

**Consultation on school
funding reform:**

**Proposals for a fairer
system**

Consultation on school funding reform: proposals for a fairer system

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Introduction and Summary

1. As we set out in our *Consultation on School Funding Reform: Rationale and Principles*, published on 13th April, the current system for funding schools has many problems. The money the Government gives to local authorities to fund schools relates not to the needs of pupils but to historical decisions about spending made by previous governments and local authorities. The system results in similar schools in different areas receiving very different levels of funding. It does not respond well to changing characteristics of pupils and therefore does not help schools support pupils' needs. The system is extremely difficult to understand. It is almost impossible to explain why a particular school receives the budget that it does.
2. This means that the current system for funding schools does not support our objective to raise the aspirations and attainment of all pupils. We have therefore not been surprised by the overwhelming support for reforming the system in response to our recent consultation. We want a system in which good schools that parents choose are more easily able to expand. A key prerequisite is being able to understand the funding that would be available. Schools require a system in which funding is transparent; where funding follows the pupil and where pupils with additional needs attract additional funding. Similar schools, serving pupils with similar needs, should be funded in broadly similar ways, no matter where they are.
3. Our first step to reforming the system has been the introduction of the Pupil Premium. The Pupil Premium provides additional funding for schools clearly and transparently, so that they can better support deprived pupils. We would like the rest of the school system to have the same clarity and transparency and propose to introduce a new fair formula which will provide funding to local authorities, schools and Academies on a fair and transparent basis. We will ensure the new system:
 - a) Supports the needs of pupils;
 - b) Is clear and transparent;
 - c) Enables schools and Academies, sponsors and Free School proposers to make informed decisions about their provision;
 - d) Enables schools and Academies to be funded on a broadly comparable basis.
4. We will also enable local circumstances to be taken into account in the setting of schools' and Academies' budgets. We are ensuring a role for local authorities and Schools Forums, including Academy representatives, in managing local pressures and priorities.
5. These reforms will bring substantial benefits. However they will require funding to be moved between schools and areas, and will take time to have effect as ensuring stability in school funding remains a key

objective. We will apply transitional arrangements from the outset to ensure that the reforms are introduced at an appropriate speed that is manageable for schools. These transitional arrangements will limit the year on year change to schools' budgets so that there is stability in budgets while the reforms are introduced.

6. We want to ensure there is adequate time for detailed consultation on the new system and time for Academies, schools and local authorities to plan for the changes. We will therefore continue with the current system for schools in 2012-13 and will consult in this document on the right time to introduce the new system. We intend to provide more detailed proposals on the new system following this consultation and then consult further through a "shadow settlement" in 2012-13 which will show potential allocations resulting from the reforms.
7. We will develop a formula that helps schools to meet the needs of pupils by ensuring that additional resource is targeted towards pupils who have additional needs. For instance, children from deprived backgrounds are less likely to reach their potential than other children, and schools therefore need additional funding to provide them with the necessary support to enable them to do so. The new national formula will include the main elements that are likely to require additional resource.
8. The new national formula will include:
 - a) A basic amount per pupil;
 - b) Additional per pupil funding for deprivation;
 - c) Additional funding to protect small schools;
 - d) An adjustment for areas with higher labour costs.
9. In addition, we are consulting on including additional funding for pupils who have English as an Additional Language (EAL) and sometimes need additional support to help them to achieve.
10. These factors will be used in the formula to determine the level of resource for each local authority. Local authorities and Schools Forums will then agree a formula to distribute funding locally between schools in order to meet local priorities and needs. This formula could also be used to calculate the budgets of Academies in the area. Academies will be represented on the Forum to ensure decisions take their needs into account. We will take steps to simplify the local formula so that whilst there remains local flexibility in order to deal with particular needs and priorities, there is also more consistency between areas.
11. Aside from the factors within it, there are two ways of calculating the formula:
 - a) A school level formula based on the schools within the area and the pupils within those schools;

