Havering
LONDON BOROUGH

CABINET 26 SEPTEMBER 2012	REPORT

Subject Heading:	The Council's Financial Strategy
Cabinet Member:	Cllr Roger Ramsey
CMT Lead:	Andrew Blake-Herbert Group Director Finance & Commerce
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Policy context:	The Council is required to approve an annual budget and this report provides information to enable Cabinet to make recommendations to Council in February 2013
Financial summary:	There are no specific financial issues, this report deals with developments relating to the localisation of business rates
Is this a Key Decision?	No
Is this a Strategic Decision?	No
When should this matter be reviewed?	December 2012
Reviewing OSC:	Value

The subject matter of this report deals with the following Council Objectives

Ensuring a clean, safe and green borough	[X]
Championing education and learning for all	[X]
Providing economic, social and cultural activity in thriving towns and villages	[X]
Valuing and enhancing the lives of our residents	[X]
Delivering high customer satisfaction and a stable council tax	[X]

SUMMARY

Over the course of the previous two years, Havering Council has agreed a package of savings to mitigate the impact of very significant cuts in central government funding to local authorities.

These savings, totalling in excess of £19 million in the first tranche, with a further £16 plus in the second tranche, were made up of a range of measures designed to reduce back-office costs, cut bureaucracy and focus resources where they would have the most impact – while remaining fair to those local residents who most rely on the Council for their day-to-day support.

Government plans for radical changes to a number of areas were announced over this period. More detail is gradually emerging. These changes will fundamentally alter the way in which local authorities are funded. This report updates Cabinet on developments relating to the localisation of business rates.

A further report will be submitted to Cabinet in due course, dealing with a number of other developments and setting out the position in the current financial year, and a number of other relevant issues, as these need to be taken into account in developing the detailed budget for 2013/14.

RECOMMENDATIONS

Cabinet is asked to:

1. Note the current position with developments relating to the funding of local authorities through the localisation of business rates.

2. Note that details of the Local Government Financial Settlement for 2013/14 will be reported to Cabinet in full in January.

3. To delegate to the Cabinet Member for Value approval of the Council's response to the technical consultation on the localisation of business rates.

4. To note that a further report will be submitted to Cabinet on a range of other financial matters.

REPORT DETAIL

1. BACKGROUND

1.1 In the light of the global financial climate and the decisions taken by the Coalition Government on public sector spending, the broad financial position and prospects for the future have been set out in previous reports to Cabinet. In very broad terms, the anticipated funding reductions were expected to lead to an overall budget gap of around £40m over a 4 year period. In response to this, Cabinet agreed two tranches of savings, totalling around £36m, and these were subsequently included in the budget formally approved by Council.

1.2 The proposals agreed by Cabinet would largely meet the Authority's savings requirements without excessive Council Tax increases and not raising Council Tax above 2.5% throughout the life of this Administration. It would ensure a stabilised financial position with clear plans in place to meet the overall budget gap and bring as much certainty as possible to residents over both Council Tax levels – given the Administration's commitment to low increases – and the level of service they can expect.

1.3 The Coalition Government had already previously announced proposals for fundamental changes to the funding system for local authorities, as well as a number of other proposals that will impact directly on the Council. The most immediate and critical of these relating to the localisation of business rates is covered as part of this report as this will affect the budget setting process for 2013/14.

2. FUNDING CHANGES

2.1 The Government had previously announced a variety of changes that will impact, either directly or indirectly, on the funding regime for local authorities. These have, to a greater or lesser extent, been reported to Cabinet previously, but progress towards the implementation of these changes is accelerating rapidly. An update on each of the following areas will presented to Cabinet in due course, but the most immediate of these is addressed below:

- Localisation of business rates
- Localisation of Council Tax support
- The Social Fund Replacement Scheme
- School Funding Reform
- Academies
- Public Health Transfer
- Local Government Pension Scheme.

