

TECHNICAL NOTE ON LOCAL GOVERNMENT FINANCE COVID-19 PACKAGE

On 2 July, the Secretary of State for Local Government announced a funding package for councils to help address the range of COVID-19 pressures they face. This package included:

- A further £500m of unringfenced funding to respond to spending pressures, adding to the £3.2 billion of unringfenced funding previously provided – the government has now announced the allocation of this additional funding
- A new scheme to reimburse councils for lost income from sales, fees, and charges
- Changes so that local authorities spread their tax deficits over three years rather than the usual one

This technical note provides additional details for finance and other professionals in the sector, on how these components will operate.

Allocations of £500m funding

Summary

- Local Government Secretary Robert Jenrick has today (Thursday 16 July) confirmed allocations for individual councils in England from the £500 million of additional support for coronavirus-related spending pressures announced on 2 July.

Additional points for Finance Directors

Design and scope of the scheme

- Our allocation methodology is analogous to the proposed methodology for the Foundation Formulas in the Review of Relative Needs and Resources.
- The data is drawn from the second and third round of financial monitoring of COVID-19 expenditure pressures.
- An allocation is made for upper tier services and for lower tier services, based on the pressures reported by councils in their monitoring data.
- The upper and lower tier totals are allocated between authorities using a statistical technique called regression analysis.
- This suggests that the most important factors in driving the costs of service delivery are population and deprivation. The allocation is therefore based on a weighted combination of these factors to give a COVID-19 Relative Needs Formula.
- Where a council is responsible for both sets of services, the amounts are summed together.
- An adjustment to allocations is made to take account of the varying cost of delivering services across the country – both labour costs and premises costs. This area cost adjustment also takes account of the extra costs of delivering services in sparser and denser areas.
- As there is no area cost adjustment data available for the Isles of Scilly, the department has top-sliced £18,014 from the £500m for the Isles of Scilly using its 2020/21 population share, before the COVID-19 Relative Needs Formula is used to determine allocations for other authorities.
- In order to provide targeted support to the small number of authorities with acute pressures arising from costs relating to Unaccompanied Asylum Seeking Children (UASC), we have agreed to top-slice £6m for this purpose. Further details will follow in due course.
- Further detail on the methodology is annexed to this note (Annex A and B).

Tax - Three year phasing of 2020-21 collection fund deficits

Summary

- Local tax income is collected by billing authorities and paid into local 'collection funds'
- Where there is a shortfall in tax receipts (compared to expected levels), this leads to a deficit on the collection fund
- Billing and major precepting authorities are usually required to meet their share of any deficit during the following financial year
- The government is proposing that repayments to meet collection fund deficits accrued in 2020-21 will instead be phased over a three-year period (2021-22 to 2023-24) to ease immediate pressures on budgets

Additional points for Finance Directors

Design and scope of the scheme

- The Government's intention is for the deficit phasing to apply to all authorities, set at a fixed period of three years
- The phased amount will be the entire collection fund deficit for 2020-21 as estimated on the 15 January 2021 for council tax and in the 2021-22 NNDR1 for business rates
- The scheme will be prescribed in secondary legislation. Subject to parliamentary time, MHCLG would expect the necessary regulations to be laid in the early autumn.
- MHCLG is minded to put in place a scheme where the deficit will be phased across the financial years 2021-22, 2022-23 and 2023-24.
- MHCLG will continue to work with CIPFA and local government on the detailed operation of the scheme – including the accounting, audit and reporting implications – with a view to providing guidance to councils later in the year
- Parish and town councils are already protected from the impact of collection fund deficits. Any deficit relating to their share of council tax receipts in 2020-21 will be the responsibility of billing authorities in the usual way.
- For council tax, billing authority and major precepting authority shares of the phased 2020-21 collection fund deficit will be fixed according to the relative size of their council tax requirements ('CTRs') for 2020-21.
- For business rates, billing authority and major precepting authority shares of the phased 2020-21 collection fund deficit will be fixed according to tier splits for 2020-21. The impact on authorities in pools will depend on the particular pooling agreement in place.
- MHCLG will maintain a watching brief in respect of potential collection fund deficits relating to 2021-22 or future years.

