Local Government Resource Review: Proposals for Business Rates Retention

Technical paper 1: Establishing the baseline

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August 2011
Department for Communities and Local Government

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Chapter 1

Introduction

1.1. On 18 July, the Department for Communities and Local Government (DCLG), published a consultation paper, *Local Government Resource Review: Proposals for Business Rates Retention*.

1.2. This set out proposals for a rates retention scheme to replace the current local government finance system, under which business rates are distributed as part of formula grant.

1.3. The consultation paper outlined the principal features of the proposed rates retention scheme. It undertook to provide further detail in a series of technical papers, to be published in August.

1.4. Taken together, the consultation paper and technical papers raise a number of questions about the proposed rates retention scheme, on which the Government is seeking views. The **consultation will close on Monday 24 October 2011**. Details of how to respond can be found on page 7 of the main consultation paper[1].

1.5. This is one eight technical papers. The full list is:

Paper 1: Establishing the Baseline
Paper 2: Measuring Business Rates
Paper 3: Non-billing Authorities
Paper 4: Business Rates Administration
Paper 5: Tariff, Top Up and Levy Options
Paper 6: Volatility
Paper 7: Revaluation and Transition
Paper 8: Renewable Energy

1.6. All technical terms in the papers appear in italics and are explained in the Glossary of technical terms, which is attached to each technical paper as an annex.

1.7. An outline of the eight papers can be found in *Business Rates Retention – Technical Papers: An Overview*.

[1] www.communities.gov.uk/publications/localgovernment/resourcereviewbusinessrates

Chapter 2

About this paper

2.1. As set out in the main consultation paper, *Local Government Resource Review: Proposals for Business Rates Retention*, the Government intends to establish a fair starting point, so that no authority loses out as a result of its business rates base at the outset of the scheme.

2.2. It proposes to achieve this through a rebalancing of resources in the first year of the scheme (which we intend to implement from 2013-14). This would involve establishing a *baseline funding* level for each authority, against which to compare its *individual authority business rates baseline*. Those authorities with *individual authority business rates baselines* in excess of their *baseline funding* level would pay a *tariff* to central government, and those whose *individual authority business rates baseline* was below their *baseline funding* level would receive a *top up* from central government.

2.3. Tariffs and top ups would be self-funding and would be fixed in future years (see *Technical Paper 5: Tariff, Top Up and Levy Options*). Individual authorities' *baseline funding* levels would not be re-assessed, until any reset of the scheme to realign resources with changing service pressures. This means that authorities whose business rates grew would retain a significant proportion of that growth in revenue (subject to the operation of the *levy*), while those whose rates declined or grew at a lower rate would experience lower or negative growth in revenue (subject to the operation of the *safety net*), providing a strong incentive to promote business growth.

2.4. This paper discusses the detailed issues and options for establishing individual authorities' *baseline funding* levels, against which to compare their *individual authority business rates baseline* and so calculate tariffs and top ups.

Setting aside a share of forecast national business rates

2.5. As explained in the main consultation paper, to deliver a fiscally sustainable system and avoid putting the Government's deficit reduction programme at risk, we will ensure that the business rates retention scheme operates within the expenditure control totals for 2013-14 and 2014-15, set out in the Spending Review 2010.

2.6. Chapter 3 discusses proposals for dealing with the expectation that the *forecast national business rates* will exceed those expenditure control totals. It explains how we propose to calculate the share of the *forecast national business rates* to be set aside to fund other grants to local government (the *set aside*).

Adjusting to establish the national business rates baseline

2.7. Chapter 4 discusses the need for a number of further adjustments to the *forecast national business rates*, to fund:

- the New Homes Bonus which, as set out in the main consultation paper, the Government is committed to continuing to fund within a business rates retention scheme

- police authorities, and potentially also single purpose fire and rescue authorities, which, as set out in the main consultation paper, the Government proposes to provide with guaranteed levels of funding that are unaffected by fluctuations in business rates in 2013-14 and 2014-15*.* This is discussed further in *Technical Paper 3: Non-billing Authorities*

- any changes in local authority functions and responsibilities which have been agreed for the first year of the system (2013-14)

2.8. It considers and invites views on the detailed issues and options for making such adjustments. The share of the *forecast national business rates* remaining, after the *set aside* and *adjustments*, will form the *national business rates baseline* for the purposes of the scheme.

Establishing individual authorities' baseline funding levels

2.9. The *national business rates baseline* represents the overall quantum available for distribution between individual authorities to establish their *baseline funding* levels, against which tariffs and top ups will be set.

2.10. The main consultation paper set out the Government's proposal, for reasons of budget stability, to use 2012-13 formula grant as the basis for establishing individual authorities' *baseline funding* levels. Chapter 5 provides detailed discussion of the two options for using 2012-13 formula grant outlined in the main consultation. This discussion will be of interest to all authorities, including police authorities and single purpose fire and rescue authorities, since their guaranteed levels of funding would be calculated and fixed as part of the process for establishing other authorities' individual *baseline funding* levels.

2.11. Chapter 5 also explains how, under either option, the Government's commitment to manage the scheme within the spending control totals for 2013-14 and 2014-15 means that *baseline funding* levels must be based on the lower (2014-15) spending figures. It discusses proposals to ensure that no authority loses out in 2013-14 as a result of this approach by returning the difference between the two control totals to local authorities as a separate grant.

Fixing individual authorities' baseline funding levels between resets

2.12. Once individual authorities' *baseline funding* levels have been established and used to calculate tariff or top up amounts, they would remain fixed and would not be reviewed until any reset. As a result, authorities would stand to benefit from growth in their business rates, while those whose rates declined or grew at a lower rate would experience lower or negative growth. This provides a strong incentive for local authorities to promote business growth in their area.

2.13. Chapter 6 considers the implications of fixing *baseline funding* levels between resets, including options for dealing with any mergers or boundary changes, changes in local authority functions and new burdens that arise between resets. It also discusses proposals for the future of Revenue Support Grant, for retaining a local government finance report and for funding specified bodies.

Resetting the system

2.14. The proposals set out in the main consultation paper include the option for government to reset the system if it was felt that resources no longer sufficiently met service pressures within individual local authority areas (for example, because of population movements, or the characteristics of the area changing).

2.15. A reset would involve re-assessing individual authorities' *baseline funding* levels, potentially on the basis of a completely new assessment of need rather than formula grant, and recalculating tariff and top ups accordingly. Chapter 7 discusses and seeks views on the options for resetting the system.

Chapter 3

Setting aside a share of forecast national business rates

3.1. The 2010 Spending Review set spending control totals for local government over the four year period from 2011-12 to 2014-15. The Spending Review table setting these out is reproduced below.

Table 2.7: Local Government

	£ billion				
	2010-11	2011-12	2012-13	2013-14	2014-15
Resource DEL[12]	28.5	26.1	24.4	24.2	22.9
Capital DEL	0.0	0.0	0.0	0.0	0.0
Total DEL	**28.5**	**26.1**	**24.4**	**24.2**	**22.9**
Departmental AME	**0.5**	**0.5**	**0.5**	**0.5**	**0.5**

1 In this table, Resource DEL excludes depreciation and AME excludes non cash items
2 LG DEL includes funding for police and fire authorities. Excluding these contributions LG DEL for councils will fall by 28 per cent

Source: Spending Review 2010

3.2. To deliver a fiscally sustainable system and avoid putting at risk its deficit reduction programme, the Government proposes to ensure that the business rates retention scheme operates within these expenditure control totals for 2013-14 and 2014-15.

3.3. As set out in the main consultation document, we expect that business rates collected in England in 2013-14 and 2014-15 will be greater than these expenditure control totals. We will therefore need to set aside a share of the *forecast national business rates* to fund other grants to local government (the *set aside*).

Calculating the set aside

3.4. As authorities' *baseline funding* levels will not be reviewed until any reset, and tariffs and top ups will be fixed, it would not be possible to alter the *set aside* once the business rates retention scheme were introduced. It is therefore necessary to base the calculation of the *set aside* on the lowest expenditure control total. We propose comparing the 2014-15 expenditure control total with the *forecast national business rates* we expect will be collected in 2014-15. The difference between the two would be the *set aside* amount.

3.5. In 2013-14, when spending figures are higher, the Government proposes to distribute the difference in such a way as to ensure that no authority loses out as a result of this approach. This is discussed in further detail at paragraphs 5.7-5.10 below.

3.6. Whilst the expenditure control totals were published in the Spending Review 2010, the *forecast of national business rates* for 2014-15 will only be made in the autumn of 2012, so it is not possible, at this stage, to say what the *set aside* amount would be. (T*echnical Paper 2: Measuring Business Rates* provides further details about how we propose to calculate the *forecast national business rates*, and about how we propose the *set aside* amount would be apportioned between each billing authority on the basis of *proportionate shares*.)

3.7. As set out in the main consultation paper, the Government proposes to consider, at the next Spending Review, the total spending figures for local government with a view to more closely aligning local authority functions and responsibilities with business rates income from 2015-16.

3.8. Chapter 6 considers the implications of fixing individual authorities' *baseline funding* levels until any reset, including options for dealing with any changes in local authority functions between resets.

TP1 Q1: Do you agree with the proposed approach to calculating the amount of business rates to be set aside to fund other grants to local government? If not, what alternative do you suggest and why?

Chapter 4

Adjusting to establish the national business rates baseline

4.1. After the *set aside* has been deducted from the *forecast national business rates* to ensure that the business rates retention scheme operates within the spending control totals, we propose to make a number of further adjustments to fund:

- the New Homes Bonus - in line with the commitment made by the Government, in the main consultation paper, to continue funding the New Homes Bonus within the business rates retention scheme
- police authorities, and potentially also single purpose fire and rescue authorities – in line with the Government's proposal to provide guaranteed levels of funding that are unaffected by fluctuations in business rates for these authorities in 2013-14 and 2014-15 (as discussed in *Technical Paper 3: Non-billing Authorities*)
- any changes in local authorities' functions and responsibilities which have been agreed for the first year of the system (2013-14)

4.2. The amount of *forecast national business rates* remaining after the *set aside* and the above *adjustments* will form the *national business rates baseline* for the purposes of the scheme.