Localisation of Business Rates

2.2 The Government announced plans to fundamentally change the basis on which local authorities were funded some time ago. Under the current funding system, local authorities had historically been funded through a combination of specific and general grants. Specific grants were for a designated purpose and authorities were expected, and indeed in some cases only allowed, to spend these funds on explicit functions.

2.3 In the wake of the general economic climate, the Coalition Government is reducing the amount of funding available to the public sector. For local authorities, this has been reflected in an ongoing reduction in grant funding. There have also been major changes to specific grant funding, with both a reduction in number and value, but a shift towards grants being unringfenced, and thus more general in nature.

2.4 The next stage of this process will be the cessation of the existing funding system, and the core element of the new system will be the localisation of business rates. This new system is being implemented in April 2013, and will thus impact on the next budget setting process. Reports setting out information on this new system have previously been submitted to Cabinet, but more detail is emerging. This report updates Cabinet on the most recent developments.

2.5 In broad terms, the current system will cease. In its place, local authorities will retain funds generated locally through business rates. This will see a shift from the present system, where local authorities effectively collect business rates on behalf of the Government, and receive general grant funding, to one where they will now retain those business rates locally.

2.6 However, the proposals announced by the Government will not see full retention. Instead, it is proposed that authorities will retain only 50% of the sum collected, with the remaining 50% being returned to the Government. In return, local authorities will receive a general grant. There will also be limits on how much authorities can "gain" or "loose" through local shifts in the level of business rates, so for example, a material reduction in local business rates would be compensated for.

2.7 The Government recently published a Technical Consultation on Business Rates Reform. This sets out a range of proposals on how the new system would operate. The consultation paper contains 83 questions; responses are required by 24 September 2012.

2.8 Details of the key highlights of the scheme are set out in Appendix A, and in summary are as follows:

- A "50/50" share, with local authorities retaining 50% of business rates
- New RSG system to fund the 50% which will be returned to Government
- A system of tariffs and top ups
- Changes in the treatment of existing grants
- Impact on tax base.

2.9 Details of funding, including the base amount for business rates and the level of general grant, will be set out in the Local Government Financial Settlement (LGFS). It is clear that the previous system of funding announcements through the LGFS will continue inspite of the shift to a new funding system. Whilst there are more uncertainties over the transition this year, this does mean that, unless the Government chooses to issue multiple years, the exact funding position will not be known until the settlement is released. For 2013/14 in particular, this is not expected until December. This will mean a significant amount of work will need to be undertaken at that time and it will not be possible to provide details to Cabinet until January, when budget proposals are formally submitted for consultation purposes.

2.10 Officers are working through the technical consultation document, which runs to over 250 pages, and will be drafting a response in time for the close of the consultation process. To maximise the time available, the response will need to be finalised after the Cabinet meeting. It is therefore proposed that approval of the response is delegated to the Cabinet Member for Value, and Cabinet is asked to agree this.

2.11 Although there is a distinct lack of clarity over what impact the new funding system will have, there does seem to be a clear incentive for authorities to maximise the yield from their business base. With that in mind, officers are considering what steps might be appropriate, and what resources might be needed to do so. This will be the subject of a separate report to Cabinet.

2.12 Given that the new funding system will include some form of relative needs and resources, grant transfers and adjustments, floor damping, and a system of tariffs and top-ups, there is an argument that this replicates most if not all of the key elements of the existing system. That, in turn, heightens the risk that the new system may be no more transparent than the current one.

2.13 Finally, it is important to bear in mind that, although local authorities will retain a proportion of business rates, control of the system remains firmly with central Government. The business rates multiplier, which generates the actual sum due from the rateable value (RV), will still be set by Government; there is no ability for Councils to vary this. Moreover, RVs themselves are driven by various factors, and again in broad terms are not actually set by local authorities. This, plus the continued reliance on a formula-based grant allocation, means in reality that local authorities will remain heavily dependent on how central Government approaches the commercial taxation and public sector finance systems.

