



Office of the
Deputy Prime Minister

Creating sustainable communities

Local Government Finance

Amending Reports

Local Government Finance Reports 2003/04 and 2004/05

A Consultation Paper

May 2004
Office of the Deputy Prime Minister

Introduction

1. This consultation covers local authorities in England that receive grant via the Formula Spending Share (FSS) grant distribution system.
2. This paper sets out options for the principles to be used in amending the 2003/04 Local Government Finance Report, and also considers options for amending the 2004/05 Local Government Finance Report.

Background

3. Ministers have already announced that there will be an Amending Report for 2003/04 following revisions that have been made to the mid-2001 population data as used in the 2003/04 local government finance settlement.
4. The Office for National Statistics (ONS) are continuing to do further research into the population data estimates.
5. In addition to the Manchester and Westminster matching project, studies relating to population estimates for nine local authorities were announced in November 2003 - Wandsworth and Middlesbrough as priorities, together with Bradford, Derby, Kingston upon Hull, Shepway, Southend, Wirral and Bristol. These studies have recently been extended to include a review of evidence for all local authorities and ONS intend to announce the results of these studies at the same time as they publish the mid-2003 population estimates (i.e. August 2004). If the evidence suggests that a revision is required, they will, at the same time, revise both the mid-2001 and mid-2002 population estimates.
6. Further studies on other areas are planned as far ahead as 2007. We understand the ONS' intention is to use these further studies to inform their future work on population estimates.
7. We are only able to issue one Amending Report for each financial year, which must be made by the end of the financial year following the year of the report. For example, the Amending Report for 2003/04 must be made by 31 March 2005.
8. The 2003/04 Amending Report will revise the amount of grant an authority should have received in 2003/04. For authorities that should have received more grant than was allocated in 2003/04, additional payments will be made in 2005/06; for authorities that should have received less grant than was allocated in 2003/04, the amount owed will be netted off their 2005/06 RSG payments.

Content of the Consultation Paper

9. Consultation with local authorities on matters relating to grant distribution is usually accompanied by exemplifications showing the effects of the Government's proposals. However, the revised mid-2001 population estimates are not due to be published by ONS until late August 2004.
10. As we will not be able to redo regression analysis and exemplify distributional changes until we have the revised population estimates, it will not be possible to provide a satisfactory period of consultation on the basis of exemplified proposals before the provisional 2005/06 settlement is announced.
11. Exemplifications provided without including the revised population estimates would be misleading, since we could only include the existing partial revisions to the mid-2001 population estimates. It has therefore been decided, following discussion with local government representatives, that such misleading exemplifications should not be provided for the purposes of this consultation exercise.
12. **Therefore, this consultation paper simply sets out options for principles on amending the 2003/04 and 2004/05 settlements, and does not provide any exemplifications of distributional changes.**
13. As 2003/04 was the first year of the current formula freeze, it follows that any changes made to the 2003/04 formulae would automatically apply to 2004/05 and future settlements.

How to respond

14. The Government would like your views on which of the principles presented here should be used to amend the 2003/04 and 2004/05 Local Government Finance Reports. Specific questions and issues for comment are posed throughout the paper.
15. We welcome responses submitted electronically. Please send responses by e-mail to: lqf.amendingreport@odpm.gsi.gov.uk.
16. If you are not able to respond by e-mail, please send your response to:

Ms Arvind Thandi
Formula Grant Review Team
Office of the Deputy Prime Minister
Zone 5/F6
Eland House
Bressenden Place
London

17. Alternatively, they may be faxed to 020 7944 2963.
18. **Responses should reach us by 10 August 2004.**

Confidentiality

19. Ministers may make responses to this consultation public unless respondents request that their comments are treated as having been made in confidence. **If you wish your response to be treated in confidence please say so clearly. Corporate confidentiality clauses automatically attached to e-mails will not be taken into account.**

Questions

20. If you have any questions about this publication or require paper copies, please e-mail: lgf.amendingreport@odpm.gsi.gov.uk or telephone Ms Thandi on 020 7944 3328.

The Purpose and Scope of the Amending Reports

21. The basic rationale of an Amending Report is to correct for errors in the data used in the relevant settlement. We are therefore proposing to amend only the mid-year population data, together with those variables that use this data, the Community Fire Safety indicator for 2003/04¹, plus a small number of other data errors that were brought to our attention immediately following the 2003/04 and 2004/05 settlements. However, we have already received representations to take into account other changes; these are discussed further below.