Administering data collection

- The NNDR1 forms returned to the Department in January 2021 will collect data as usual on the estimated collection fund deficit relating to business rates
- The Council Tax Requirement forms returned to the Department in March 2021 will additionally ask billing authorities to record the estimated collection fund deficit relating to council tax and its apportionment between the billing authority and its major preceptors

Governance and accountability

- Billing authorities will be responsible for estimating their collection fund deficit in January and for apportioning shares between major precepting authorities and themselves in the usual way
- Individual authorities will be responsible for taking into account phased deficit repayments when setting their budgets and council tax each year, as required by the legislation

Sales, fees and charges

Summary

- The new income loss scheme will involve a 5% deductible rate, whereby councils will absorb losses up to 5% of their planned sales, fees and charges income, with the government compensating them for 75p in every pound of relevant loss thereafter.
- By introducing a 5% deductible the government is accounting for an acceptable level of volatility, whilst shielding authorities from the worst losses.

Additional points for Finance Directors

Design and scope of the scheme

- The scheme compensates for income that local authorities generate independently which is defined as a sale, fees and charges – for example, car parking charges or receipts from cultural asset charges.
- The 5% deductible will be calculated using sales, fees and charges budgets for 2020/21 as this represents what authorities expected to collect from these income sources at the start of the year.
- To help guide authorities in ensuring claims are reasonable, and in line with government's intention, the department is setting out a set of principles which will be used to define relevant claims under the announced support scheme.
- The principles-based approach acknowledges that individual councils will be best placed to determine what losses they should be claiming for. A prescriptive approach of listing eligible fees and charges would not best align with the existing structure of the local government and the nature of this income type.

	Principle	Explanation
1	Transactional income from customer and client receipts (excluding rents and investment income) which is generated from the delivery of services which was budgeted for in 20/21	<ul style="list-style-type: none">• Transactional income relating to revenues that are charged in exchange for a service offer where demand might have reduced in COVID• Income collection must be directly linked to the delivery of local services• Income from traded services could be eligible where the losses meet the principles, however commercial revenues, including rental amounts are not considered relevant losses and will not be compensated for under this scheme
2	As a result of COVID-19, and consequent reductions in economic activity, these income sources have been unavoidably lost and won't be recovered in this financial year.	<ul style="list-style-type: none">• Reductions in economic activity because of lockdown and social distancing restrictions directly led to lost revenues or decisions which caused a loss of revenue• Unavoidable losses relate to factors outside of the authorities' control causing the loss to be incurred. Voluntary decisions made locally which result in loss (e.g. closure of services by choice) which are out of line with government guidance, should not be covered• Won't happen in future means that the income is truly irrecoverable with regards to the 20/21 budget that was set at the beginning of the year. Deferred income that could be recovered within this year should not be compensated for but if it cannot be recovered within this financial year it may be considered eligible.
3	Compensation should be based on net losses, where a local authority has been able to reduce expenditure, or has received over compensation, only the residual loss would be compensated for	<ul style="list-style-type: none">• Compensation should be provided to mitigate the net budget gap which income losses have created. Where it is possible to do so, authorities should have taken internal action to mitigate the impact of losses, e.g. save on costs (furlough).• If funding to compensate for losses has been received from elsewhere it should also be netted off

Administering data collection and making payments

- Local authorities will be sent a DELTA form at the relevant time which they should use to enter the totality of all relevant losses for the relevant period under consideration.
- Alongside this, data on budgeted income collection will also need to be submitted, as per original budgets for the full 20/21 year. Where income makes up part of a net service, the LA will be asked to provide income targets/budgets for the relevant service elements.
- Finally, a description of the type of income will also need to be provided. This is likely to align with existing service categorisations used by government.
- Evidence to support all data entries will be required and should be kept by the authority in case it is asked for by the department, or as part of the annual audit process (to demonstrate compliance with grant conditions).
- The exact design of the data collection form is being finalised by the department.

- The department will release more detailed guidance in due course to support local authorities in the claims that they will be able to make under the scheme.
- The department's preference is to run periodic data collections throughout the year, e.g. quarterly, to ensure a frequent reimbursement of losses is made. The first data collection and payments are expected to take place later this summer.
- The scheme will be in place for the 2020/21 financial year only.
- There is no obligation for an authority to submit a claim under the scheme.