2.14 This emphasises the level of risk that exists with the transition to the new funding system, and that necessitates that a prudent approach is maintained.

3. BUDGET TIMETABLE

3.1 Although, as this report sets out above, there is a significant level of change being made to the funding system, and various uncertainties affecting the Council's financial position, it is essential that work continues in planning for the budget setting process for 2013/14.

3.2 A broad timetable has been developed and is set out in the table below.

Activity	Date
Update on other financial matters	October 2012
Announcement of LGFS	Nov/Dec 2012
Budget proposals for consultation to Cabinet Details of LGFS to Cabinet	23 Jan 2013
Budget proposals to Cabinet	13 Feb 2013
Formal budget setting proposals to Council	27 Feb 2013

3.3 Further reports will be submitted to Cabinet as more information becomes available on the various issues covered in this report. It is proposed to provide an update to Cabinet at the next meeting on a range of other financial matters and an assessment of the financial position and its potential impact on 2013/14.

REASONS AND OPTIONS

Reasons for the decision:
It is essential that the Council's financial strategy takes due account of Government plans, and any other material factors where these are likely to have an impact on the Council's financial position. This report provides an update to Cabinet on the most immediate issue relevant to the budget setting process.

Other options considered:
None. The Constitution requires this as a step towards setting the Council's budget.

IMPLICATIONS AND RISKS

Financial implications and risks:
The Council's budget process will ensure that financial implications and risks are fully met. There are continuing risks given the uncertainty over the transition to localised business rates, and to the associated announcement of the LGFS, and the potential impact on funding, together with the other aspects referred to in this report. The steps already taken by the Council should mitigate this, but to what extent remains unclear. It will therefore be necessary to assess the position once the funding levels are finally known.

There are considerable risks in the medium to longer term, with the continuing economic uncertainty as well as the imminent changes. The Council therefore needs to maintain a prudent approach over its financial management and the budget setting process.

Legal implications and risks:
The Council is subject to a number of duties in relation to revenue, capital and procurement. For instance, as a Best Value Authority the Council is under a duty to "make arrangements to secure continuous improvement in the way in which its functions are exercised, having regard to a combination of economy, efficiency and effectiveness." s 3 Local Government Finance act 1999.

Human Resources implications and risks:
The Council continues to work closely with its staff and with Trades Unions to ensure that the effects on staff of the savings required have been managed in an efficient and compassionate manner.

All savings proposals or changes to the funding regime that impact on staff numbers, will be managed in accordance with both statutory requirements and the Council's Managing Organisational Change & Redundancy policy and associated guidance

Equalities implications and risks:
There are no equalities implications or risks at this stage. However any savings that need to be considered following publication of details of the Local Government Financial Settlement may carry equalities implications and risks and accordingly, these will need to be analysed.

Other Risks:
There are no particular other risks arising, other than a significant increase in workload is likely to implement the new legislation as and when it is enacted. This is being planned for but much of the detail will have to await the final announcements and publication.

BACKGROUND PAPERS

There are none.

APPENDIX A

FORMULA GRANT & LOCALISATION OF BUSINESS RATES

Introduction

The Department for Communities and Local Government (CLG) issued the business rate consultation on the 17th July 2012. This briefing note highlights the key developments of the proposals to date.

The consultation is due to run for ten weeks and closes on the 24th of September 2012 with the view to provide local authorities with a draft model and provisional figures in late November / early December.

Business Rate Consultation

The Department of Communities and Local Government released the Business Rate Retention Technical Consultation. This provides further details of how the new funding regime will be implemented however the final design and funding allocation will not known until mid / late January. The new funding regime will operate in-line with the spending control totals which still currently has two more years of budget cuts to be built into the model.