The New Homes Bonus adjustment

4.3. The New Homes Bonus creates a powerful incentive for local authorities to increase housing supply. The main consultation paper set out the Government's commitment to continue funding the New Homes Bonus within the business rates retention scheme. This will ensure a balance of incentives for both business and housing growth.

4.4. We propose to deliver this commitment by making an adjustment to remove a sufficient amount from the *forecast national business rates* to fund the New Homes Bonus.

4.5. New Homes Bonus payments are awarded for six years. As the *baseline funding* levels will not be reviewed until any reset, and given that tariffs and top ups will be fixed, it will not be possible to change the New Homes Bonus adjustment between resets. As explained in the main consultation paper, it will therefore be necessary to remove an amount sufficient to fund the future 'steady state' cost of the New Homes Bonus. So, in the early years of the business rates retention scheme, this adjustment will remove significantly more money than is actually required. We would return any surplus New Homes Bonus funding to local authorities in full each year.

4.6. We will discuss estimates of the adjustment needed to fund the New Homes Bonus with partners, including the Settlement Working Group.

4.7. In the absence of the New Homes Bonus adjustment, this money would otherwise have been distributed to local authorities as part of the process for establishing individual authorities' *baseline funding* levels. The Government therefore proposes to make an annual forecast of the surplus New Homes Bonus funding and return it to local authorities in proportion to their *baseline funding* levels. Whilst this would not exactly replicate the distribution that would have resulted had the money formed part of the overall amount available when setting baseline levels of funding, it provides the closest practical equivalent[2].

4.8. The money could either be paid as a Section 31 grant or, potentially, as Revenue Support Grant (see the section in chapter 6 on the Future of Revenue Support Grant)

4.9. We propose to announce New Homes Bonus payments alongside the draft Local Government Finance Report. This should mean that we have final New Homes Bonus allocations and totals in time for the final Local Government Finance Report. This will help local authorities budget for the following financial year.

TP1 Q2: Do you agree with the proposed approach for making an adjustment to fund New Homes Bonus payments, and for returning any surplus to local authorities in proportion to their *baseline funding* levels?

Adjusting for any changes in local authority functions

4.10. In establishing the *national business rates baseline*, it may be necessary to make an adjustment to take account of any changes in local authority functions and responsibilities agreed in advance of 2013-14.

4.11. In the case of a function being transferred <u>from</u> local authorities at the start of the first year of the business rates retention scheme, we propose to adopt a similar approach to that described above for the New Homes Bonus adjustment. This would involve calculating and removing a sufficient amount to fund the maximum cost of the function or responsibility being transferred; and returning any surplus funding to local authorities in proportion to their *baseline funding* levels via either

[2] This is because the overall amount available for distribution when setting baseline levels of funding affects the year-on-year change in funding, which in turn affects floor damping decisions; and also affects the shares of taxbase, leading to a different distribution between authorities in each floor damping group.

a section 31 grant or, potentially, Revenue Support Grant (see the section in chapter 6 on the "*Future of Revenue Support Grant*").

4.12. In the case of a function or responsibility being transferred to local authorities at the start of the first year of the business rates retention scheme, we propose that the *set aside* should be reduced by a sufficient amount to fund the costs involved, meaning a larger *national business rates baseline* would be available for distribution as part of the process for establishing individual authorities' *baseline funding* levels.

4.13. As *baseline funding* levels would not be reviewed until any reset, and tariff and top ups would be fixed, the scope to transfer functions from local authorities between resets would be very limited.

4.14. In the case of a function or responsibility being transferred to local authorities between resets, we propose to adopt a similar methodology to that described for funding new burdens between resets at chapter 7.

TP1 Q3: Do you agree with the proposed approach for making an adjustment in the event of any functions being transferred to or from local authorities?

The police and fire adjustments

4.15. *Technical Paper 3: Non-billing Authorities* sets out the Government's proposal that police authorities, and potentially also single purpose fire and rescue authorities, should receive guaranteed levels of funding for the remaining two years of the Spending Review 2010, rather than sharing in business rates growth or decline.

4.16. As a consequence, in establishing the *national business rates baseline* it would be necessary to make a further adjustment to fund police authorities ("the police adjustment"), and potentially also single purpose fire and rescue authorities ("the fire adjustment"), in 2013-14 and 2014-15.

4.17. The police adjustment would be an amount equivalent to the total of the police funding levels included in the 2010 Spending Review. Similarly, if required, the fire adjustment would be an amount equivalent to the total funding for single purpose fire and rescue authorities included in the 2010 Spending Review.

4.18. Chapter 5 discusses how these amounts would be distributed between individual police authorities and single purpose fire and rescue authorities in such a way as to ensure that no authority is worse off than they would have been under the current system.

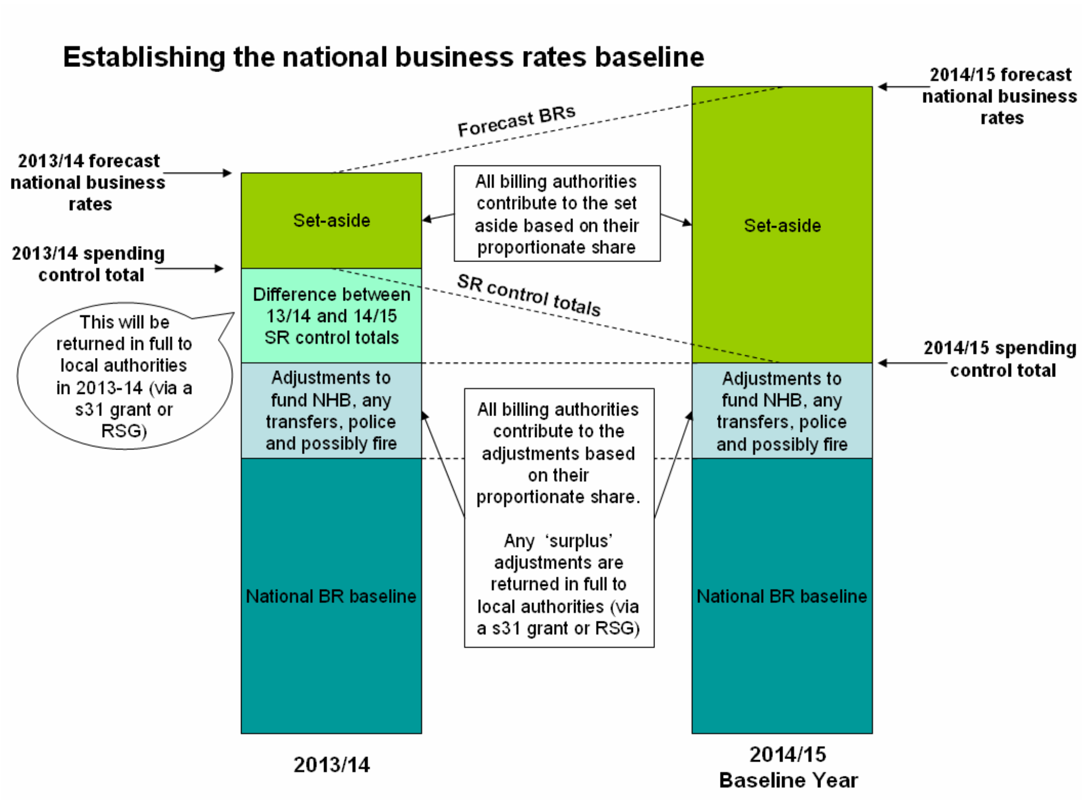
4.19. As explained in the main consultation paper, the way in which the police and fire sectors are funded beyond 2014-15 will be fully reviewed in time for changes to be made from the next Spending Review period, from 2015-16. This review will consider the potential for all government funding for the police to come from the Home Office. The Government will, in parallel, consider more closely aligning local authority functions and responsibilities with business rates income.

TP1 Q4: Do you agree with the proposed approach for making an adjustment to fund police authorities, and potentially also single purpose fire and rescue authorities?

Chapter 5

Establishing individual authorities' baseline funding levels

5.1. After the *set aside*, discussed in chapter 3 and the *adjustments*, discussed in chapter 4 have been deducted, the remaining *forecast national business rates* will form the *national business rates baseline*. This is illustrated below:



5.2. As set out in the main consultation paper, in considering how to establish individual authorities' *baseline funding* levels, we have taken as a priority the need to maintain local budget stability and to give local authorities the opportunity to benefit from the growth incentive provided by the business rates retention scheme at the earliest opportunity. We consider that the best and most pragmatic way to achieve this is to start from local authorities current formula grant position, rather than introduce major change and turbulence into the system, which would result in a long period of transition and potentially weaken the incentive effect.

5.3. The main consultation document outlined two options, which this chapter discusses in more detail:

- Option one: adjust actual 2012-13 formula grant allocations in proportion to the sum of the *national business rates baseline*, the police adjustment and any fire adjustment.

- Option two: apply the 2012-13 formula grant process to the sum of the *national business rates baseline*, the police adjustment and any fire adjustment, and at the same time make technical updates to the formulae.

5.4. The main consultation paper asks consultees what they think the Government should consider in setting *baseline funding* levels; whether they agree with the proposal to use 2012-13 formula grant; and, if so, which of these two options would be preferable and why.

5.5. This chapter discusses each of the two options in further detail, to help inform responses to the questions posed in the main consultation and to seek views on further questions regarding the choices that would need to be made about the detail of our approach under each option.

