Introduction

1. This Government’s aim for local government finance is to provide councils with the freedom to use funds in a way that responds to local needs and priorities, ensures financial sustainability and supports sound financial management on the part of authorities themselves.

2. The Spending Review is the Government’s primary mechanism for determining questions of finance for the local government sector in the medium term. As with previous Spending Reviews, the 2019 Spending Review will decide the overall amount of funding available to local government, whether through retained businesses rates or grants, as well as determining the overall central government policy on council tax.

3. Alongside this the department is supporting the Department for Health and Social Care on the Social Care Green Paper which will set out Government’s plans for a sustainable social care system, and on the implementation of the NHS Long Term Plan. Both of these are vital to helping to secure the sustainability of local government within and beyond the next Spending Review period.
Scope of this submission

4. For the purposes of this submission, we will cover the aspects of local authority funding which are under consideration in the Spending Review and the work that is under way to give the authorities the freedom and support required to deliver their services.

5. This will include:
   a. The current system and policies, including business rates retention, council tax, settlement allocations and our work on local government efficiency
   b. Our work to support the Spending Review.
The current system and policies

6. The Spending Review is an agreement across Government on key decisions relating to the distribution of funding, including the overall quantum of funding for local government. This includes the relative priorities for different services, the balance of income from business rates and council tax, and other grants.

7. Over the five-year Spending Review period from 2015-16 to 2019-20 councils will have had access to more than £200 billion. Local authorities’ revenue funding available for local services, including council tax and locally retained business rates, is known as their “Core Spending Power”. The total Core Spending Power of authorities in England for 2019-20 is £46.4 billion, an increase of 3.8% from 2015-16 where Core Spending Power was £44.6 bn.

8. The composition of Core Spending Power has changed over the period of the Spending Review. Revenue Support Grant, an unringfenced block grant from central government, has reduced from £9.9bn in 2015-16 to £2.2bn in 2019-20, while baseline funding has increased from £11.3bn to 12.3bn, and available council tax revenue increased from £22bn to £26bn.

9. This is part of an ongoing objective to give local authorities more control over the money they raise. Local authorities have campaigned for more flexibility over the income they generate – including the ability to raise council tax. Over the course of this Spending Review period local government has moved towards increased self-sufficiency, while central Government has protected council tax-payers from excessive bill increases through setting referendum thresholds.

Business rates

10. Business Rates (National Non-Domestic Rates) are a tax on non-domestic properties that are capable of beneficial occupation. Non-domestic properties are business properties such as shops, offices, warehouses and factories. Each property has a rateable value. Rateable values are assessed on the basis of the annual rent that a tenant would be willing to pay for it on the open market. All properties are assessed in a similar way to ensure that the burden of the non-domestic rate is shared fairly amongst businesses around the country.

11. Exemptions on business rates exist for properties such as places of worship, open public spaces like parks, properties used for the disabled, properties in enterprise zones, etc. Additionally, properties that are liable to pay business rates may benefit from business rates relief. For instance, small businesses with a rateable value of less than £12,000 have a relief of 100%, making them effectively exempt from business rates.

12. The rateable value is assessed by the Valuation Office Agency, generally every 5 years up until 2017. However, the Chancellor has announced an increase in the frequency of revaluations to every three years from 2021, which will ensure business rates assessments more closely reflect local market rental values.

13. To support businesses, the Government has introduced a range of reforms to the business rates tax regime in England, benefitting businesses to the value of £13bn over
the five years to 2023. We have doubled Small Business Rate Relief from 50% to 100% for eligible businesses and raised the threshold for the relief from £6,000 to £12,000. As a result, over 655,000 small businesses – occupiers of a third of all properties – pay no business rates at all. We have also switched the annual indexation of business rates from RPI to CPI. This means that business rates will increase less than they otherwise would have done, representing a cut in business rates, every year. Switching to CPI will help all ratepayers and save them over £6 billion over the next five years (2019/20 to 2023/24).

