

Fairness/Consistency

The consultation makes clear that there are certain low-income groups it does not expect to work to increase their income. It therefore wishes to protect pensioners from any change in award, and invites councils to identify other groups they would wish to protect. For example this might be families with children and people with disabilities. Protection for some may mean more significant benefits reductions for other claimants.

The consultation highlights a number of issues to be addressed so that schemes fit with overall government policy objectives:

- How local schemes fit with the universal credit, and support the incentive to work
- How to incentivise local authorities to co-operate to minimise risk and achieve administrative efficiencies
- How to make neighbouring schemes similar to avoid confusion for claimants
- How to protect the interests of precepting as well as billing authorities
- The potential difficulty of the DWP meeting different information requirements of different schemes

If the government does not wish to address these issues through the inclusion of council tax benefit in the Universal Credit, then the council may need to look at arrangements like shared service arrangements in order to resolve these issues.

Cost of local schemes

The 10% reduction in grant would cost the council £1.3m if it maintained the same entitlements as now with the same claimant numbers and mix. That equates to 2% on council tax.

Growth in the number of those entitled to a council tax benefit discount, either pensioners or those of working age, would add a further pressure. The consultation does recognise that a fixed grant would leave councils exposed to changes in demand in year, and potentially longer-term. This is because government subsidy currently picks up the cost of all appropriate claims without setting an annual cash limit; but government does not want councils to ration or amend the local scheme mid-year.

When determining the grant for administration of council tax benefit it will need to be disaggregated from housing benefit. Government plans to make assumptions about savings councils could make through joint administration or operating a joint scheme when setting the level of that grant.

The risk transfer involved

By moving to fund Council Tax Benefit through a cash limited grant, there is a significant risk transfer to local authorities, as it could be difficult to administer schemes within cash-limited resources. The consultation does not say how year to year increases in the level of grant will be planned and managed. It implies a fixed grant sum for a number of years to facilitate local planning.

It is not clear whether grant will increase if there is a growing number of the elderly entitled to the benefit as the population ages. Significant local economic shocks such as a major industry closure could also substantially increase benefit costs, but the consultation paper suggests it is for the local authorities to develop local mechanisms to manage these risks. The paper suggests one option could include collaborative approaches with neighbouring authorities or the LEP. However the approach taken to localisation of business rates recognises the need for a national safety net for economic shocks and the same would be appropriate for council tax benefit costs. The combined effect of a significant reduction in business rate (arising from localization proposals) and increased council tax benefit costs could restrict the capacity for local action to support the economy at a time of need.

Administrative deliverability

Introducing the new council tax benefit system from 1st April 2013 is a challenging target. Primary and secondary legislation is not due until 2012, which leaves little time for the design and consultation of new schemes, the development and procurement of new systems, and the robust evaluation of scheme costs in council budget setting. There are a number of practical issues:

- The separation of housing benefits and council tax benefit delivery, with staff transfers to DWP
- Transitional arrangements from the old system to the new
- The procurement of new IT systems or significant adaptation to existing systems where there are a limited number of software companies able to deliver change and potentially 326 separate schemes to be created
- An implementation date which differs from that for the universal credit (October 2013)
- The establishment of a single national fraud service for benefits but councils to manage fraud investigation for council tax benefit

- The administrative requirements of collecting council tax from a greater number of people on low incomes for whom, currently, the benefit is automatically calculated and transferred.

Efficiency/Collectability

A reduction in council tax benefit payable to some claimants may lead to councils seeking to collect small amounts of cash from low income groups who under the current system would have had all or a large part of their council tax covered directly by a transfer of benefit to the council. This could lead to potential collection difficulties: the community charge of the early 1990s illustrated the potential difficulty of collecting small amounts from low income groups.

Appendix 3

A Consultation on School Funding Reform: Proposals for a Fairer System

On 19 July the government launched the second part of its consultation on school funding reform, which lasts until 11 October. The consultation document sets out proposals for the mechanics of a new funding system, the contents of a new national formula and future funding arrangements for the pupil premium, early years provision and high cost pupils. It also clarifies the responsibilities of local authorities, schools and academies in relation to central services.

The focus is on how Government funding is allocated to local areas, but local authorities will, as now, have a role in distributing the funding through a local school funding formula agreed with the Schools Forum. These local formulae are to be simplified.

Proposal

The DFE would like the whole school funding system to have the same clarity and transparency and propose to introduce a new formula which will provide funding to local authorities, schools and Academies on a fair and transparent basis. The aims of the new system are to:

- Support the needs of pupils;
- Be clear and transparent;
- Enable schools and Academies, sponsors and Free School proposers to make informed decisions about their provision;
- Enable schools and Academies to be funded on a broadly comparable basis.

The new system will enable local circumstances to be taken into account in the setting of schools' and Academies' budgets. There will remain a role for local authorities and Schools Forums, including Academy representatives, in managing local pressures and priorities.

It is acknowledged that the changes will require shifts in funding between schools and areas and there will be transitional arrangements required to ensure stability in school funding.