5.6. It also seeks views on our approach to two issues that arise regardless of which option is selected:

- how to ensure that no authority loses out in 2013-14 as a result of managing the scheme within 2014-15 spending control totals; and

- whether to use 2012-13 formula grant levels before or after floor damping (and, if after, which year to take as the base position)

Ensuring that no authority loses out in 2013-14 as a result of managing the system within 2014-15 spending control totals

5.7. Under either of the two options for establishing individual authorities' *baseline funding* levels, which are considered in detail below, the Government's commitment to manage the business rates retention scheme within the spending control totals for 2013-14 and 2014-15 means that *baseline funding* levels will be based on the lower (2014-15) spending figures.

5.8. We would return the difference between 2013-14 and 2014-15 expenditure control totals to local authorities in full in 2013-14, to ensure that no authority loses out in 2013-14 as a result of using the lower 2014-15 expenditure control totals.

5.9. To that end, we propose to make two different calculations. One would be based on the 2014-15 expenditure control totals, and would establish individual authorities' *baseline funding* levels for the purposes of the business rates retention scheme. The other would be based on the 2013-14 expenditure control totals, and would establish a 2013-14 funding equivalent for each authority. Each authority would receive a "2013-14 adjustment", which would be the difference between its *baseline funding* level and its 2013-14 formula grant equivalent.

Authorities would be paid their 2013-14 adjustments as a separate grant, either as a section 31 grant or, potentially, as Revenue Support Grant (chapter 6 discuses the future of Revenue Support Grant in further detail).

5.10. In addition, each billing authority will make a contribution to the *set aside* based on their *proportionate shares*. The *set aside* will be based on the 2014-15 *forecast national business rates*, as part of our commitment to manage the business rates retention scheme within 2014-15 spending figures. Since the *forecast national business rates* will be lower in 2013-14, we will reduce the amount each billing authority pays towards the *set aside* in 2013-14 accordingly.

TP1 Q5: Do you agree with the proposed approach for ensuring that no authority loses out in 2013-14 as a result of managing the business rates retention system within the 2014-15 expenditure control total?

Floor damping

5.11. For either option, we would need to decide whether to use 2012-13 formula grant before or after floor damping; and, if it is used after floor damping, which year to take as the base position for the floor damping calculations.

5.12. To ensure stability in the financing of local services, the Government currently ensures that a lower limit - known as a “floor” - is set to each authority’s change in their formula grant allocation year on year. This floor works on a like-for-like basis (i.e. after adjusting for changes in funding and responsibility). The floor is paid for by scaling back the change above the floor for other authorities. Annex A sets out how floor damping works in the current system.

5.13. The charts in annex A help to illustrate the wide variation in formula grant before floor damping compared to formula grant after floor damping. The tables illustrate this further.

Education/Personal Social Services Authorities

Change in formula grant before and after floor damping expressed as a percentage of the previous year's formula grant	Number of authorities
-20% or more	7
-20% to -10%	8
-10% to -5%	10
-5% to 0%	24
0% to 5%	71
5% to 10%	30
10% to 20%	1
20% or more	0

Police Authorities

Change in formula grant before and after floor damping expressed as a percentage of the previous year's formula grant	Number of authorities
-20% or more	1
-20% to -10%	0
-10% to -5%	5
-5% to 0%	11
0% to 5%	17
5% to 10%	3
10% to 20%	1
20% or more	1

Fire Authorities

Change in formula grant before and after floor damping expressed as a percentage of the previous year's formula grant	Number of authorities
-20% or more	0
-20% to -10%	0
-10% to -5%	2
-5% to 0%	6
0% to 5%	23
5% to 10%	0
10% to 20%	0
20% or more	0

Shire Districts

Change in formula grant before and after floor damping expressed as a percentage of the previous year's formula grant	Number of authorities
-20% or more	0
-20% to -10%	17
-10% to -5%	36
-5% to 0%	42
0% to 5%	56
5% to 10%	30
10% to 20%	17
20% or more	3

5.14. Removing floor damping would see some authorities face significant losses, whilst other authorities would experience significant gains.

5.15. The Government believes it is important to maintain local budget stability whilst a new model of local government finance is introduced, particularly in the current challenging economic climate. We are therefore minded to establish individual authorities' *baseline funding* levels on the basis of 2012-13 formula grant after floor damping.

5.16. Under this approach, we would need to decide which year to take as the base year for floor damping calculations. It could be argued that we would, in effect, be recalculating the 2012-13 formula grant, and should therefore again use 2011-12 as the base year. It could alternatively be argued, since the rationale for using 2012-13 formula grant to establish individual authorities' *baseline funding* levels is to ensure a fair starting point at the outset of the business rates retention scheme in 2013-14, that this is the equivalent of calculating a 2013-14 formula grant and we should therefore use 2012-13 as the base year.

5.17. However, in practice, as explained at paragraph 5.9, we would make two separate calculations: one to establish their *baseline funding* levels using the lower (2014-15) spending figures; and a second to establish a 2013-14 funding equivalent for each authority, on which their 2013-14 adjustment would be based. We intend that, in 2013-14, the sum of an authority's *baseline funding* level and the separate grants it receives (to reflect its 2013-14 adjustment and its share of the forecast surplus New Homes Bonus funding) should be broadly equivalent to what it would have received in formula grant in 2013-14. We therefore propose to use 2012-13 allocations as the base position for floor damping in the calculation of each authority's 2013-14 formula grant equivalent.

5.18. We further propose to use each authority's 2013-14 formula grant equivalent as the base position for floor damping in the calculation of their *baseline funding* levels, which will be based on 2014-15 spending figures as discussed above. This approach would maximise local budget stability whilst the new funding system is introduced.

TP1 Q6: Do you agree that we should use 2012-13 formula grant after floor damping as the basis for establishing authorities' *baseline funding* levels? If not, why?

TP1 Q7: Do you agree that we should use 2012-13 allocations as the base position for floor damping in calculating the 2013-14 formula grant equivalent; and use the 2013-14 formula grant equivalent as the base position for floor damping in calculating individual authority's *baseline funding* levels?

TP1 Q8: If not, which years should be used as the base position for floor damping in each of these calculations, and why?

5.19. The rest of this chapter discusses the two options for using 2012-13 formula grant to establish individual authorities *baseline funding* levels in further detail. It also seeks views on proposals for establishing guaranteed funding allocations for police authorities, and potentially also single purpose fire and rescue authorities.

Option one: adjust actual 2012-13 formula grant allocations

5.20. Under this option, we would reduce actual 2012-13 formula grant allocations in proportion to the reduced spending control totals to establish individual authorities' *baseline funding* levels. This option would freeze the 2012-13 distribution.

5.21. In scaling down, it would not be possible simply to reduce the 2012-13 allocation for each authority according to the overall 2014-15 expenditure control total, as this would not reflect the different spending profiles for the four different tiers of service (lower-tier, upper-tier, police and fire) included in the 2010 Spending Review. The table below illustrates this.

Service	2010-11	2011-12	2012-13	2013-14	2014-15
Police	£3,544m	£3,345m	£3,138m	£3,093m	£3,051m
Year on year change		*-5.6%*	*-6.2%*	*-1.4%*	*-1.4%*
Fire	£1,038m	£995m	£988m	£953m	£909m
Year on year change		*-4.1%*	*-0.7%*	*-3.5%*	*-4.6%*
Other	£23,452m	£20,641m	£19,259m	£19,150m	£17,896m
Year on year change		*-12.0%*	*-6.7%*	*-0.6%*	*-6.5%*
Total	£28,034m	£24,981m	£23,385m	£23,196m	£21,856m
Year on year change		*-10.9%*	*-6.4%*	*-0.8%*	*-5.8%*

5.22. A number of authorities provide more than one tier of service (for example Cornwall County Council provides both lower- and upper-tier services as well as fire services for its area). For these authorities, we would first have to break down their 2012-13 formula grant into the amount allowed for each tier of service, and then apply standard reduction rates to each service tier. Annex B provides further details of how we would do this.

TP1 Q9: If option one is implemented, do you agree that we should reduce the formula grant for each tier of services according to its Spending Review profile?

TP1 Q10: If so, do you agree with the proposed methodology for splitting formula grant between the service tiers for those authorities that have responsibility for more than one tier of service, as described in annex B?

*O*ption two: apply the 2012-13 formula grant process

5.23. This approach would apply what is essentially the existing process for calculating formula grant to the sum of the *national business rates baseline*, the police adjustment and any fire adjustment, retaining most of the features of the 2012-13 methodology. This option would produce greater changes to the current distribution than option one.

5.24. There are a number of choices to be made within this option:

- whether to update data
- whether to review the formulae for grants rolled in using tailored distributions[3]
- whether to review the relative needs formula; and
- whether to alter the amount that we take service demands and resources into account

[3] Part B of Section 5 of the draft Local Government Finance Report (England) 2012/2013

5.25. We would welcome views on these choices, each of which is discussed in more detail below.

Whether to update data

5.26. Under the current system, we have used the most up to date data available in setting formula grant. Population data is the biggest driver influencing the cost of providing services. We therefore propose that we should use updated population data. As the 2011-based sub-national population projections will not be available until late 2013, we would need to use either:

- revised 2010-based sub-national population projections (likely to be available May 2012), incorporating further improvements to migration data but not 2011 Census data; or

- mid-2011 population estimates (available September 2012), incorporating 2011 Census data, as well as improved migration data

5.27. Under the current system, we would normally use population projections, as they are forward-looking and relate to the actual period of the multi-year settlement, whereas mid-year population estimates relate to the period prior to the multi-year settlement.