Governance and accountability

- Individual local authorities will be responsible for making sure that the claims they make under the scheme meet the principles we have set out
- The S.151 officer will be responsible for self-certifying the accuracy and reasonableness of their claim against the principles and guidance provided.
- Payment of grant will also be conditional on the accuracy and reasonableness of the claims made. We expect local auditors to fulfil their existing function under the local accountability system.
- In addition, the department will check a proportion of the claims to gain extra assurance that authorities are submitting appropriate claims. This will take the form of evidence requests being asked for once claims are submitted.

ANNEX A – DETAILED METHODOLOGY OF COVID-19 RELATIVE NEEDS FORMULA

This Annex sets out the detailed methodology for allocating the £500m of additional funding announced by the Secretary of State for Communities and Local Government on 2 July.¹

The allocation of this further funding is calculated for each local authority² using a relative needs formula (RNF) as follows:

$$Allocation_{LA} = (Tier\ Split \times RNF_{LA}^{Lower\ Tier}) + ((1 - Tier\ Split) \times RNF_{LA}^{Upper\ Tier})$$

Where:

$$RNF_{LA}^{Lower\ Tier} = Pop_{LA}^{20/21} \times ACA_{LA}^{Lower\ Tier} \times (Per\ Capita\ Amount^{Lower\ Tier} + (Deprivation\ Weight^{Lower\ Tier} \times IMD_{LA}))$$

$$RNF_{LA}^{Upper\ Tier} = Pop_{LA}^{20/21} \times ACA_{LA}^{Upper\ Tier} \times (Per\ Capita\ Amount^{Upper\ Tier} + (Deprivation\ Weight^{Upper\ Tier} \times IMD_{LA}))$$

Note that Shire Counties do not receive a lower tier allocation and Shire Districts do not receive an upper tier allocation. London Boroughs, Metropolitan Districts and Unitary Authorities receive an allocation from both formulas.

Where:

<i>Tier Split</i>	is the England level ratio of Shire District to Shire County expenditure in April, May and June 2020 from the MHCLG R2 and R3 financial monitoring data. This is approximately 0.21. The unrounded value can be found in the table below.
$Pop_{LA}^{20/21}$	is the ONS population projection for 2020/21 for each local authority ³ .
$ACA_{LA}^{Lower\ Tier}$	is the latest Area Cost Adjustment (more detail below) designed for use in the lower tier Foundation Formula as part of the Review of Relative Needs and Resources.
$ACA_{LA}^{Upper\ Tier}$	is the latest Area Cost Adjustment designed for use in the upper tier Foundation Formula as part of the Review of Relative Needs and Resources.
<i>IMD</i>	is the 2019 IMD Average Score ⁴ .
<i>Per Capita Amount</i> ^{Lower Tier}	means for every resident, a local authority receives £3.35 of funding (before adjusting for their ACA and deprivation score). The unrounded value can be found in the table below.
<i>Per Capita Amount</i> ^{Upper Tier}	means for every resident, a local authority receives £4.42 of funding (before adjusting for their ACA and deprivation score). The unrounded value can be found in the table below.
<i>Deprivation Weight</i> ^{Lower Tier}	means for each IMD average score point, a local authority receives £0.25 of funding per resident (before adjusting for their ACA). For example, an authority with an IMD average score of 10 receives an additional £2.47 of funding for each resident, on top of the per capita amount. The unrounded value can be found in the table below.
<i>Deprivation Weight</i> ^{Upper Tier}	means for every resident and each IMD average score point, a local authority receives £0.20 of funding (before adjusting for their ACA). For example, an authority with an IMD average score of 10 receives an

¹ £500m of funding is available in total. £6m has been distributed separately for Unaccompanied Asylum-Seeking Children. The remaining £494m is distributed using the RNF – excluding the Isles of Scilly who have been allocated a top slice based on their share of the 2020/21 national population.

² Fire authorities and Greater London authority are not within scope of this tranche of funding. Isles of Scilly due to their specific circumstances have been allocated a top slice based on their share of the national population.

³ <https://www.ons.gov.uk/file?uri=%2fpeoplepopulationandcommunity%2fpopulationandmigration%2fpopulationprojections%2fdatasets%2flocalauthoritiesinenglandtable2%2f2018basedprincipal2019geographies/table24.xls>

⁴ <https://www.gov.uk/government/statistics/english-indices-of-deprivation-2019>

additional £2.02 of funding for each resident, on top of the per capita amount. The unrounded value can be found in the table below.

