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Subject: **Local Authority funding Changes**

1.0 Background

1.1 Local Authorities currently receive funding for their revenue flood and coastal erosion activities from the Department of Communities and Local Government (DCLG) supplemented by capital grants from the Environment Agency.

1.2 The Coalition Government has announced changes to the funding for Local Government such that it is not as dependent on central Government grant. This is achieved through enabling local authorities to retain a share of their business rates.

1.3 The Coalition Government has also reduced the restrictions on local government decision making by providing a general power of competence and removing ring fences on funding. In May 2010 there were around one hundred different funding streams that local authorities had to reconcile to and which restricted the ability to innovate.

In June 2010 the Secretary of State for DCLG announced that the ring fences would be removed, providing the flexibility at the local level to use all funding to address local priorities.

2.0 DCLG Funding

2.1 Currently local authorities bill and collect the national business rate from businesses in their area. The funding they collect is pooled centrally and redistributed by DCLG.

2.2 Local authorities are funded through Council Tax, locally raised charges e.g. car parking fees and funding from DCLG. The DCLG funding comprises sums made available by other Government departments e.g. Education, and funding from the pooled business rates. The amount of grant paid to a local authority depends on a variety of factors. Annually local authorities submit a funding needs assessment to DCLG who derive an Aggregate External Funding grant (revenue support grant) for the local authority.

2.3 Local Authorities have four needs indicators for flood and coastal erosion.

- Local Levy paid to the Environment Agency (Upper Tier and Unitary)
- Special Levy paid to Internal Drainage Boards (Lower Tier and Unitary
- Own Spend on Flooding (Lower Tier and Unitary)
- Own Spend on Coastal Erosion (Maritime Lower Tier and Unitary)

2.4 We have to date been able to use the needs assessment and the fact that previous expenditure forms a part of the needs submission to encourage local authorities to fund land drainage, flood and coastal erosion in their area.

2.5 In addition to the above grants the Department of Environment Food and Rural Affairs (Defra) is also funding, via DCLG, a special grant to Lead Local Flood Authorities known as an Area Based Grant to cover the costs of the leadership role. This grant generally is only allowed for one spending review period. Under the changes around 50% of the funding for the Lead Local Flood Authority role has been consolidated into the LLFA baseline and 50% will continue to be provided by way of Area Based Grant for this spending review period.

2.6 The Local Government Finance Bill in December 2011 set out that from 1 April 2013 local authorities will retain up to 50% of the business rates collected instead of handing over the sums collected and then seeking funding. The complex needs assessments will cease and the amount of funding made available by DCLG will reduce. The localisation of Business Rates was approved in the October 2012 Local Government Finance Act.

2.7 The consultation was extensive and contained significant technical content, concerns remain that some authorities, primarily urban areas, will see a leap in the funding available, whilst others, primarily rural will see a decrease. DCLG propose to avoid this problem by a set of tariffs and top-ups which will redistribute the business rates collected and not retained by an individual Local Authority.

2.8 One aim of the changes is to enable local authorities to adjust to the new regime and build their way to a balanced budget. They have introduced a phrase ‘disproportionate growth’ which when triggered would result in a levy being paid to DCLG, they in turn will use this levy to fund a safety net that will be used if a local authority has an unexpected significant reduction in business rates.

2.9 DCLG retains a discretionary power to make grants available. The total funding baselines for local authorities will be the 2012/13 year budget adjusted for the 10% reduction set in the Spending Review 2010. The baselines are initially fixed for 7 years and thereafter expected to be reviewed every 10 years. In the meantime they will be adjusted by RPI annually in line with the Business Rate system. A further complication is that Enterprise Zones business rates are excluded from a local authority baseline because they are retained by the enterprise zones for 25 years.

2.10 The changes are challenging for local authorities to implement, many of the indicators for local authority needs will change, for example using the 2011 census data. In addition Local Authorities will now bear the risks from Council Tax support which used to be provided by DCLG. Local Authorities have to consult on local schemes for support which need to be approved by 31 January 2013. The mechanism for this has included a recalculation of the council tax base to ensure that an allowance has been included for properties unlikely to be contributing to council tax.

2.11 Treasurers in Local Authorities will be concerned about the impact of the funding changes, the risks of fluctuations in income and the application of the new top-ups and tariffs. This means that they need to pay far more attention to their income forecasts when budgeting and given the general expectation of council tax freezes continuing may have to change budgets in year if income falls. A number of authorities are moving ahead with pooling of financial resources with neighbouring authorities to create a larger funding base able to withstand shocks. When they do this the top-ups and tariffs are re-calculated meaning the decisions around doing this are complex.

2.12 A number of other freedoms are introduced such as enabling local authorities to borrow against future increased income - known as tax increment funding, and to securitise income, this allows a local authority to seek a lump sum now to invest in exchange for future income.

3.0 Capital Grant Funding

3.1 The Environment Agency makes capital grant funding available to local authorities and internal drainage boards. This power, set out in Section 16 of the Floods and Water Management Act 2010, was inherited from Defra for whom we have administered funding since 2006.

3.2 The Coalition Government included capital grants in the de-ring fencing initiative which means that a local authority has the freedom to use grants received for any purpose and don't have to spend the money on the area for which they received grant. The only restriction is that they must spend capital grant on capital schemes. This means that Local Authority Finance Officers must be able to capitalise the asset created using the grant.

3.3 Because of the implications for FCERM, it being unlikely that we could afford to make lump sum payments to a local authority for say a £11 million scheme, we have secured the approval of DCLG to continue to provide grants in the way we have for the last six years. Local authorities and Internal Drainage Boards are able to claim for work done to date and forecast work three months into the future within a financial year (claims can be made up to 31 March in any year)

3.4 With the removal of ring fencing there is an issue around management of contingency. Previously we allocated the project cost plus contingency. We are no longer able to recover unspent contingency which would reduce the number of projects able to progress. We have agreed with DCLG that in order to maximise the programme we will not allocate contingency, but manage it at a program level.

3.5 We are also required to seek approval for any payments to local authorities. The changes have led to a reassessment of our capital funding with DCLG. We have managed to secure approval to continue to fund most of the elements in the Medium Term Plan. Some changes are required and we are currently looking to use Section 13(4) of the Floods and Water Management Act to provide funding to local authorities for the activities that we need them to do for us.

3.6 All funding to local authorities and internal drainage boards is covered by the new DCLG arrangements this extends to local levy funding made available under partnership funding arrangements to local authorities. It should be noted that we make this funding available through Section 16 of the Act as a grant.

4.0 Implications for Wales

4.1 There are no implications for Wales because the Wales Assembly Government has different processes and the Environment Agency does not make grant payments in Wales.

Phil Winrow
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