5.28. Under the business rates retention scheme, individual authorities' baseline levels of funding would not be reviewed annually. Instead, they would be used to calculate tariffs and top ups which would then be fixed until any reset, therefore providing a strong incentive for business growth. It could be argued that the fact that tariffs and top ups will be fixed means it continues to be important that *baseline funding* levels are calculated using forward-looking datasets, to anticipate future cost pressures. This would, however, mean that we were unable to reflect any changes resulting from the 2011 Census. Alternatively, it could be argued that using forward-looking data is less relevant, and that tariffs and top ups should reflect our best estimate of relative needs at the outset of the business rates retention scheme so that the future distribution of resources is closely aligned with business growth.

5.29. Under the current system, we also use projections for the *council tax base* dataset (i.e. the number of council tax band-D equivalent properties in an authority's area, after adjusting for discounts and exemptions). A number of local authorities have commented that the projections over-estimate their council tax base. However, if we were to use the mid-2011 population estimates in the baseline, this may be viewed as inconsistent with using projections for the council tax base. If option two were implemented, and Government decided to update population and/or council tax base data, we would consult in summer 2012 on whether to use projections.

5.30. In addition, around 100 other data sets are used in calculating formula grant, including data regarding the costs of service delivery which is used to make an area cost adjustment. We do not attempt to use projections for other data; instead we generally use historic multi-year averages, to smooth the variability between years.

TP1 Q11: If option two is implemented, do you think we should update none, some or all of the data sets used in the formula grant calculations? If you think some should be updated, which ones, and why?

Whether to review the formulae for grants rolled in using tailored distributions

5.31. A number of special grants were rolled into formula grant as part of the 2010 Spending Review with distributions based on their 2010-11 allocations. Under option two, we could take the opportunity to review the formulae to take account of grants rolled in using tailored distributions, which includes:

- Local Transport Services funding (£72m in 2012-13), which is made up of three elements: road safety, rural bus subsidy and detrunking. The elements for road safety and rural bus subsidy could be included in the County-level Environmental, Protective and Cultural Services relative needs formula, after adjusting the London scaling factor to reflect the fact that these services are funded differently in London. The detrunking element could potentially be incorporated into the Highway Maintenance relative needs formula, however, previous work has shown that this may not be possible, and this element may therefore need to remain separate.

- Supporting People funding (£1.62bn in 2012-13), which was rolled in using the Supporting People Distribution Formula. Prior to this funding being rolled into formula grant, a “pace of change” approach was used to smooth the transition from a legacy pattern of funding to one based on a distribution formula. Since formula grant already operates its own floor damping methodology, we did not continue the pace of change approach. If we were to review the formulae for distributing Supporting People funding, we would want to consider carefully what would be the appropriate relative needs formula to use, or whether we would need to derive a new formula, if the existing distribution differs considerably from that of other existing relative needs formulae.

- Housing Strategy for Older People funding (£13.5m in 2012-13), which is currently distributed using the same formulae as the older people element of Supporting People funding. If reviewed, we would consider alongside Supporting People.

- Learning and Skills Council staff transfer funding (£42.3m in 2012-13), which could be incorporated into the Local Authority Central Education Services relative needs formula.

- Preserved Rights funding (£221.7m in 2012-13) and HIV/AIDS Suppor*t* (£30.5m in 2012-13), which have very different distributions to the current adult social care formulae. If reviewed, separate formulae could be created.

- Animal Health and Welfare funding (£4m in 2012-13), which could be included in the County-level Environmental, Protective and Cultural Services relative needs formula.

- County Council Functions for Civil Contingencies in London funding (£0.6m in 2012-13) may need to remain separate.

5.32. Under option two, if we were to take the opportunity to review the formulae for these grants, we would involve local government experts and would consult formally on the options in summer 2012.

TP1 Q12: If option two is implemented, do you think we should review the formulae for none, some or all of the grants rolled in using tailored distributions? If you think the formulae should be reviewed for some of these grants, which ones, and why?

Whether to review relative needs formulae for concessionary travel

5.33. Under option two we could take the opportunity to review relative needs formula, such as the relative needs formula for concessionary travel.

5.34. Many local authorities have raised concerns over the relative needs formulae used for concessionary travel in the 2011-12 and 2012-13 settlement, in part as a result of responsibility for concessionary travel transferring from shire districts to shire counties. In response, we consulted on a wide range of options over the summer of 2010. The formula that was eventually chosen, as it received the most support during consultation, was not based on specific concessionary travel variables.

5.35. If option two is implemented, and we take the opportunity to review the formula for concessionary travel, we would work up options with local government and consult widely on them in summer 2012.

5.36. The majority of other relative needs formulae were reviewed prior to the 2011-12 Settlement with the exception of those used for adult social services. The Government is carefully considering the recommendations of the Commission on the Funding for Care and Support. Following engagement with stakeholders, it will publish a white paper on wider social care issues next spring, and a progress report on funding. It would not be sensible to review the formulae before the white paper has been published. This means a review is unlikely to be possible for 2013-14.

TP1 Q13: If option two is implemented, do you think we should review the relative needs formula for concessionary travel?

TP1 Q14: Do you think we should review any of the other relative needs formulae? If so, which ones and why?

Whether to alter the balance between service demands and resources

5.37. The current system takes account of both relative needs (the relative cost of providing services in the area) and relative resources (an authority's relative ability to raise council tax). It achieves this by distributing a proportion of the overall amount according to relative needs, known as "the relative needs amount"; a proportion according to relative resources, known as "the relative resources amount"; and a proportion allocated on a per head amount, depending on the services provided, known as "the central allocation".

5.38. Under option two, we could take the opportunity to review the balance between these amounts, which has periodically been altered as shown in the table below:

Year	Relative Needs Amount	Relative Resource Amount	Central Allocation
2006-07 and 2007-08	70.99%	-24.57%	53.58%
2008-09, 2009-10 and 2010-11	73.0%	-26.6%	53.6%
2011-12 and 2012-13	83.0%	-26.6%	43.6%

TP1 Q15: If option two is implemented, do you think we should alter the balance between service demands and resources; and if so, how?

Establishing guaranteed funding levels for police authorities

5.39. *Technical Paper 3: Non-billing Authorities* discusses the Government's proposal to provide police authorities, and potentially also single purpose fire and rescue authorities, with guaranteed funding allocations in 2013-14 and 2014-15. These allocations would not be affected by business rates growth or decline.

5.40. We propose to establish guaranteed funding allocations by applying the 2012-13 formula grant process to the sum of the *national business rates baseline*, the police adjustment and any fire adjustment. The calculated amounts for police authorities, and potentially also single purpose fire and rescue authorities, for 2013-14 and 2014-15 could be distributed via either Section 31 grant or, potentially, Revenue Support Grant[4] (see the section in chapter 6 on the "Future of Revenue Support Grant").

5.41. Since this is broadly the same as option two for establishing *baseline funding* levels for all other authorities, we intend to use consultation responses to questions on option two to inform decisions on the methodology for establishing guaranteed levels of funding for the relevant authorities. We would use 2012-13 as the base year for damping the 2013-14 allocations and 2013-14 as the baseline for damping the 2014-15 allocations.

TP1 Q16: Do you agree with the proposed approach for establishing guaranteed levels of funding for police authorities, and potentially also single purpose fire and rescue authorities, in 2013-14 and 2014-15?

[4] The City of London has responsibility for police together with the same functions as other London Boroughs. Since 2011-12 it has been notionally split into two authorities for floor damping purposes – one for police services and the other for non-police services. We would therefore continue to treat the City of London notionally as two separate authorities under the rates retention system. That portion that relates to police services would be treated in the same way as other police authorities and that which relates to non-police services would be treated in the same way as other London Boroughs.

Chapter 6

Fixing individual authorities' baseline funding levels

6.1. Once individual authorities' *baseline funding* levels have been established and compared with their *individual authority business rates baseline* to derive tariffs and top ups, they would not be reviewed to take account of changes in relative needs or resources until any reset.

6.2. Instead, tariffs and top ups would be fixed, so that authorities would stand to benefit from growth in their business rates (subject to the operation of the *levy*) while those whose rates declined or grew at a lower rate would experience lower or negative growth in revenue (subject to safety net), providing a strong incentive for local authorities to promote business growth in their area.

6.3. This chapter considers options for funding new burdens, dealing with any boundary changes, and handling any changes in local authority functions that arise when *baseline funding* levels are fixed between resets. It also discusses the future of Revenue Support Grant, including options for making it discretionary; proposals for retaining a Local Government Finance Report; and funding for specified bodies.

Funding new burdens

6.4. To ensure that pressure on council tax is kept down, there is a long standing principle that the net additional cost to local government of any new burdens placed on local authorities (including parishes, police and fire and rescue authorities) by central government must be assessed and fully funded.

6.5. Under the current system, new burdens are funded by transferring additional funding into Revenue Support Grant at the beginning of a multi-year settlement period. If a new burden arises during a multi-year settlement period, a section 31 grant is paid, before it is rolled into Revenue Support Grant at the beginning of the next multi-year period.

6.6. Under the business rates retention scheme, some form of new burdens principle would continue to be needed to prevent excessive increases in council tax. We therefore propose to review the existing new burdens doctrine to take account of the proposals in this consultation.

6.7. We propose to continue funding new burdens within the business rates retention scheme between resets via section 31 grants or potentially Revenue Support Grant. The amount of Revenue Support Grant paid to authorities would be determined on an annual basis. Any new burdens arising during the year could be paid to local authorities by central government departments through section 31 grants. As soon as it is feasible, the funding would be transferred into Revenue Support

Grant, where it would remain until any reset of tariffs and top ups to realign resources with service demands.

6.8. This approach would provide transparency and certainty over new burdens funding and be consistent with our objective to reduce the amount of ringfenced funding.

TP1 Q17: Do you agree with the proposed approach for funding new burdens within the business rates retention scheme? If not, why?