The Per Capita Amounts (and Deprivation Weights) are estimated by the following regressions⁵:

$$\frac{\text{Expenditure}_{LA}^{\text{Lower Tier}}}{\text{Pop}_{LA}^{20/21} \times \text{ACA}_{LA}^{\text{Lower Tier}}} = \alpha^{\text{Lower Tier}} + \beta^{\text{Lower Tier}} \text{IMD}_{LA}$$

$$\frac{\text{Expenditure}_{LA}^{\text{Upper Tier}}}{\text{Pop}_{LA}^{20/21} \times \text{ACA}_{LA}^{\text{Upper Tier}}} = \alpha^{\text{Upper Tier}} + \beta^{\text{Upper Tier}} \text{IMD}_{LA}$$

Where:

$\text{Expenditure}_{LA}^{\text{Lower Tier}}$ is local authority total expenditure pressure in April, May and June from MHCLG financial monitoring data. For Shire Districts, this is simply total expenditure. For London Boroughs, Metropolitan Districts and Unitary Authorities this is total expenditure multiplied by *Tier Split*.

$\text{Expenditure}_{LA}^{\text{Upper Tier}}$ is local authority total expenditure pressure in April, May and June from MHCLG financial monitoring data. For Shire Counties, this is simply total expenditure. For London Boroughs, Metropolitan Districts and Unitary Authorities this is total expenditure multiplied by 1 minus *Tier Split*.

All other variables are defined as above.

Worked examples

Single Tier Area

Consider a Local Authority with a population of 300,000, an IMD average score of 20 and an Area Cost Adjustment of 1.05 (assume the lower and upper tier ACA score are the same for simplicity).

$$\begin{aligned} \text{RNF}_{LA}^{\text{Lower Tier}} &= 300,000 \times 1.05 \times (\text{£}3.35 + (\text{£}0.25 \times 20)) = \text{£}2.6\text{m} \\ \text{RNF}_{LA}^{\text{Upper Tier}} &= 300,000 \times 1.05 \times (\text{£}4.42 + (\text{£}0.20 \times 20)) = \text{£}2.7\text{m} \\ \text{RNF}_{LA} &= (0.21 \times \text{£}2.6\text{m}) + ((1 - 0.21) \times \text{£}2.7\text{m}) = \text{£}2.6\text{m} \end{aligned}$$

Shire County

Consider a Shire County with a population of 500,000, an IMD average score of 15 and an Area Cost Adjustment of 0.95.

$$\begin{aligned} \text{RNF}_{LA}^{\text{Lower Tier}} &= 0 \\ \text{RNF}_{LA}^{\text{Upper Tier}} &= 500,000 \times 0.95 \times (\text{£}4.42 + (\text{£}0.20 \times 15)) = \text{£}3.5\text{m} \\ \text{RNF}_{LA} &= (0.21 \times 0) + ((1 - 0.21) \times \text{£}3.6\text{m}) = \text{£}2.8\text{m} \end{aligned}$$

Note: numbers in the allocations table may differ due to rounding.

Per Capita Amounts, Deprivation Weights and the Tier Split

Variable	Coefficient/Value
<i>Per Capita Amount</i> ^{Lower Tier}	3.346861996716
<i>Deprivation Weight</i> ^{Lower Tier}	0.2470740827349
<i>Per Capita Amount</i> ^{Upper Tier}	4.420628067115
<i>Deprivation Weight</i> ^{Upper Tier}	0.2017662838806
<i>Tier Split</i>	0.2133530463876

⁵ City of London is not included in the regressions as it is considered an outlier, however it receives an allocation using the regression outputs in the same way as other authorities.

