

PROVISIONAL LOCAL GOVERNMENT SETTLEMENT

The Comprehensive Spending Review (CSR) released in October 2010 and the detailed Local Government Finance Settlement that followed confirmed the unprecedented reductions in Local Government Funding over the next four years, which were front loaded. Detailed settlement figures were provided for 2011/12 and 2012/13 but the final two years were subject to a Local Government Resource Review, which concluded with the announcement of the draft settlement in December.

No detailed grant settlement figures had been released for 2013/14 and beyond, and given the level of uncertainty, in calculating an indicative Council Tax for 2013/14 it had been assumed that the figures for National Non-Domestic Rates (NNDR) and Revenue Support Grant (RSG) would reduce by 7%. Uncertainty was heightened as the financial year 2013/14 sees a number of fundamental changes including:

- The retention of Business Rates and the extent to which Local Authorities may benefit or lose from increases / decreases in Business Rate growth.
- The localisation of support for Council Tax including an associated 10% reduction in funding.
- The transfer of Public Health to Local Authorities and its associated funding.
- The introduction of Police Commissioners from November 2012 and the associated transfer of crime prevention responsibilities from Local Authorities.

In addition, it was difficult to predict the future of health funding allocated to Local Government beyond 2012/13 but it was assumed that there would be a continuation of this funding in line with the indicative levels set out in the CSR.

Since the CSR announcement which set out the local government spending control totals there were subsequent changes in the light of changing government policy and the ongoing difficult economic position. These changes were crystallised in the publication by the Department for Communities and Local Government (CLG) entitled “Business Rates Retention – Technical Guidance” and indicated a reduction in funding in excess of that set out in 2010.

The changes included transfers and adjustments to the local government spending control totals, and included proposed methodologies for incorporating those separate grant funding streams into the new Business Rates Retention (BRR) Scheme from April 2013.

In the light of the information set out in the publication by the Department for Communities and Local Government (CLG) entitled “Business Rates Retention – Technical Guidance” the original 7% reduction in funding was reduced downwards by a further £1M, effectively allowing for an 8% reduction in government grant funding, (excluding the impact of New Homes Bonus for which the Council will receive additional funding).

The Local Government Financial Settlement was officially released on 19 December 2012 but many of the figures did not become available until the next day. Even then the figures have been continually amended with DCLG even sending out a revised settlement on the 4 January 2013 and there remain details to be published.

Unlike the CSR which provided a national high level funding position for the 4 year period 2011/12 – 2014/15, the provisional settlement provides Southampton with our provisional funding allocations for the next two years (2013/14 and 2014/15) only. The final allocations are expected to be confirmed in January / February 2013. No further information is available for 2015/16.

HEADLINE POSITION AS PER GOVERNMENT ANNOUNCEMENT

The Secretary of State announced that councils will face an average cut of 1.7% in their “spending power”; and that no local authority would experience a decrease of more than 8.8% in 2013/14, as a result of the grant reductions. These comparative figures relate to local authority “revenue spending power” – a new definition used by the government, which encompasses an individual authority’s:

- council tax
- start up funding (which replaces formula funding)
- specific grants
- NHS funding for social care

A reduction in Revenue Spending Power of 2.0% was announced for Southampton. This figure is incorrect and double counts some elements of funding in respect of Council Tax Benefit and furthermore it misrepresents the true reduction in funding. The system is complicated and it can be argued this lack of transparency hides the significant cuts that local authorities have been subject to over recent years.

REAL POSITION

The Government funding system for local authorities has changed significantly since 2010. Below is the estimated position which was assumed for financial planning purposes as published in November compared to the provisional settlement:

| | 2012/13 | 2013/14 | | 2014/15 | |
|---|-------------------------|-------------------------|-----|-------------------------|------|
| | £000's | £000's | | £000's | |
| <u>Estimate</u> | | | | | |
| Non-Ring Fenced Grants (Excluding New Homes Bonus) | 19,462.7 | 18,100.3 | -7% | 16,833.3 | -7% |
| Formula Grant | 99,483.2 | 91,519.4 | -8% | 85,042.1 | -7% |
| Subtotal | <u>118,945.9</u> | <u>109,619.7</u> | | <u>101,875.4</u> | |
| New Homes Bonus | 1,864.9 | 2,664.9 | | | |
| Council Tax Benefit Support | | 14,009.0 | | 14,009.0 | |
| Total | <u>120,810.8</u> | <u>126,293.6</u> | | <u>115,884.4</u> | |
| <u>Updated</u> | | | | | |
| Non-Ring Fenced Grants (Exc New Homes Bonus & New Burdens*) | 19,462.7 | 17,773.7 | -9% | 14,139.9 | -20% |
| Formula Grant | 99,483.2 | 92,929.1 | -7% | 82,101.3 | -12% |
| Subtotal | <u>118,945.9</u> | <u>110,702.8</u> | | <u>96,241.2</u> | |
| New Homes Bonus | 1,864.9 | 2,581.8 | | | |
| Council Tax Benefit Support | | 14,254.6 | | 14,254.6 | |
| Total | <u>120,810.8</u> | <u>127,539.2</u> | | <u>110,495.8</u> | |