Changes to local authorities functions and responsibilities

6.9. Chapter 4 discusses how we would make an adjustment to the *national business rates baseline* to fund any changes to local authorities functions and responsibilities occurring prior to year one of the scheme.

6.10. Thereafter, since baseline levels of funding would not be reviewed until any reset, and tariff and top ups would be fixed, it would not be possible to make a net transfer of functions from local authorities between resets.

6.11. In the case of a function or responsibility being transferred to local authorities between resets, we propose to adopt a similar methodology to that described above for funding new burdens between resets.

Boundary changes and mergers

6.12. Under the current system, boundary changes and mergers occurring within a multi-year settlement are handled in such a way as to ensure that formula grant for all other authorities remains unchanged.

6.13. Similarly, within the business rates retention scheme, we propose that boundary changes or mergers that occur between resets should not affect the position for other authorities unchanged, and their tariffs or top ups should remain fixed.

Boundary changes

6.14. The Local Government Boundary Commission for England is responsible for conducting reviews of the structure of local government and the external boundaries of local authorities. It may undertake reviews of the external boundary of a district or county at the request of central government, at the request of a local council, or on their own initiative. It is currently reviewing the boundary between Welwyn Hatfield Borough and St Albans City Councils.

6.15. Where boundary reviews involve a small number of houses and business properties with a low net rateable value, they would not have a significant impact on a local authority's expenditure on services or on its business rates income. We would not therefore propose to alter tariffs or top ups for the local authorities concerned.

6.16. If a larger boundary review is proposed that would transfer significant service demands and/or business rates income from one authority to another, we would consider adjusting the tariff or top up of the local authorities concerned to reflect this. As tariffs and top ups are self-funding at national level, any local adjustments to tariffs and top ups would also have to be self-funding. We would consult the local authorities concerned to establish an appropriate methodology for making these changes.

Mergers

6.17. Where two or more local authorities merge to form a new authority covering the combined area of the authorities, we propose that their individual *baseline funding* levels, *individual authority business rates baselines* and tariffs and/or top ups are added together to form the *baseline funding* level, *individual authority business rates baseline* and tariff or top up of the new authority.

Example
Suppose that authorities A, B and C wish to merge.

Authority A is a tariff authority contributing £10,000
Authority B is a top up authority receiving £2,000
Authority C is a top up authority receiving £5,000

The new authority would be a tariff authority contributing £3,000 (i.e. £10,000 - £2,000 - £5,000)

6.18. If a new single purpose fire and rescue authority is created by a merger and one or more county councils transfer their responsibilities for fire services to it, an appropriate share of the tariff or top up of each county council affected would need to be apportioned to the new fire authority. The apportionment would have to be decided and agreed by negotiation between the new fire authority and the existing county authorities.

Changes which have been agreed prior to year one of the scheme

6.19. Under option one for establishing individual authorities' *baseline funding* levels, we would reduce authorities' 2012-13 formula grant allocations in proportion to the lower spending control totals. We would therefore have to deal with any boundary changes, mergers and structural changes as if we were already in a period between resets.

6.20. Under option two for establishing individual authorities' *baseline funding* levels, we would re-run the 2012-13 formula grant process using the lower spending control totals, and it would therefore be possible to take account of any boundary changes, mergers and structural changes in establishing *baseline funding* levels.

TP1 Q18: Do you agree with the proposed approach for dealing with boundary changes and mergers? If not, what alternative would you propose, and why?

Future of Revenue Support Grant

6.21. Up to now the amount of business rates collected has not been sufficient to fully fund the services local government provides, after allowing for funding raised through council tax and specific grants. The Government has made up this difference with Revenue Support Grant, which it is currently legally obliged to pay each year, based on a distribution set out in the Local Government Finance Report. The amount of Revenue Support Grant calculated under this distribution for individual authorities may be zero.

6.22. Since, under the business rates retention scheme, Revenue Support Grant would only be used to fund new burdens and any functions transferred to local authorities between resets, it follows that, at least at the outset of the new scheme, the overall amount could be zero. For this reason the Government proposes to take powers to make Revenue Support Grant discretionary rather than mandatory. To this extent, it would become similar to section 31 grants. It would be calculated differently, and would look more akin to the current Local Services Support Grant, bringing many individual funding streams together in a single grant.

6.23. Any Revenue Support Grant paid would, however, still be un-hypothecated and central government could not impose conditions on the use of the funding. It would continue to be paid in instalments throughout the year.

TP1 Q19: Do you agree with the proposals on the future of Revenue Support Grant?

Retaining a Local Government Finance Report

6.24. Under current legislation, the total amount of Revenue Support Grant to be distributed, together with its basis of distribution, and the total of business rates to be redistributed, together with its basis of distribution, must be set out in a Local Government Finance Report.

6.25. We intend to retain a Local Government Finance Report for each year under the new scheme. This would set out the basis of the rates retention scheme, including the derivation of the tariffs and top ups. It could also set out the basis of distribution for Revenue Support Grant, if any.

Funding for specified bodies

6.26. A small proportion of Revenue Support Grant is currently allocated to fund specified bodies to deliver certain functions, generally of a cross-cutting nature. In 2010-11, just over £45m was allocated to nine specified bodies. In 2011-12, £32.5m was allocated to one specified body, the Improvement and Development Agency for Local Government.

6.27. The reforms discussed in this consultation document will have no impact on the Government's decisions on the funding of these functions in the future.

Chapter 7

Resetting the system

7.1. As set out in the main consultation paper, the Government proposes there should be an option to reset the business rates retention scheme if, over time, it was felt that resources no longer met changing service pressures sufficiently within individual local authority areas (for example, because of population movements, or the characteristics of the area changing).

7.2. A reset would involve re-assessing individual authorities' *baseline funding* levels - potentially on the basis of a completely new method for assessing relative needs and resources - and recalculating tariff and top ups accordingly.

7.3. The main consultation paper invites views on the proposal for government discretion regarding the method for assessing relative needs and resources at any reset. We would develop any new methodology in discussion with local government, prior to a full formal consultation.

7.4. The main consultation paper also seeks views on options for resets to be carried out either at fixed intervals or at the Government's discretion; and to involve either a partial reset of the original *national business rates baseline*, or a full reset including growth achieved against the original baseline. Each of these options is discussed in further detail below, to help inform responses to the questions in the main consultation paper.

Partial or full resets

7.5. Under a full reset, all of the business rates within the scheme including growth achieved on the original *national business rates baseline* would be taken into account to establish individual authorities' *new baseline funding* levels, from which their new tariffs or top ups would be derived. This approach would mean that local authorities only benefited from business growth in their area in the period between resets.

7.6. Alternatively, under a partial reset, whilst the original *national business rates baseline* would be redistributed between individual authorities to establish their new *baseline funding* levels and their tariffs and top ups, any growth against the original *national business rates baseline* would continue to sit with the authorities that achieved it.

7.7. Since central government annually uprates the national business rates multiplier by *Retail Prices Index* (*RPI*), it would seem logical, in the event of a partial reset, to also uprate the *national business rates baseline* by RPI. This would ensure that business rates growth resulting from changes in the national non-domestic rates multiplier is redistributed, whilst business rates growth resulting from changes in the local tax base is retained by the authorities in which it was achieved.

7.8. Partial resets could help to achieve a balance between providing certainty over the time period for which authorities benefit from business growth to maximise the incentive effect whilst preserving Government's ability to ensure that authorities are able to meet the needs of local people in their area. For instance, one possible approach would be to only carry out full resets at fixed intervals, whilst retaining discretion to carry out a partial reset if it proved necessary to realign resources between full resets to ensure local authorities remained able to meet local needs.

Resets at fixed or discretionary intervals

7.9. Setting a fixed period between resets would give local authorities certainty over the period for which they would retain the benefits of growth. This certainty would help to ensure that the business rates retention scheme provides a strong incentive for business growth, and could also help local authorities to bring forward tax increment financing schemes under the prudential borrowing system.

7.10. In principle, the longer the period between resets, the greater the incentive for business growth, as local authorities would retain the benefit of growth for longer. If the period between resets is too short, new developments may not be completed and begin generating business rates in time for the local authority to benefit at all.

7.11. If resets were carried out at the Government's discretion, local authorities might feel they could generate better results for their area by demonstrating need in their area and lobbying government to carry out a reset, rather than driving cost efficiencies or investing in local growth.

7.12. However, if the timing of resets is known in advance, the more possible it becomes for local authorities to plan on that basis, and potentially to manage growth and investment in their area to seek to achieve the maximum gains from the reset process. This could result in perverse outcomes (particularly under full resets), with local authorities seeking to delay business growth in their area in the year before a reset is due.

7.13. Furthermore, if the Government did not have discretion to reset the system other than at fixed intervals, it would have very limited levers for re-aligning resources with needs in the event that, over time, changes in service demands meant that some authorities became unable to meet the needs of local people in their area.

7.14. The option of fixed period between full resets, discussed above, could help to achieve a balance between providing certainty over the time period for which authorities benefit from business growth to maximise the incentive effect, whilst preserving the Government's ability to ensure that authorities are able to meet the needs of local people in their area through the option of a partial reset at other times.

Annex A

The current floor damping scheme

A1 Authorities are split into four groups as follows:

- authorities with responsibility for education and personal social services ("education/Personal Social Services authorities")
- police authorities (except the Metropolitan Police Authority) and the Greater London Authority (police part)
- fire authorities (except the London Fire and Civil Defence Authority) and the Greater London Authority (fire part); and
- shire districts in two tier shire areas (i.e. those shire districts which do not have responsibility for education and personal social services)

A2 The floor damping system is self-financing within each group of authorities. Authorities in one group do not cross-subsidise the floor for authorities in another group.