ANNEX B - AREA COST ADJUSTMENT

As shown above, the allocation formula for the third tranche of COVID-19 funding includes an Area Cost Adjustment (ACA), to take account of the varying costs of delivering services across the country. The ACA is used both to deflate reported expenditure prior to the regression analysis used to calculate the RNF and to reflate final allocations. The ACA used in this formula is the updated and improved version being developed as part of the Review of Relative Needs and Resources (RRNR). Details of the methodology behind this ACA are outlined in the December 2018 RRNR consultation⁶ and a Ministry of Housing, Communities and Local Government Technical Working Group paper which is published on the Local Government Association website.⁷

This ACA continues to base the labour cost adjustment on local wage data (specifically the Annual Survey of Hours and Earnings from 2017 to 2019) which is used to measure the spatial variation in the going rate for similar workers, accounting for the effect of other factors known to affect wages.

Within this adjustment, journey time data is used to capture direct costs through staff time (Accessibility). This provides a good proxy measure of additional costs of operating in more sparse or more dense areas.

The adjustment includes a 'Dispersal' measure based on Department for Transport journey times from Output Areas (average 129 households) to the closest "hub town" (settlement of over 10,000 people). This helps capture costs in terms of employee time and paybill of longer journeys to reach households in order to provide services.

It also includes a 'Traversal' measure based on MHCLG-commissioned journey times from Lower Super Output Areas (LSOA) - defined as between 400 to 1,200 households - to the closest LSOA in an area totalling 10,000 people. This helps capture costs in terms of employee time and paybill of longer journeys between groups of households when delivering services such as waste collection.

The ACA aims to account for factors such as wages, commercial rents and other geographical features which affect the cost of delivering services. As with previous ACAs, this updated ACA continues to adjust for both labour costs - through a Labour Cost Adjustment (LCA) - and premises costs - through a Rates Cost Adjustment (RCA). It also includes several improvements to the accuracy and coverage, including:

- use of more granular levels of geography;
- a more detailed approach to assessing the going market rate for labour and removal of arbitrary lower limits in the labour cost adjustment;
- expanding the RCA to account for commercial rents as well as business rate costs including the use of a more robust data source and methodology; and
- inclusion of an adjustment to address issues of sparsity and density using sophisticated measurements of journey times that avoids 'cliff edges' between local authorities.

The ACA used for this funding does not include a 'remoteness adjustment' as decisions have not yet been taken on this element for the RRNR.

This ACA continues to include a rates cost adjustment with Valuation Office Agency data on local rateable values used to measure the spatial variation in the going rate for similar properties accounting for the effects of building characteristics known to affect valuation. This adjustment is applied to all premises costs. As rateable values for the majority of properties are based on market rents, the rates cost adjustment can be used to adjust for variation in rents paid and / or the income foregone by using space which could otherwise be rented at market rates, and other premises costs, in addition to the cost of business rates.

The different components of the ACA are weighted together into a single index for each relevant service. Weights are determined primarily using two data sources: Revenue Outturn (RO) and Subjective Analysis Return (SAR). RO statistics are based on the actual revenue spending of all local authorities in England using the final audited financial accounts where possible. SAR is completed by a sample of authorities in England and gives more detailed breakdowns of spending within services. Since weights are calculated using aggregated data at the service level, the final ACAs for individual authorities are not dependent directly on their RO or SAR return. Once the weights are determined, the indices are combined to form ACAs. Note that the weights are specific to each service, whilst the indices are specific to each local authority. The last full update of the ACA was undertaken in December 2019.

The final ACA for local authority 'i' and service area 'j' is calculated as follows:

⁶ <https://www.gov.uk/government/consultations/review-of-local-authorities-relative-needs-and-resources>

⁷ <https://www.local.gov.uk/sites/default/files/documents/business%20rates%20hub%20-%20Needs%20and%20redistribution%20working%20group%2025%20June%202019%20-%20Area%20Cost%20Adjustment.pdf>

$$ACA_{i,j} = [(Accessibility_i \times Accessibility\ Weight_j) + (1 - Accessibility\ Weight_j) \times LCA_i] \times LCA\ Weight_j + RCA_i \times RCA\ Weight_j + Unadjusted\ Weight_j$$

Where:

$$Accessibility_i = 0.5 \times (Dispersal_i + Traversal_i)$$

Weights

Formula	LCA	RCA	Accessibility	Unadjusted
Lower Tier Foundation Formula	55%	7%	6% (of the LCA)	38%
Upper Tier Foundation Formula	50%	8%	3% (of the LCA)	42%

The overall results for the ACA for each authority are included in the accompanying allocations spreadsheet.