Previously in May, The Department of Communities and Local Government released the publication “Business rates retention scheme: The central and local shares of business rates” stating that Local authorities would retain 50% of their business rate yield (Local Share) and 50% will be transferred to Government (Central Share). Of the Local Share, it is now understood that from the latest consultation document that a “significant amount” will be transferred to fund the GLA. This reduces the amount of business rate yield that local authorities are able to retain however this proposal will share the risks / rewards of any decline / growth in business rates between Central / Local Government and precepting authorities.

The central share will be paid to Government with the view to redistribute this funding to Local Authorities and Fire Services through grants (approximately £11bn). This will not only fund local authorities Revenue Support Grant allocations but also help fund the New Home Bonus, the GLA, Capitalisation and the Safety Net used in the event that an authority’s business rates baseline falls below a set percentage set by Central Government (between 7.5% and 10%)

To enable the local share to be set at 50%, Central Government have rolled in approximately £8bn of grants into the retention model. These grants will be rolled in after floor damping resulting in like-for-like transfer of funding. For Havering, this amounts to approximately £31m to be rolled into the retention model. The grants which are to be rolled in are as followed:

- Early Intervention Grant
- Learning Disability and Public Health
- Council Tax Freeze Grant

- Council Tax Support
- Homelessness Prevention
- Lead Local Flood Authorities

In addition to the rolled in grants, £3bn and £1.2bn will be transferred out to fund the police authorities and Local Authority Central Spend Equivalent Grant (LACSEG) respectively.

It is also expected that minor adjustments to the indicators used in establishing the current formula grant will transfer further funding out of London to District authorities. This will reduce Havering's funding starting position for 13/14 onwards.

There are huge variations between the amount of business rates local authorities collect and the formula grant they receive. In 2012/13 Havering will contribute £67.6m to the national pool of which will only receive back £51.3m from the Local government Finance Settlement. Under the new funding regime, to ensure local authorities are not subject to large variation in funding, local authorities will either be required to pay a tariff (up rated by RPI each year) or receive a top-up (up rated by RPI each year) to ensure stability from the new system against their previous years formula grant allocation. At this stage until further details are provided in regards to the impact of the GLA contribution it's difficult to ascertain whether Havering will be a Top-up or Tariff authority.

The final scheme design will be announced in Late November / early December, however it is understood at this moment in time that the Government will set a business rate baseline for each authority based on a five year average in business rate yield. This baseline will identify whether authorities are a top-up or tariff authority, as well as identify whether any authority has a shortfall against their expected 13/14 yield. In the event that the anticipated income is less than the business rate baseline then authorities would need to budget for this outcome and potentially having to factor in any safety net payment into their budget.

Table A below shows the estimated allocations for 13/14 based on the information provided to date.

Local Authority	Amount of Formula grant 12/13 exc council tax freeze grant	Estimated Rolled in grants	Total	Anticpated 13/14 funding including the SR spending reductions
	(£ Millions)	(£ Millions)	(£ Millions)	(£ Millions)
Havering	51.363	31.10	82.46	77.35
Barking and Dagenham	99.028	30.40	129.43	119.54
Bexley	60.524	26.70	87.22	81.12
Bromley	59.636	34.60	94.24	88.31
Newham	202.749	47.30	250.05	229.74
Redbridge	93.660	30.40	124.06	114.72
Outer London Average	94.131	36.78	130.91	120.76
Inner London Average exc City of London	169.688	37.46	207.15	188.39

As can be seen above, the amount of formula grant Havering has received in previous years has been significantly lower compared neighbouring authorities and the London average. The indicators used in apportioning the formula do not reflect the demographics of the borough. In contrast, the amount of grant Havering received through unringfenced and specific grants which are to be transferred into the retention scheme has been more reflective of the demographics as the data used to allocate funding is based on actual caseload, population etc. This is evident by the amount of rolled in grant Havering has received compared to other authorities. The transfer of these grants in the long-term will be detrimental as these allocations will be subject to spending cuts and formula grant changes.