A3 The reduction in grant for authorities above the floor is calculated by applying a constant re-scaling factor to each authority's change in grant above their floor level (not their total grant change). The re-scaling factor is calculated so that when it is applied to all authorities within the group, the saving exactly offsets the net cost of the floor. The fact that the scaling factor is only applied to changes above the floor level means that no authority can move from the 'scaled' group to the floor group.

A4 The diagrams below are a visual interpretation of how this system works for fire authorities and police authorities in the provisional 2012-13 Settlement. As can be seen, the net cost of the floor is met by a reduction for the scaled authorities. This is demonstrated by the vertical gap between the scaled authorities grant changes before and after the application of the floor damping scheme.

Diagram 1: Floor damping for fire authorities in the provisional 2012-13 settlement

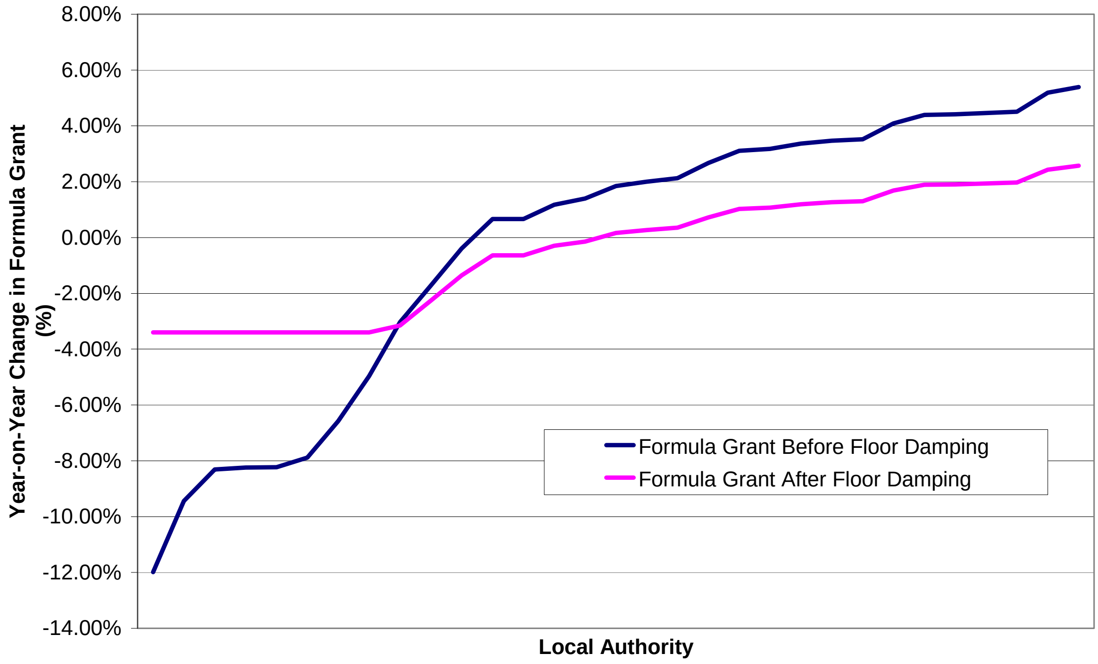
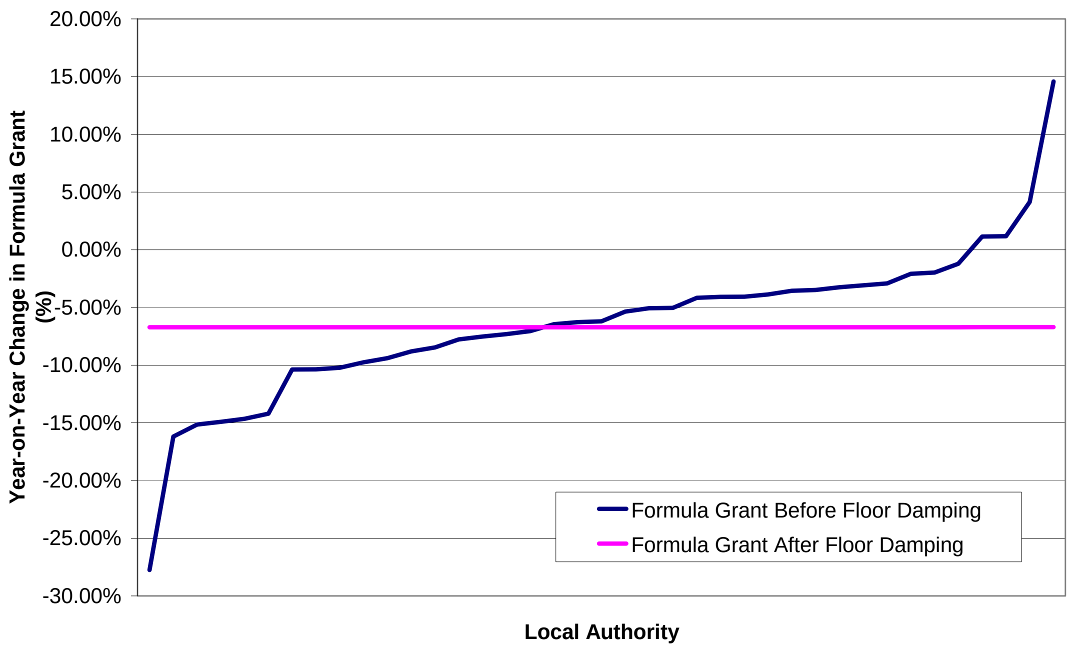


Diagram 2: Floor damping for police authorities in the provisional 2012-13 settlement

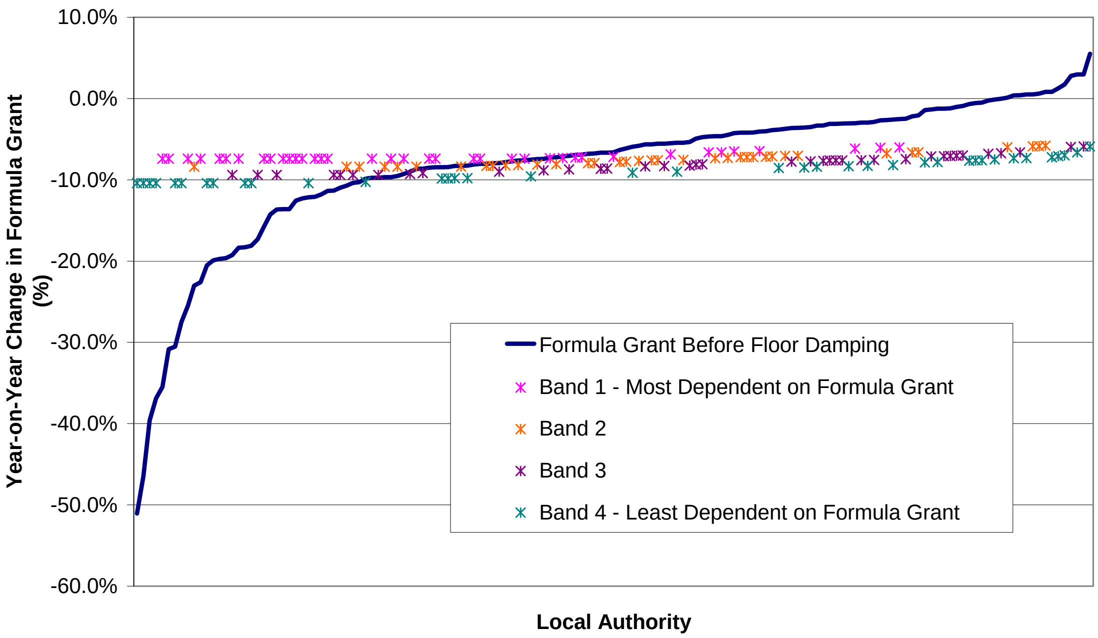


A5 In 2012-13, the floor level for fire authorities was set at -3.4 per cent, giving a scaling factor of 0.67913822; the floor level for police authorities was set at -6.703 per cent, giving a scaling factor of 0.00015768. It can clearly be seen that the higher scaling factor for fire authorities allows much more of the formula change to come through for authorities above the floor. For police, where the floor is set very close to the average, it means that the distribution of formula grant will be very similar to that for the adjusted prior year's grant.

A6 In 2011-12, the Government adopted a new approach to setting the floors for education/Personal Social Services authorities and shire districts. It recognised that some authorities have a higher proportion of their budget requirement funded through formula grant – and are consequently more dependent on formula grant than others. For the purpose of floor damping, authorities are therefore placed into one of four bands based on the proportion of their 2010-11 budget requirement funded by formula grant, and different floor levels are applied to each band.

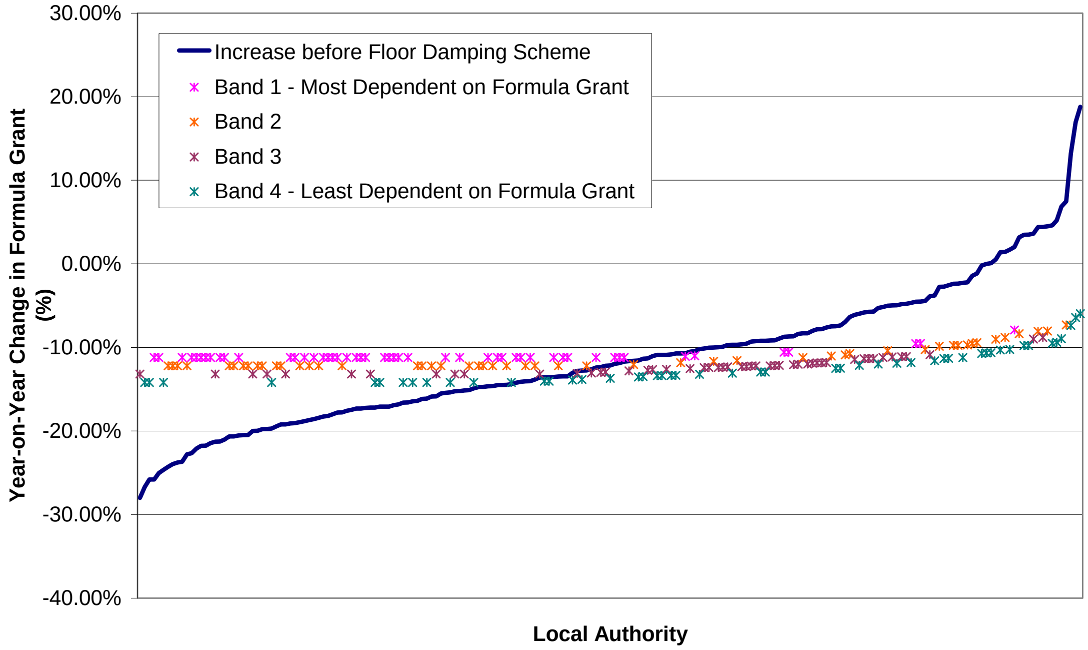
A7 The diagram below is a visual interpretation of how this system works for education/Personal Social Services authorities and shire districts in the provisional 2012-13 settlement.