14. Recognising the pressures on retailers, the Government also announced as part of last year’s Budget that from April 2019, the business rates bills of retail properties with a rateable value below £51,000 would be cut by a third for the next two years. This is worth an estimated £1 billion and is providing upfront support for small and independent retailers, including shops, cafes and pubs.

15. Local authorities are compensated by central government for any reduction in their income which results from new business rates reliefs or changes that have been implemented since the introduction of the rates retention system in 2013. The Government is considering how best to account for these, and future changes, within potential reforms to the business rates retention system.

16. Prior to the introduction of the current 50% business rates retention system, business rates were collected at the local level, but receipts were pooled nationally and redistributed via the Formula Grant. This meant that local authorities had no financial incentive to promote business growth in their area, as they did not receive the receipts from such growth.

17. Since 2013/14, Government has allowed local government as a whole to retain 50% of locally collected business rates, and individual local authorities now retain a proportion of growth in business rates in their area. This move has given local authorities more control over the way they manage their locally raised taxes and an incentive to grow the amount of business rates they can raise from businesses in their area.

18. The current business rates retention system is yielding strong results. According to local authority estimates, in 2019/20 the sector will keep around £2.5 billion of additional funding in business rates growth.¹

Council tax

19. Local authorities decide the level of council tax to set each year, considering other income sources and the service needs of each area. Since 2012-13, the Government has maintained referendum thresholds. These are levels of council tax increases above which local authorities must hold a local referendum which allows residents to approve or veto the increase.

¹ This figure represents local authority estimates of business rates income in 2019-20. These figures take into account business rates pilots, Section 31 grants and levy and safety net calculations, as well as taking into account the previous year’s surplus / deficit.
20. Following the voluntary council tax freeze schemes which were in place between 2011-12 and 2015-16, a number of flexibilities have been offered to local authorities in recent years. For example, the introduction of the Adult Social Care Precept and a £5 flexibility for shire district councils from 2016-17 onwards. The latter has allowed shire district councils to increase their council tax by 2/3% or £5, whichever is greater, each year. This was of particular benefit to the lower-taxing shire districts. The Government also allowed the police further flexibility to increase their precept by £12 for 2018-19 and then by £24 for 2019-20, without triggering a referendum. To date no principles have been set for mayoral combined authorities or town and parish councils. However, this is kept under review and these sectors have been strongly encouraged to exercise restraint when setting increases.

21. In setting referendum thresholds, a balance is struck between ensuring local authorities have resources to provide local services and protecting council tax-payers from excessive bill increases. The Secretary of State consults on referendum principles as part of the annual Settlement process, and considers a range of factors, including the views of the sector, when deciding final thresholds. Referendum thresholds are not a cap — councils can set any council tax increase they like provided they obtain the consent of their local electorate in a referendum.

22. The average band D council tax for 2019-20 is £1,750, which is an increase of £78 or 4.7% on the 2018-19 figure of £1,671. This is less than the increase of £81 or 5.1% between 2017-18 and 2018-19.

23. The council tax system has evolved in response to pressures and concerns and continues to have a high collection rate, with an in-year collection rate of 97.1% in 2017-18. As well as offering flexibilities through bespoke referendum principles, the Government increased the range of local discretionary discounts for individual taxpayers from the 2013-14 financial year, allowing local authorities greater flexibility to respond to local circumstances. The Government is willing to consider the scope for further freedoms and flexibilities in the context of Spending Review discussions, while remaining mindful of the manifesto commitment to protect bill payers from high increases.

24. The Government has also taken action to double to 100% the maximum level of the council tax premium that councils can apply to homes that have been empty for at least two years, in order to further strengthen the incentive for owners of long-term empty properties to bring them back into productive use for the benefit of local communities. In response to concerns that some second-home owners may be exploiting the system under which holiday lets are valued for business rates, we have consulted on the criteria, and are considering all responses to determine whether this remains appropriate.