This shows that the headline reductions in funding are broadly in line with expectations in 2013/14 but 2014/15 represents a worsening position. Having tracked the headline numbers then further work has been undertaken to factor in changes to expenditure which are summarised below:

| | 2013/14 | 2014/15 |
|--------------------------------|-------------------------|-----------------------|
| | Updated | Updated |
| | £000's | £000's |
| Difference | (1,245.6) | 5,388.6 |
| Offsetting Expenditure Changes | (1,836.3) | (2,547.3) |
| | <u>(3,081.9)</u> | <u>2,841.3</u> |

(* This includes provision for the Social Fund of £654.2k in 2013/14 and £644.7k in future years, responsibility for which passes to the Council from the DWP in April 2013)

BUSINESS RATES

The 2013/14 provisional finance settlement sees the launch of the Business Rates Retention (BRR) Scheme as the principle form of local government funding. In previous years, the provisional settlement announcement provided local authorities with their expected general revenue allocations for the following financial year. For 2013/14, the provisional settlement provides authorities with a combination of provisional grant allocations and their respective starting points within the BRR Scheme.

The settlement announces the key numbers around which authorities will take their decisions and this is the final element of the settlement.

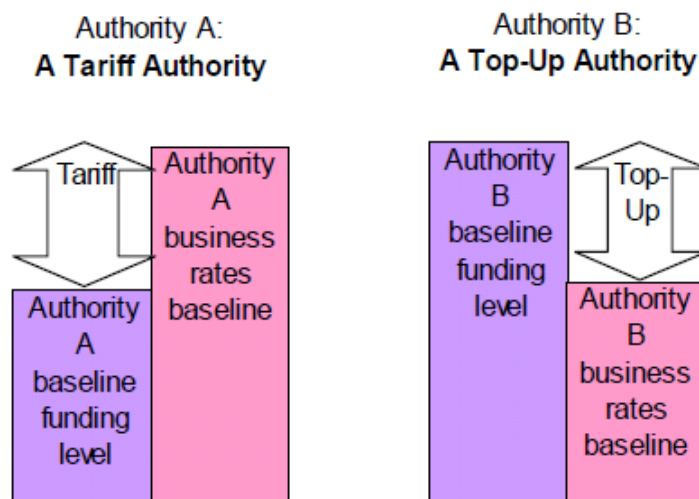
The Estimated Business Rates Aggregate for 2013/14 has been announced as £21.8bn. This is the overall amount that the Government estimate will be collected through business rates in the coming year. This figure is lower than anticipated.

The expected business rates aggregate is divided between the central and local share - 50% for each. The central share is retained by the Government and will be used to pay Revenue Support Grant and police funding. The local share for Southampton is further split with the Council receiving 48% and the Fire Service 2%.

'Proportionate shares' are the mechanism for apportioning the local share between authorities. They are based on the percentage of national business rates that an authority has historically collected and this has been calculated as the average of business rates collected in 2010/11 and 2011/12. For Southampton this figure is 0.44% which is lower than previously anticipated. This is due to the impact of large refunds made in 2010/11 relating to prior years which distort the two year average as shown below:

| | 2010/11 | 2011/12 | Average |
|-------------|----------------|----------------|----------------|
| | £ | £ | £ |
| Southampton | 82,229,210 | 96,493,905 | 89,361,557 |

For each authority the result of this calculation is compared with its baseline funding level. If the expected business rates are greater than the baseline funding level it is a tariff authority; if it is the other way round it is a top-up authority.



For Southampton the figures in question are:

| | £ |
|--|---------------|
| Billing Authority Business Rates Baseline | 47,763,377.95 |
| Business Rates Baseline (After 2% to Fire Authority) | 46,808,110.39 |
| Baseline Funding Level | 48,357,475.34 |
| Top Up | 1,549,364.95 |

These figures reflect the lower than anticipated overall estimate of business rates at a national level and the distortion of the two year average and result in Southampton being a top up Authority which was not anticipated.

Once the scheme is up and running, there will be a system of levies and safety nets to prevent what Ministers see as excessive gain or loss. All authorities will receive a safety net payment if their actual local share business rates income is 7.5% or more beneath the funding baseline. Levy rates will be set individually for authorities, determined by the ratio of their expected local share income to their baseline funding level. They will not exceed 50% and cannot be negative. As a top up Authority the levy rate for Southampton is zero and the safety net has been set at £44.7M for 2013/14.