Changes to the FSS formulae due to revised population data

22. There are potentially three options for changing the FSS formulae to take account of revised population data:
23. **Option 1: Replace the population data in the existing formula without changing the regressions.**

Option 1 would minimise the decisions that would have to be retaken regarding the 2003/04 settlement. The scaling factors within the floor

¹ The error in calculating the Community Fire Safety indicator for 2003/04 was found by ODPM whilst calculating the 2004/05 Community Fire Safety indicator.

and ceilings scheme will change, but it might still be necessary to change the level of the floors and ceilings since the changes to the data result in different floor/ceiling/scaling factor combinations. However, it would be inconsistent, and technically incorrect, not to update both the mid-2001 population-based Highway Maintenance regressions and the regressions that contain the revised ACA data.

24. **Option 2: Change the FSS formulae depending on regressions but leave the judgmental formulae unchanged.**

Option 2 would reflect the fact that some of the regression formulae used in the 2003/04 settlement were based on the mid-2001 population data (e.g. Highway Maintenance). Most of the formulae were based on the 2003/04 ACA data which is partially dependent on the mid-2001 population data - although the changes in the ACA data resulting from the revised mid-2001 population data being used are very small. The changes to the mid-2001 population data may change the relationship between the different explanatory variables. The best technical options if the revised mid-2001 population data is used may therefore differ from those using the original mid-2001 population data.

Most other services are also based on regressions although they are based on earlier mid-year population estimates. ONS have issued revisions to the mid-year population estimates going back to mid-1992, based on the 2001 Census (but do not yet reflect the Manchester revisions). Further revisions may be made to these figures following the reviews (see paragraphs 5 and 6). Therefore, it would be possible to amend the regressions for the other services currently based on earlier population data as well. However, this would be a fundamental change and we are not proposing to do this (we did not do this during the review of grant distribution). It should also be noted that we do not expect that the 1992-2000 population estimates available in September 2004 will be consistent with the new mid-2001 and mid-2002 population estimates.

25. **Option 3: Change the judgmental FSS formulae used for the 2003/04 settlement, as well as those depending on regressions.**

Option 3 reflects the fact that the EPCS formulae are judgement- rather than regression-based. Although we have the legal power to amend these formulae it would be very hard to justify doing this on technical grounds.

26. ODPM currently propose to adopt Option 2, ie to continue to use the regressions based on the 1991 Census-based mid-year population estimates for services other than highway maintenance.

Question 1: Which of these three options for changing the FSS formulae to take account of revised population estimates would you prefer to be implemented?

Changes to the FSS formulae due to other data errors

27. In addition to the changes resulting from the changes in population data (i.e. the population data indicators, the ACA and those indicators where population is used as the denominator) we also intend to amend other data errors which were notified to the Department immediately following the 2003/04 and 2004/05 settlements whilst making the 2003/04 and 2004/05 Amending Reports. These are:

For 2003/04

- Community Fire Safety Indicator - Incorrect ACORN categories were erroneously used in calculating this indicator. The amending report would correct this to use the right categories.
- Education SCA amounts for those 8 authorities who received SCA instead of BCA for Basic Needs funding (Barnsley, Bath & NE Somerset, Derbyshire, Greenwich, Haringey, Lambeth, N Somerset, Swindon), corrections to Transport SCA amounts for Durham.

For 2004/05

- Traffic Flow Indicators for Derby City - An incorrect total road length figure was used in the calculations of the 'annual average flow of all motor vehicles' (flowall.gla) and the 'annual average flow of HGVs, buses and coaches' (flowhgvbus.gla) indicators. The amending report would correct this calculation error for both indicators for Derby City.
- Corrections to transport SCE(R)/SCA amounts for Tameside and the Isles of Scilly.

Question 2: Do you have any comments on the proposed data corrections to be included in the Amending Reports?

Inclusion of the 2001 Census data in FSS formulae

28. Suggestions have been made that we could use the 2001 Census data in the Amending Reports. The Amending Reports would therefore reflect both the revised population estimates and the new 2001 Census data.
29. The 2001 Census data differ considerably from the 1991 Census data. This is of course to be expected since they reflect the considerable changes in the demographic make-up of the English population that have occurred in the last decade.
30. The Formula Spending Share formulae are based on the relationships that exist between the various indicator data. For the 2003/04 and 2004/05 Settlements these relationships were based on the 1991 Census data. Incorporating the 2001 Census data will change the Formula Spending Share formulae since the relationships between the data have changed. ODPM officials are working with the local authority association experts on options to update the formulae. This is not however a simple process.

31. Discussions started last year and one early result was that it would be technically incorrect to simply use the new Census data in the existing formulae.
32. As stated above, the purpose of the Amending Reports is to correct for errors in the data used for the 2003/04 and 2004/05 settlements. The use of the 1991 Census data in these settlements was not erroneous, as the 2001 Census data was simply not available at the time of the settlements.
33. Therefore, ODPM do not propose to use the 2001 Census data for the Amending Reports.

Question 3: Do you have any comments on the ODPM's proposal not to use the 2001 Census data for the Amending Reports?