25. The Government recognises that different local authorities have differing abilities to generate council tax income, primarily due to variation in tax base, which is difficult for local authorities to influence. In response, we take account of the main resources available to councils when allocating central Government funding through the local government finance settlement. When the Adult Social Care Precept was introduced, the Government also took account of the fact that the ability of an area to raise funds is not correlated with their need for social care. As such the improved Better Care Fund was allocated in such a way that the overall distribution of the precept and iBCF grant reflected adult social care pressures across the country. The Government is currently
reviewing local authorities’ relative needs and resources and will take a fresh look at how council tax income is taken into account when redistributing business rates at local government finance settlements.

26. To ensure fairness in the system, council tax is also mitigated by a range of discounts and exemptions to reflect personal circumstances, such as the single person’s discount and student exemptions. In addition, since 2013, the Government has given local authorities new powers to design their own working-age council tax support schemes for low-income residents. Local authorities are best placed to make judgements about the appropriate level of support that should be made available. They know their areas and local communities best and can ensure that the design of their council tax support schemes reflects those local circumstances.

27. The Government also continues to guarantee pensioners the same level of council tax support as they would have done under the former council tax Benefit system. This means that the lowest-income pensioners are not required to make a contribution towards their council tax. Unringfenced funding for local council tax support is provided through the local government finance settlement.

The local government settlement

28. The annual local government finance settlement funds delivery of key local services across England. It distributes Revenue Support Grant and sets some of the parameters for locally retained business rates.

29. The 2016-17 settlement introduced a new methodology to allocate Revenue Support Grant (RSG).

30. This methodology takes account of the main resources available to councils including RSG, retained business rates and council tax – this is called ‘settlement core funding’ (SCF). This is a narrower measure of local government resources than Core Spending Power (CSP), excluding many of the income sources in CSP, such as Improved Better Care Fund and other adult social care grants. SCF is a notional measure designed to implement the reductions to Revenue Support Grant (RSG) since 2016-17, whereas Core Spending Power is meant to be a broad measure of local government funding. The council tax figures included in SCF are fixed at 2015-16 levels, whereas the council tax figures in CSP include growth in the tax base and increases in council tax levels.

31. The methodology ensures that councils delivering the same set of services receive the same percentage change in ‘settlement core funding’ for those services – e.g. every upper tier authority receives the same % change in the upper tier element of its funding.

32. As a result of this change, authorities with relatively more income from council tax and business rates receive larger reductions in their Revenue Support Grant than under the old methodology in order to ensure that all councils delivering the same services receive the same reduction in their overall Core Funding (as defined above).
33. Transition Grant was introduced in 2016-17 to help councils’ transition to the new methodology for allocating Revenue Support Grant (RSG).

Local Government Efficiency

34. In a context of devolution, the responsibility for efficiency will always rest with local authorities, nonetheless, the Government aims to incentivise and support local authorities to drive efficiency, self-improvement and wider public reform.

35. In 2016-17, the Government offered a four-year funding deal, which was accepted by 97% of authorities in return for publishing efficiency plans. This offer included Revenue Support Grant, business rates tariff and top-up payments and Rural Services Delivery Grant.

36. All councils who accepted the multi-year settlement published efficiency plans to show how greater funding certainty can help enable proactive planning of service delivery and strategic collaboration with local partners. Those councils have been able to plan ahead with confidence as they move from Whitehall dependency to being funded from locally-raised funds – something they have called for over decades. We received overwhelming positive feedback from local authorities to that change.

37. Councils have performed well in reforming the way they work to become more efficient, both in back-office functions and front-line service delivery. Councils account for a quarter of all public spending and need to continue playing their part in tackling the deficit, and the department is supporting them to do so.
Our work to support the Spending Review.

Business rates retention

38. The Government is aiming to introduce 75% BRR from 2020. The Government intends to do this by replacing exiting grants (Revenue Support Grant, Rural Services Delivery Grant, Public Health Grant and the GLA Transport Grant) with retained business rates. The value of these grants beyond 2019/20 will be subject to the 2019 Spending Review.