Diagram 3: Floor damping for education/Personal Social Services authorities in the provisional 2012-13 settlement



A8 In 2012-13, the floor level for education/Personal Social Services authorities is set at -7.4 per cent for those in band 1 (the authorities most dependent on formula grant), -8.4 per cent for those in band 2, -9.4 per cent for those authorities in band 3, and -10.4 per cent for those authorities in band 4 (the least dependent on formula grant), giving a scaling factor of 0.28260139.

Diagram 4: Floor damping for shire districts in the provisional 2012-13 settlement



A9 In 2012-13, the floor level for shire districts is set at -11.2 per cent for those in band 1 (the authorities most dependent on formula grant), -12.2 per cent for those in band 2, -13.2 per cent for those authorities in band 3, and -14.2 per cent for those authorities in band 4 (the least dependent on formula grant), giving a scaling factor of 0.24901888.

Annex B

Splitting formula grant between tiers for authorities that provide more than one service tier

Chapter 5 discusses the options for using 2012-13 formula grant to establish individual authorities baseline funding levels, from which their tariffs and top ups would be derived. Under option one, the 2012-13 formula grant allocations would be scaled back in proportion to the reducing spending control totals. For authorities that provide more than one tier of service, we would have to break down their 2012-13 formula grant into the amount allowed for each tier of service, and then apply standard reduction rates to each service tier. This annex provides further details of how we would do this.

Grants Rolled In Using Tailored Distributions

B1 The components within the Grants Rolled In Using Tailored Distributions relate to upper-tier services. For unitary authorities receiving these allocations they would therefore be assigned to the upper-tier services.

B2 So for example, for Cornwall County Council all of its Grants Rolled In Using Tailored Distribution under the provisional 2012-13 Settlement - £19,971,229 - would be assigned to the upper-tier services portion.

Relative Need Amount

B3 The Relative Needs Amount is calculated as follows.

B4 The Relative Need Formulae (RNF) are first combined into six groups, dependent on which authorities provide the service. These are:

i. Upper-tier services which consists of children's services, adult personal social services, highway maintenance, County-Level Environmental, Protective and Cultural Services and continuing EA levies.

ii. Police services

iii. Fire services

iv. Lower-tier services which consists of district-level Environmental, Protective and Cultural Services and flood defence

v. Mixed tier services, which are provided by both upper- and lower-tier authorities, and consist of fixed costs and coast protection.

vi. Capital financing, which is provided by all authorities.

B5 For each of the six groups we then work out the minimum amount per head across all relevant authorities. This enables us to calculate an amount per head above minimum for each relevant authority. We then add together the amounts per head above the minimum across all six groups for each authority and multiply these back up by population projections. Finally, to ensure that the correct amount of funding is distributed by the Relative Needs Amount, we multiply the amount above the minimum for each authority by the “needs scaling factor” that is the relative needs amount control total divided by the sum of the amounts above minimum for all authorities.

B6 Therefore in order to split the Relative Needs Amount between the four service tiers we need to consider how to assign each of the six groups of services between the tiers.

B7 The first four groups already relate to a particular service tier so it is obvious how we will split these. We therefore simply need to consider how we would split the mixed-tier services and capital financing.

B8 We suggest for those authorities that provide both upper- and lower-tier services that the mixed tier services are assigned to the lower-tier portion.

B9 The table below shows the needs amounts per head above the minimum for Cornwall County Council in the provisional 2012-13 Settlement.

Needs amounts per head above the minimum for Cornwall County Council

Amount per head above the minimum for upper-tier services	0.00309911098072
Amount per head above the minimum for fire & rescue services	0.00022786814688
Amount per head above the minimum for lower-tier services	0.00022092690698
Amount per head above the minimum for mixed-tier services	0.00001057808670
Amount per head above the minimum for capital financing	0.00105929473996
	0.00461777886125

B10 So for example, for Cornwall County Council, we would therefore assign the upper-tier services amount (0.00309911098072) to the upper-tier services portion; the fire & rescue services amount (0.00022786814688) to the fire services portion; and the sum of the lower-tier services amount and the mixed-tier services amount (0.00022092690698 + 0.00001057808670 = 0.00023150499368) to the lower-tier services portion.

B11 For capital financing we suggest that the whole of the assumed1990 debt is assigned to the upper-tier portion, but that the subsequent Basic Credit Approvals, Supplementary Credit Approvals and Supported Capital Expenditure (Revenue) amounts are assigned according to the service to which they relate. For example we would therefore expect credit approvals for housing to be assigned to the lower-tier. Receipts taken into account (RTIA) will remain within the service they were assigned to when calculated for that year. This will enable the calculation of a capital financing Relative Needs Formulae for each service tier.

B12 However, in order to calculate the Relative Need Amount for an authority we then subtract from its capital financing Relative Needs Formulae per head, the minimum capital financing Relative Needs Formulae per head across all authorities. If we were to apply this methodology to each of the separate tier-level capital financing Relative Needs Formulae then the total of the amounts above the minima would not add back up to the original authority's capital financing Relative Needs Formulae per head above the minima. In order to solve this issue, we think that the fairest way would be to split the minimum capital financing Relative Needs Formulae per head between the tiers pro-rata to the tier-level capital financing Relative Needs Formulae per head.

B13 So for example, for Cornwall County Council for 1990 this would mean that the sum of Cornwall's districts and the County Council debt would be assigned to the upper-tier – a total of £146,696,311.

B14 Subsequent Basic Credit Approvals, Supplementary Credit Approvals and Supported Capital Expenditure (Revenue) amounts would then be taken into account according to service; so in 1992-93 for example: £17,684,000 would be assigned to the upper-tier, comprising of credit approvals for education, Personal Social Services, transport and specific Environmental, Protective and Cultural services . The lower-tier would be assigned £2,336,000, comprising of housing and specific Environmental, Protective and Cultural services credit approvals. While fire and rescue would be assigned the amount of £102,000 of credit approvals.

B15 This would ultimately lead to an assumed 2011-12 end-of-year debt for upper-tier services of £389,797,128; for lower-tier services of £23,482,662; and for fire of £3,295,792. The equivalent 2012-13 end-of year debt for upper-tier services is £374,205,243; for lower-tier services is £22,543,356; and for fire services is £3,229,876.

B16 This leads to a capital financing Relative Needs Formulae for Cornwall for upper-tier services of 0.00054649030258; for lower-tier services of 0.00003292237463; and for fire services of 0.00000462065554.

B17 From this we can calculate the service-tier needs amounts per head above the minimum for Cornwall County Council. This is shown in the table below.

	Upper-tier services	Lower-tier services	Fire Services	Provisional 2012-13 Cornwall Allocations
Capital Financing Relative Needs Formulae	0.00054649030258	0.00003292237463	0.00000462065554	0.00058403333275
2012 Sub-National Population Projections	546,129	546,129	546,129	546,129
Capital Financing Relative Needs Formulae per head	0.00100066157003	0.00006028314671	0.00000846074012	0.00106940545686
Minimum Capital Financing Relative Needs Formulae per head	0.00000946077634	0.00000056994831	0.00000007999225	0.00001011071690
Capital Financing Relative Needs Formulae per head Above Threshold	0.00099120079369	0.00005971319840	0.00000838074787	0.00105929473996

Relative Resource Amount

B18 The Relative Resource Amount is calculated as follows.

B19 Firstly the council tax base for each area is split between the four service tiers using the proportions given in annex B of the provisional Local Government Finance Report (England) 2012/2013. We then split the council tax base for the area into the four service tiers assigning these to the appropriate authorities. For each of the four tiers we then work out the minimum amount per head across all relevant authorities. This then enables us to calculate an amount per head above minimum for each relevant authority. We then add together the amounts per head above the minimum across all four tiers for each authority and multiply these back up by population projections. Finally, to ensure that the correct amount of funding is distributed by the Relative Resource Amount, we multiply the amount above the minimum for each authority by the “resource scaling factor”, that is the relative resource amount control total divided by the sum of the amounts above minimum for all authorities.

B20 Since these are already split into the four service tiers, it is obvious how they will be assigned.

B21 The table below shows the resource amounts per head above the minimum for Cornwall County Council in the provisional 2012-13 Settlement.

Resource amounts per head above the minimum for Cornwall County Council	
Amount per head above the minimum for upper-tier services	0.08610303670396
Amount per head above the minimum for fire & rescue services	0.00166753730201
Amount per head above the minimum for lower-tier services	0.01232487864235
	0.10009545264831

B22 So for example, for Cornwall County Council, we would therefore assign the upper-tier services amount (0.08610303670396) to the upper-tier services portion; the fire and rescue services amount (0.00166753730201) to the fire services portion; and the lower-tier services amount (0.01232487864235) to the lower-tier services portion.