Having determined our Business Rates Baseline (which is lower than expected), this then needs to be compared to the level of business rate income we forecast will be collected in 2013/14. Our latest provisional figures are set out below and these will be finalised and submitted to the CLG at the end of January:

| | £ |
|--------------------------------|----------------|
| Estimate of Amount Collectable | 101,089,850.00 |
| Amount to be paid to the CLG | 50,544,925.00 |
| Retained by SCC | 49,534,026.50 |

| | |
|---------------------------------------|--------------|
| Amount to be passed to Fire Authority | 1,010,898.50 |
| Levy Rate | 0.00 |
| Levy | 0.00 |
| Gain to SCC | 2,725,916.11 |

Estimation

The sum retained by SCC of £49.5M is an estimate of the level of business rate income that the Authority believes it will keep in 2013/14 based on a 48% share of the forecast estimated amount to be collected of £101.1M.

The forecast gain to the Authority based on this estimate compared to our initial funding assumption is £2.7M. This figure is the net additional forecast business rates to be retained over and above the Business Rates Baseline (£49.5M less £46.8M).

However, the total business rates income which is forecast to be collected is only an estimate, and although it builds in as many factors as possible, such as the impact of the closure of Fords and the outcome of both known and further appeals, the actual figures will need to be closely monitored.

Appeals

In arriving at the total estimate of business rate income, an assessment must be made of the level of likely reduction in business rate yield due to successful appeals. In the past this has not been an issue for Local Authorities, as the reduction in yield has been borne centrally by the Government.

Under the new system of locally retained business rates, SCC will now share 48% of the burden of any reduction in yield due to lost appeals. However, the position is compounded, as the rules mean that not only is SCC liable for 48% of the lost yield for new appeals from 2013/14 onwards, but also for 48% for all appeals lodged before 2013/14; even though the Government will have already collected in full the income to which those appeals relate.

There is no way of knowing precisely what level of income will be lost due to appeals, as clearly this can only be known once the Valuation Office rule on each individual appeal (there are currently 900 businesses in Southampton who have outstanding appeals to be determined by the Valuation Office). An estimate of the income to be 'lost' due to successful appeals has however been calculated on a formulaic basis in line with Valuation Office guidance, and the overall estimate of business rates to be collected (£101.1M) has already been netted down to reflect appeals.

If however the value of successful appeals exceeds this estimate, then the additional lost income will reduce the actual amount of business rate income to be retained by SCC, and all other things being equal, would impact on the Council's bottom line, as less business rates will be collected than forecast.

Business Rates – Transfer of Risk

It is recognised that the introduction of BRR whilst offering an incentive to Local Authorities to grow their economies and resulting business rate income, also transfers

risks as well as possible rewards. As set out above, there will be a system of levies and safety nets to prevent excessive gains or losses.

Upside – There is still an incentive to grow the business rates base, particularly as being a Top-Up Authority, our levy rate is set at zero. This means that the Authority would keep in full its 48% share of any growth above the Baseline Funding level.

Downside – Conversely, where there is a fall in the level of business rate income collected, the Authority can lose in full its 48% share of all reduced income, capped at a total reduction of 7.5% of the Business Rates Baseline. A fall in business rates income could be due to the impact of businesses closing with insufficient new business opening to offset the reduction in rateable value, or it could be due to a higher than anticipated reduction in income due to lost appeals.

The Safety Net level of BRR funding for Southampton is £44.7M for 2013/14, compared with the forecast level of business rate income included in the budget of £49.5M. The inherent risk in this new system is therefore that compared to the budgeted position, the Safety Net funding level means that protection would only kick in once business rate income has fallen by £4.8M from our estimated position.

Compared to the fairly static funding position in the current and previous years achieved through the Formula Grant system, the potential to lose income in year under the new BRR system is a significant new risk.

Summary

When this new element of additional business rates is added to the picture then the final position is as set out below:

| | 2013/14 Updated £000's | 2014/15 Updated £000's |
|--------------------------------|---------------------------------------|---------------------------------------|
| | (3,081.9) | 2,841.3 |
| Estimated Business Rate Income | (2,725.9) | (2,807.7) |
| | <u>(5,807.8)</u> | <u>33.6</u> |

IMPACT OF DRAFT SETTLEMENT ON THE COUNCIL'S BUDGET POSITION

The impact of the settlement is that our financial position is now better than anticipated in 2013/14 by £5.8M and broadly in line with predictions in 2014/15. For completeness it is worth noting that whilst no firm figures have been provided for 2015/16 the updated position is approximately £3.0M worse than we had anticipated.