The current system of school funding will continue for 2012-13.

It is proposed that the new national formula will include:

a) A basic amount per pupil;
b) Additional per pupil funding for deprivation;
c) Additional funding to protect small schools;
d) An adjustment for areas with higher labour costs.
e) Possible additional funding for pupils who have English as an additional language.

These factors will be used to determine the level of resource for each local authority which will then be distributed between schools using a local formula agreed with the Schools Forum. The determinants of a local formula will be simplified to enable more consistency between areas.

The new funding formula will be allocated in four blocks:

i. Schools block (functions done or paid for by school and functions where there is local discretion to retain centrally for maintained schools)
ii. High Needs Pupils block
iii. Early Years block
iv. Central Services block

In addition there would be elements of school support funded from the local authority's resources as now. Currently that means council tax and formula grant, but relocalised business rates and council tax from 2013/14 (see Appendix 1).

v. General local authority funding (functions done or paid for by the local authority for all maintained schools and academies)
vi. Local Authority Central Spend Equivalent Grant (LACSEG) funding block (functions which must be done or paid for by the authority for maintained schools but would be within academy budgets - this would be split between local authorities and academies

Comment

The current system allocates a total grant to the local authority based on a guaranteed unit of funding per pupil. This ranges from £4,428 to £9,373 per pupil in 2011-12 with the England average being £5,083. North Lincolnshire is funded £4,818 per pupil. There have long been concerns at the wide disparity of funding, with similar schools in different parts of the country receiving widely different resources. The new simpler national formula aims to address this.

Schools Block (block 1)

The proposals will lead to clarity and transparency of funding allocations, particularly if it is calculated at school level.

The schools block will be calculated either using area data or using school level data. The allocation will be made at authority level which will be distributed to schools using a local formula. The factors which are being proposed are significantly reduced and are in line with the new North Lincolnshire formula. The proposals consider whether Academies will be funded based on local formulae, which would be more transparent and simple to administer. The new funding system will strengthen the role of Schools Forum in applying local factors.

The deprivation factors being considered are based on eligibility for free school meals either pupils at January census or pupils at January census who are or have been eligible at some point in the last 3 or 6 years. This may be subject to the governments plans for Universal Credits as a replacement for things like free school meals.

The consultation suggests that a lump sum of £95,000 would be allocated for each primary school in order to provide the level of protection for small schools. Depending on what impact this had on the per pupil rate for primary schools this could possibly benefit North Lincolnshire primary schools if this was allocated in full through the local formula. The wider sparsity factor is likely to give more benefit to North Lincolnshire than the narrow measure.

High Needs Pupils (block 2)

The High Needs Block will fund SEN provision including statement funding and special school provision. There is also provision within the Education Bill to delegate budgets to Pupil Referral Units and there also may be a transfer of responsibility for alternative provision to schools in due course.

If the funding is allocated based on individual needs of children and young people then this would be a better mechanism for funding. The consultation proposes that where a pupil's needs cost less that £10,000 in total this would not, for the purpose of the national formula, be deemed to be high need and the assumption would be that the funding would be found from the mainstream funding blocks. This could be flexed locally. The assumption is that mainstream schools should meet from their base budgets the first additional tranche of cost for any actual high needs pupils, which may be set at around £6,000 – and above that cost the funding would come from the local authority as an additional payment.

To avoid perverse incentives, it is proposed that special schools and units receive a base funding reflecting the assumed £10,000 in mainstream school base funding. Funding above the base would be based on individual pupil's needs. North Lincolnshire Special Schools are currently funded a base funding of £4,728 per pupil primary and £5,426 per pupil secondary. There are 9 place bandings ranging from £6,457 per pupil to £34,200 per pupil. It is also proposed that the new methodology be extended to post 16 provision.

The consultation considers how best to administer the funding to academies, alternative providers and free schools for high need pupils. One option would be for the Education Funding Agency to fund the £10,000 per place (or pupil) with the local authority funding any top up required from their overall allocation.

Alternative provision is by definition additional to the mainstream provision and therefore there is logical that the funding mechanisms should follow that of special school provision.

Early Years (block 3)

Proposals to simplify the local formula would be welcomed. The change to using a formula to calculate the block would bring consistency across local authorities. As with the Schools block there would need to be a transitional period to avoid turbulence for providers. This block could be calculated based on current levels of spend on early years provision or built up based on pupil data.

There is a further **Central Services block (block 4)** largely Schools Forums related expenditure.

Timing and local implications

A key issue is what the reform will mean for this area. Implementation from 2013-14 would mean that local authorities in the lower funding quartiles would start moving closer to average sooner (North Lincolnshire schools funding is currently 45 out of 151 and could potentially benefit from the changes to the national formula).

However, with transitions required within the tighter spending envelope for 2011/15 there is unlikely to be any significant change in resources until the next spending period. As long as the decision is made early then we can plan our budgets accordingly to give schools and providers some stability over their financial planning.