Central Allocation

B23 This is built-up using the minima from the relative needs amount and relative resource amount described above. The sum of the relevant needs minima are multiplied by the sum of relevant needs minima by the “needs scaling factor”. We then subtract from this the sum of relevant resource minima multiplied by the “resource scaling factor”.

B24 The result is then multiplied by the projected population.

B25 Finally, to ensure that the correct amount of funding is distributed by the Central Allocation, we multiply the amount calculated above for each authority by the “central allocation scaling factor”, that is the central allocation control total divided by the sum of the amounts calculated above for all authorities.

B26 We ought to treat the individual minima in the same way as we are treating the amounts above the minima for those services. Therefore if the proposals above are accepted, the only issue arising is how to split the minima for capital financing. The simplest way would be to split the minima between service tiers proportionate to the capital financing Relative Needs Formulae for each tier.

B27 The table below shows the needs minima per head used in the provisional 2012-13 Settlement.

Minimum needs amount per head for upper-tier services	0.00464371303424
Minimum needs amount per head for fire & rescue services	0.00045538538123
Minimum needs amount per head for lower-tier services	0.00138298855115
Minimum needs amount per head for mixed-tier services	0.00000244446668
Minimum needs amount per head for capital financing	0.00001011071690
	0.00649464215021

B28 So for example, for Cornwall County Council, we would therefore assign the sum of the upper-tier minimum amount per head plus the upper-tier capital financing minimum amount per head (0.00464371303424 + 0.00000946077634 = 0.00465317381058) to the upper-tier services portion; the sum of the fire & rescue minimum amount per head plus the fire capital financing minimum amount per head (0.00045538538123 + 0.00000007999225 = 0.00045546537348) to the fire services portion; and the sum of the lower-tier minimum amount per head plus the mixed-tier minimum amount per head plus the lower-tier capital financing minimum amount per head (0.00138298855115 + 0.00000244446668 + 0.00000056994831 =0.00138600296614) to the lower-tier services portion.

B29 The table below shows the resource minima per head used in the provisional 2012-13 Settlement.

Minimum resource amount per head for upper-tier services	0.19573222938180
Minimum resource amount per head for fire & rescue services	0.00782237812912
Minimum resource amount per head for lower-tier services	0.02801731583313
	0.23157192334406

B30 So for example, for Cornwall County Council, we would therefore assign the upper-tier minimum amount per head (0.19573222938180) to the upper-tier services portion; the fire & rescue services amount (0.00782237812912) to the fire services portion; and the lower-tier services amount (0.02801731583313) to the lower-tier services portion.

Floor Damping

B31 Since the floor damping amount is based on the total formula grant for the authority, there is no obvious way of splitting this amount between tiers. We would therefore propose to split this between services tiers proportionate to the formula grant before floor damping amounts.

B32 The table below shows the how the formula grant amount for Cornwall would be split between the services.

	Upper-tier services	**Lower-tier services**	**Fire Services**	**Provisional 2012-13 Cornwall Allocations**
Grants Rolled in Using Tailored Distributions	£19,971,229			£19,971,229
Relative Needs Amount	£154,658,444	£11,011,227	£8,932,788	£174,602,459
Relative Resource Amount	-£48,745,029	-£6,977,414	-£944,034	-£56,666,477
Central Allocation	£43,042,950	£24,150,872	£8,454,430	£75,648,252
Formula Grant Before Floor Damping	£168,927,594	£28,184,685	£16,443,184	£213,555,463
Floor Damping	-£10,365,231	-£1,729,385	-£1,008,938	-£13,103,553
Formula Grant After Floor Damping	£158,562,362	£26,455,300	£15,434,247	£200,451,909

Annex C

Business Rates Retention: Glossary of technical terms

Adjustments
After deducting the *set aside* from the *forecast national business rates* further adjustments will be made to fund the New Homes Bonus, police authorities and potentially single purpose fire and rescue authorities.

Reference: *Technical Paper 1: Establishing the Baseline*, Chapter 4

Allowable deductions
A deduction made to a billing authority's business rates income, when calculating its *proportionate share*. Examples of where allowable deductions will be made are for rate reliefs and cost of collections.

Reference: *Technical Paper 2: Measuring Business Rates*, Chapter 4

Banded levy
Authorities assigned to their different levy bands with different pence in the pound levy rates based on the ratio of their *individual authority business rates baseline* and their *baseline funding level*.

Reference: *Technical Paper 5: Tariff, Top Up and Levy Options*, Chapter 4

Baseline funding level (or **individual authority baseline funding level**)
A fair starting point based on formula grant distribution, within the overall expenditure controls set out in Spending Review 2010.

Reference: *Technical Paper 1: Establishing the Baseline*, Chapter 5

Billing authority business rates baseline (pre-tier split)
Derived by dividing the *national business rates baseline* between *billing authorities* on the basis of their *proportionate shares*.

Reference: *Technical Paper 2: Measuring Business Rates*, Chapter 5

Flat rate levy
The same pence in the pound levy rate for all authorities.

Reference: *Technical Paper 5: Tariff, Top Up and Levy Options*, Chapter 4

Forecast national business rates
Forecast of national business rates for England in 2013/14 and 2014/15. Based on the 2012/13 national non-domestic multiplier, uprated for *Retail Prices Index* and the latest published information from the national non-domestic rates returns.

Reference: *Technical Paper 2: Measuring Business Rates*, Chapter 3

Gearing effect
The relationship between *individual authority business rates baseline* and the *individual authority baseline funding level*.

Reference: *Technical Paper 5: Tariff, Top Up and Levy Options*, Chapter 2

Individual authority business rates baseline
Derived by apportioning the *billing authority business rates baseline (pre-tier split)* between billing and non-billing authorities on the basis of *tier splits*.

Reference: *Technical Paper 2: Measuring Business Rates*, Chapter 5

Individual authority business rates
The amount of business rates income which each authority receives before payment of *tariffs and top ups*.

Reference: *Technical Paper 2: Measuring Business Rates*, Chapter 5

Interactive Calculator
Enables users to explore the principal features of the proposed rate retention scheme by entering their own inputs and varying components.

Reference: *Technical Paper 5: Tariff, Top Up and Levy Options*, Chapter 7

Levy
To manage the possibility that some local authorities could see disproportionate financial gains, the *levy* will recoup a share of this disproportionate benefit. Applied to the change in *pre-levy income* (either all growth or growth above *Retail Prices Index*), as measured against the *individual authority baseline funding level*.

Reference: *Technical Paper 5: Tariff, Top Up and Levy Options*, Chapter 4

National business rates baseline
The *forecast national business rates* less *set aside* and *adjustments*.

Reference: *Technical Paper 1: Establishing the Baseline*, Chapter 5 and
Technical Paper 2: Measuring Business Rates, Chapter 5

Post-levy income
Individual authority business rates minus/plus the *tariff* or *top-up*, minus any *levy*.

Reference: *Technical Paper 5: Tariff, Top Up and Levy Options*, Chapter 3

Pre-levy income
Individual authority business rates minus/plus the *tariff or top up*.

Reference: *Technical Paper 5: Tariff, Top Up and Levy Options*, Chapter 3

Proportional levy
Individual pence in the pound levy rate for each authority so that percentage growth in *retained income* is proportional to growth in *individual authority business rates*.

Reference: *Technical Paper 5: Tariff, Top Up and Levy Options*, Chapter 4

Proportionate shares
Used to apportion the *set aside*, *adjustments* and *national business rates baseline* between billing authorities. Equals a billing authority's business rates income (after *allowable deductions*) as a proportion of total business rates yield (after *allowable deductions* and exclusive of the impact of transitional relief).

Reference: *Technical Paper 2: Measuring Business Rates*, Chapter 4

Retail Prices Index
A measure of inflation in the UK.

Reference: *Technical Paper 5: Tariff, Top Up and Levy Options*, Chapter 2

Retained income
Individual authority business rates minus/plus *tariff* or *top up*, minus any *levy*, plus any *safety net* payments.

Reference: *Technical Paper 5: Tariff, Top Up and Levy Options*, Chapter 4

Revaluation adjustment
An adjustment to tariffs and top ups to ensure that authorities do not experience gains or losses as a consequence of a revaluation.

Reference: *Technical Paper 7: Revaluation and Transition*, Chapter 3

Safety net
The safety net offers: i) annual protection against a decline in *retained income* and ii) protection against a decline in *retained income* relative to the *individual authority baseline funding level*.

Reference: *Technical Paper 5: Tariff, Top Up and Levy Options*, Chapter 5

Set aside
The share of the *forecast national business rates* that will be set aside to meet the overall expenditure controls set out in Spending Review 2010. The set aside will be apportioned between billing authorities and non-billing authorities on the basis of their *proportionate shares*.

Reference: *Technical Paper 1: Establishing the Baseline*, Chapter 3

Tier splits or **tier split shares**
Applied to *billing authority business rates baseline (pre-tier split)* to establish the *individual authority business rates baseline.*

Reference: *Technical Paper 3: Non-Billing Authorities*, Chapter 3

Tariffs and top ups
Assigned to a local authority to achieve a fair starting point. An authority will pay a *tariff* if their *individual authority business rate baseline* is more than their *baseline funding level*. An authority will receive a *top up* if their *individual authority business rate baseline* is less than their *individual authority baseline funding level*.

Reference: *Technical Paper 5: Tariff, Top Up and Levy Options*, Chapter 3

Transitional adjustment
An adjustment to ensure that authorities do not experience gains or losses as a consequence of granting transitional relief.

Reference: *Technical Paper 7: Revaluation and Transition*, Chapter 4

Volatility
The degree to which individual authority business rates in a particular area may change.

Reference: *Technical Paper 6: Volatility*, Chapter 3

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