Inclusion of the revised mid-2000 population data in the 2002/03 grants used as the base position for floors and ceilings

34. It has been suggested that the 2002/03 grants used in the base position for floors and ceilings in 2003/04 should be recalculated using the revised mid 2000 population data.
35. Floors and ceilings are based on the actual formula grant received by an authority in the preceding year, after adjusting for changes in function and funding. We do not recalculate for changes in data.
36. The purpose of the proposed 2003/04 Amending Report is to correct for revisions to the mid-2001 population data and we do not intend to revisit the population data used for 2002/03 in amending the 2003/04 settlement.

Question 4: Do you have any comments on the ODPM's proposal not to revisit the population data used for 2002/03 grants used in the base position for floors and ceilings in 2003/04?

Changes to the shares of Assumed National Council Tax (ANCT)

37. We set the shares of ANCT for each group of authorities so that the increase in grant broadly reflects the increase in FSS.
38. The change in FSS resulting from the revised mid-2001 and mid-2002 population may mean that the original shares of ANCT allocated to each class of authority do not ensure that the increase in grant broadly reflects the increase in FSS.
39. ODPM are therefore proposing to change the shares of ANCT if necessary.

Question 5: Do you have any comments on the ODPM's proposal to change shares of ANCT to better reflect the increase in FSS, if necessary?

Floors and ceilings

40. The FSS formulae changes, and possible ANCT changes, will change the floor and ceiling calculations. This will lead to a change in scaling factors, and Ministers may also wish to consider whether the levels of floors and ceilings should be revised.
41. In 2004/05, the floor and ceiling scheme included the guarantee that every education authority would receive a grant increase at least the size of the increase in their Schools FSS ("the passporting guarantee").
42. Population is not an important factor in the Education FSS formulae, and decisions on passporting for 2004/05 have already been made.
43. Therefore, ODPM propose that the passporting guarantee in the Amending Report continues to reflect the increase in Schools FSS at the time of the 2004/05 settlement.

Question 6: Do you have any comments on the ODPM's proposal to revisit the floors and ceilings arrangements to reflect the changes in distribution, if necessary?

Question 7: Do you have any comments on the ODPM's proposal that the passporting guarantee continues to reflect the increase in Schools FSS as announced in the 2004/05 settlement?

Will there also be an Amending Report for 2004/05?

44. The amount of Revenue Support Grant (RSG) an authority receives each year is currently subject to floors and ceilings. The floors and ceilings are based on the amount of grant received by the authority in the preceding year after adjusting for changes in function and funding.
45. For 2004/05, floors and ceilings are currently based on the amount of grant an authority received in 2003/04. Revisions to the mid-2001 population data will change the base position for the floors and ceiling calculations in the 2004/05 settlement. Any further revisions to the mid-2002 population data, and consequential formulae changes resulting from the mid-2001 population data changes, will also need to be reflected in the 2004/05 FSS formulae calculations.
46. It therefore follows that we should also revise the 2004/05 RSG allocations to take into account the distributional changes of the 2003/04 Amending Report.

Timing of the 2004/05 Amending Report

47. An Amending Report for 2004/5 could be issued with either the 2005/6 or 2006/7 settlements. However, if the 2004/05 Amending Report has not been agreed by Parliament by the time the 2005/06 settlement is approved by Parliament, it follows that we should then do an Amending Report for 2005/06. This is because the amount of formula grant an authority receives is dependent on the amount of formula grant it received in the previous year.

48. However, as we only have the legal powers to issue one Amending Report for 2004/05 we will be unable to take into account any changes to the mid-2002 population estimates made after the beginning of January 2005, or any other errors that may subsequently be discovered.
49. ONS may, following the studies described in paragraph 5, make revisions to the mid-2001 and mid-2002 population estimates. ONS will be aiming to make all the necessary Census-related revisions in August 2004. The prospect of further revisions cannot be ruled out at this stage. A continuing programme of work on population estimates is underway which could result in revisions in the future. As required under the National Statistics Code of Practice, ONS are developing proposals for a Revisions Policy on Population Estimates; key stakeholders will be consulted on these proposals.
50. We therefore have a choice: to wait for possible further revisions that may be announced in 2005, amend the 2004/05 settlement with the 2006/07 settlement, and then have to amend the 2005/06 settlement as well; or to amend the 2004/05 settlement at the time of the 2005/06 settlement, avoiding this further complication but running the risk of some corrections not being reflected. ODPM's current view is that the balance of advantage is with making the 2004/05 Amending Report at the same time as the 2005/06 settlement.

Question 8: Do you have any comments on the ODPM's proposal to issue the 2004/05 Amending Report at the time of the 2005/06 settlement?