39. Alongside the aim to increase business rates retention the Government has been working with the sector on potential reforms to the business rates retention system. On 13 December 2018 we published a further consultation on business rates retention reform. The consultation was open for 10 weeks and closed on 21 February 2019.

40. The consultation built on our work with the sector to improve the way the local government finance system works. It sought views on the right balance of risk and reward, and options on reducing volatility in income for local authorities in the business rates retention system. It also sought views on a proposed reform of the administration of the business rates system and views on whether hereditaments are incorrectly listed on the central or local lists.

41. Notably, the consultation proposed a new approach towards business rates appeals and other valuation changes. We acknowledge that the impact of appeals in the current system has led to some volatility in local authority income through business rates. This is why we are continuing to engage with the sector on this and other questions to improve certain elements of the current system from 2020/21. We will consider very carefully all the interactions between the review of local authorities’ relative needs and resources, resets and the next Spending Review before taking any final decisions.

42. We are currently considering responses to the consultation and will confirm the reforms we will make to the retention system in due course. The Government will continue to work on delivering reforms to the BRR system through 2019.

The review of local authorities’ relative needs and resources

43. The current funding baselines, the amount of funding required, for local authorities in England, as determined by the annual local government finance settlement, are based on an assessment of their relative needs and resources. The methodology behind this assessment was introduced over a decade ago and has not been updated since the introduction of the 50% business rates retention system in 2013-14.

44. While this approach has ensured that councils which have grown the amount of business rates, they can raise from businesses in their area have benefited from the additional income generated. It also means that councils’ underlying levels of need have not been updated since the 2013-14 settlement. In addition, a desire to fully capture every aspect of local authorities’ needs has led to increasingly large numbers of variables being
included in the formulas, many of which had a relatively minimal impact on the overall
distribution of funding.

45. In order to address concerns that the current formula is unfair, out of date and overly
complex, the Government is carrying out a review of local authorities' relative needs and
resources (the ‘review’) to develop a more robust and up-to-date approach to distributing
funding across all councils. The review will enable the Government to reconsider the
drivers of local authorities' costs, the resources available to them to fund local services,
and how to account for these in a way that draws a more transparent and
understandable link between local circumstances and resource allocations.

46. The review will:
   a. set new baseline funding allocations for local authorities,
   b. deliver an up-to-date assessment of the relative needs of local authorities using
      the best available evidence,
   c. examine the relative resources of local authorities by taking a fresh look at how
council tax income should be taken into account when redistributing business
rates at local government finance settlements, and will also consider other
potential sources of income available to councils,
   d. focus initially on the services currently funded through the local government
finance settlement. If any further responsibilities are devolved under business
rate retention, this is be considered subsequently,
   e. consider appropriate transitional arrangements to ensure any changes in funding
are introduced in a manageable way, and
   f. be developed through close collaboration with local government to seek views on
the right approach.

47. As well as publishing a call for evidence and two technical consultations so far, the
Government has continued to work closely with local authorities and their
representatives on the review, including through a joint Local Government Association
and Ministry of Housing, Communities and Local Government-chaired steering group
and technical working group. In line with the review’s principle of transparency, records
of technical papers and discussions from the meetings are available on the Local
Government Association's website.

48. The most recent 10-week consultation, which closed on 21 February 2019, set out
proposals for the measurement of local authorities’ relative needs, options for a
resources adjustment and principles for potential transitional arrangements to the new
system. Over 300 consultation responses were received, all of which will be fully
considered in the next phase of this work.

49. The Government’s current aim is to implement the outcome of the review through the
2020-21 local government finance settlement. This will be kept under review as the
timing of the 2019 Spending Review becomes clearer.

Spending Review 2019

50. The Chancellor has announced he will launch a full three-year Spending Review before
the summer recess to be concluded alongside an Autumn Budget, if a deal with the EU
is agreed. Ahead of the Spending Review, we have been working with Departments
across Whitehall who have policy responsibility for many of the services councils deliver, as well as the sector, in order to build a robust evidence base and methodology for assessing and quantifying the financial need of local government.

51. We are actively implementing changes in the way we approach spending reviews, in response both to the NAO’s report on the financial sustainability of local authorities and the recommendations of the Public Accounts Committee in relation to the NAO report on capital spending in November 2016. This includes:
   a. considering the interactions between revenue spending, capital spending and borrowing and the resulting pressures on local authority capital programmes,
   b. reviewing unfunded pressures,
   c. developing our analytical capacity to look at the impacts of different funding decisions across different classes and locations of authority and statistical nearest neighbours, and
   d. working with DfE to improve our understanding of the drivers of costs and variation in spending on children’s social care.

52. The business rates retention system is a mechanism of local government funding with an emphasis on incentivising local authorities to increase the amount of business rates they can raise from businesses in their area, but it does not define the amount of money circulating within the system. This is the remit of the Spending Review.

*The adult social care green paper*

53. The Government has committed to publishing a Green Paper at the earliest opportunity setting out its proposals for reform to ensure the social care system is sustainable in the longer term.

54. Building a sustainable care and support system will require some big decisions. But getting this right promises a better system that everyone can have confidence in, where people understand their responsibilities, can prepare for the future, and know that the care they receive will be to a high standard and help them maintain their independence and well-being.

55. Government has already invested funding to put social care on a more stable footing and alleviate short-term pressures across the health and care system. However, further reform is required to ensure that the system is prepared to meet the challenges of an ageing society.

56. It is right that social care funding is agreed alongside along the rest of the local government settlement at the forthcoming Spending Review.

*Future Efficiency Plans*

57. The department has developed a package of measures to help councils become more efficient, more effective and ultimately more resilient. This package of support includes several elements:
a. This year (2018/19) we have given £20 million in grant to the Improvement and Development Agency (part of the LGA) to provide improvement support to local government.

b. Carrying out analysis to give us a proper understanding of efficiency in the sector, and then engaging with individual councils. This engagement seeks to understand how much has been saved in adults’ and children’s social care, and possible scope for future savings. We have been working with other government departments – DHSC, DfE, and HMT – to help us to unlock future efficiencies.

c. Working with the sector to take more advantage of cutting-edge digital technologies. The arrival of the internet has transformed the world around us. Public services have already made great progress in using technology to reduce cost and deliver better services – but we know there is more to do if services are to be as flexible, easy to use and user-focussed as they can be. In September 2018 we invited bids for the £7.5m Local Digital Innovation Fund, which will support dozens of councils make more effective use of digital technologies. In December the first 16 winners bids into the £7.5m Digital Innovation Fund were announced.

d. Developing, in partnership with the LGA and iESE, a self-assessment tool which will be used by councils to plot their efficiency journey. This continuous improvement tool will enable councils to understand where they are on this journey, where they want to be, and what steps they need to take to reach full their full efficiency potential. The tool is currently being tested and will be soft-launched in Spring 2019.

58. This important package of measures will support councils to continue the work they have done to manage their budgets and deliver high quality services.

Conclusion

59. Providing councils with the freedom to use funds in a way that responds to local needs and priorities and avoiding the ringfencing of specific funds, is key to ensuring financial sustainability and sound financial management on the part of authorities themselves.

60. We will continue to work with the sector on how best to implement the business rates retention reforms in 2020/21, and we will work with the sector to identify other opportunities to further increase business rates retention when it is right to do so. However, we cannot ignore the current pressures on the legislative programme, and this will inevitably have an impact on timing for any primary legislation.

61. Government will publish the Social Care Green Paper at the earliest opportunity, setting out its proposals for reform.

62. The Government aiming to implement, through the Spending Review, a review of local authorities' relative needs and resources which will develop a more robust and up-to-date approach to distributing funding across all councils. The review will enable the Government to reconsider the drivers of local authorities' costs and the resources available to them to fund local services.