The Floor and Ceiling Scheme in 2005/06

51. The financial effects of the Amending Reports will be felt by authorities in the financial year following the making of the Report. If the 2003/04 Amending Report, or the 2003/04 and 2004/05 Amending Reports, are made at the same time as the 2005/06 Settlement, then the financial effects on local authorities will come through in 2005/06. We could simply apply floors and ceiling damping without taking into account the financial effects of the Amending Reports (Option 1).
52. Alternatively, ODPM may wish to consider reflecting these financial effects in the floor and ceiling scheme for 2005/06, ensuring that authorities which may need to pay back money from 2003/04, and 2004/05 if made at the time of the 2005/06 settlement, nonetheless receive a reasonable increase in grant in 2005/06.
53. One way of doing this would be to ensure that the floors and ceilings operate on the amount of grant before floors and ceilings for 2005/06, minus the sum of the changes to the 2003/04 (and 2004/05) RSG amounts under the Amending Reports (Option 2). This would ensure that authorities that receive less grant under the Amending Reports would both be able to pay for the net changes and receive a reasonable increase in their 2005/06 grant. However, for authorities that receive more grant under the Amending Report, it is likely to mean that they are caught by the ceiling, or a higher scaling factor on their grant increase.

54. In order to mitigate the adverse effect on authorities gaining from the Amending Reports, a further option would be for the floors and ceilings to operate on the larger of either their 2005/06 grant before floors and ceilings, or the amount of grant before floors and ceilings for 2005/06 minus the sum of the changes to the 2003/04 and 2004/05 RSG amounts under the Amending Reports (Option 3). However, this option may lead to the ceiling having to be lower, or the scaling factor being higher, than might otherwise be the case.
55. The table below illustrates the effects of the three options on two simple authorities. For illustrative purposes a floor of 3% has been assumed for 2005/06 and a ceiling of 7%. For this example, no scaling factor has been applied to middle authorities. However, it should be noted that the scaling factor under option 3 is likely to be greater than that under option 2.

£ million unless otherwise specified

	Authority A	Authority B
Original 2003/04 formula grant	97	97
Amended 2003/04 formula grant	99	95
Change in 2003/04 formula grant	+2	-2
Original 2004/05 formula grant	98	102
Amended 2004/05 formula grant	100	100
Change in 2004/05 formula grant	+2	-2
Total change due to both Amending Reports	+4	-4
2005/06 formula grant before floors and ceilings	105	105
Change year-on-year	+5	+5
% change year-on-year	+5%	+5%
Option 1:		
2005/06 formula grant after floors and ceilings	105	105
<i>plus</i> Total change due to both Amending Reports	+4	-4
Net grant for 2005/06	109	101
Option 2:		
2005/06 formula grant before floors and ceilings	105	105
<i>minus</i> Total change due to both Amending Reports	+4	-4
Grant used for floor and ceiling calculations	101	109
% increase	1%	9%
% increase after floors and ceilings	3%	7%
2005/06 formula grant after floors and ceilings	103	107
<i>plus</i> Total change due to both Amending Reports	+4	-4
Net grant for 2005/06	107	103
Option 3:		
2005/06 formula grant before floors and ceilings	105	105
<i>minus</i> Total change due to both Amending Reports	+4	-4
Grant used for floor and ceiling calculations	101	109
% increase	5%	9%
% increase after floors and ceilings	5%	7%
2005/05 formula grant after floors and ceilings	105	107
<i>plus</i> Total change due to both Amending Reports	+4	-4
Net grant for 2005/06	109	103

Question 9: Do you consider that reductions in grant resultant from the Amending Reports should be taken into account in the 2005/06 floors and ceilings calculations?

Question 10: Which option for the calculation of floors and ceilings for 2005/06 would you prefer to be implemented?

Summary of Questions

Question 1: Which of the three options for changing the FSS formulae to take account of revised population estimates would you prefer to be implemented?

Question 2: Do you have any comments on the proposed data corrections to be included in the Amending Reports?

Question 3: Do you have any comments on the ODPM's proposal not to use the 2001 Census data for the Amending Reports?

Question 4: Do you have any comments on the ODPM's proposal not to revisit the population data used for 2002/03 grants used in the base position for floors and ceilings in 2003/04?

Question 5: Do you have any comments on the ODPM's proposal to change shares of ANCT to better reflect the increase in FSS, if necessary?

Question 6: Do you have any comments on the ODPM's proposal to revisit the floors and ceilings arrangements to reflect the , if necessary?

Question 7: Do you have any comments on the ODPM's proposal that the passporting guarantee continues to reflect the increase in Schools FSS as announced in the 2004/05 settlement?

Question 8: Do you have any comments on the ODPM's proposal to issue the 2004/05 Amending Report at the time of the 2005/06 settlement?

Question 9: Do you consider that reductions in grant resultant from the Amending Reports should be taken into account in the 2005/06 floors and ceilings?

Question 10: Which option for the calculation of floors and ceilings for 2005/06 would you prefer to be implemented?