- b) A local authority level formula based solely on the pupils within the area.
12. Under a), we would calculate a notional budget for every school using a national formula, and then give local authorities the total local budget for all schools in their area. This would enable schools to see the funding attributed to their school through the national formula.
 13. Under b), we would not calculate budgets for every school, but simply calculate a budget for the local area based on the pupils who are educated within the area.
 14. In both options it will be very clear how the budget of every local authority has been calculated and both options will also correct the historic disadvantages that some local authorities and schools have experienced.
 15. We are not proposing to introduce a national formula for individual schools with no local flexibility. We recognise that there are likely to be specific needs that need to be met which may not be possible to accommodate in any national formula.
 16. The consultation strongly supported some local flexibility in the system, but with that flexibility being limited in some way. This document sets out options on how to implement this. Our preferred option is to restrict the number and scale of additional local factors that can be used. This will ensure that all formulae are built on a comparable basis and can be understood easily by schools, Academies and others. We are also considering how we should improve the role of Schools Forums, so that they are more representative of all types of provision and that they have greater powers to challenge proposals if they think they are unfair.
 17. This document considers changing the way that Academies' budgets are calculated. We will maintain the practice that Academies are funded at the same level as other local maintained schools. We want to ensure that Academies' budgets are calculated more transparently.
 18. Under arrangements set out by the last Government, the Young People's Learning Agency¹ (YPLA) uses the information that local authorities provide to the Department about their budgets in order to calculate budgets for Academies. This process requires the YPLA to replicate the local formula and calculate the additional funding for central services (LACSEG – the Local Authority Central Spend Equivalent Grant). This system is extremely bureaucratic, prone to error and delivers budgets with a 17 month time lag.
 19. By simplifying local formulae, we will improve the transparency of school funding. This will also make the calculation of Academies' budgets by the Education Funding Agency (EFA) easier, or enable local authorities to calculate Academies' budgets for the EFA.

¹ The YPLA will be closed and replaced by the Education Funding Agency in April 2012.

20. When the first Free Schools open in September 2011, they will be funded according to a simple formula based on the average levels of funding for schools within each local authority. Whilst our long term aim is for all schools to be funded on the same methodology, this document considers how Free Schools, University Technical Colleges (UTCs) and Studio Schools should be funded in the interim.
21. Local authorities will continue to be responsible for funding high needs pupils (children with high needs SEN and those in Alternative Provision (AP)). We will provide local authorities with funding to carry out these functions, and over time seek to use a formula to distribute this funding.
22. Local authorities will also continue to be responsible for funding providers of early education and childcare for 3 and 4 year olds in the maintained, private, voluntary and independent sectors. They will continue to use a single funding formula to do this, although we are consulting on some proposals to simplify formulae, in line with schools. We are also consulting on whether, over time, we should move to a nationally determined formula to distribute this funding.
23. Therefore there will be three main blocks of funding for local authorities – Schools, High Needs Pupils and Early Years. There will also be a small fourth block for non-delegated items within the Schools Budget. We will allow local authorities to move funding between these Schools Budget blocks to ensure that they are able to meet local pressures, albeit with local checks through the Schools Forum such as the Central Expenditure Limit provides now. In addition there will continue to be funding provided through the DCLG Formula Grant, or its successor as part of the business rates retention scheme².
24. In order to ensure the continued additionality and transparency of the Pupil Premium, we will keep it separate from the formula for the duration of this Spending Review period. This will ensure that whatever other changes are made to the underlying funding system, schools with deprived pupils will still receive the Pupil Premium in full in addition.
25. We are also consulting on how to distribute the Pupil Premium from 2012-13. We intend both to increase the amount available per pupil and to increase the number of pupils that attract the premium. We are consulting on extending eligibility of the Pupil Premium to those pupils who have previously been eligible for Free School Meals (FSM) in the last 3 or 6 years.

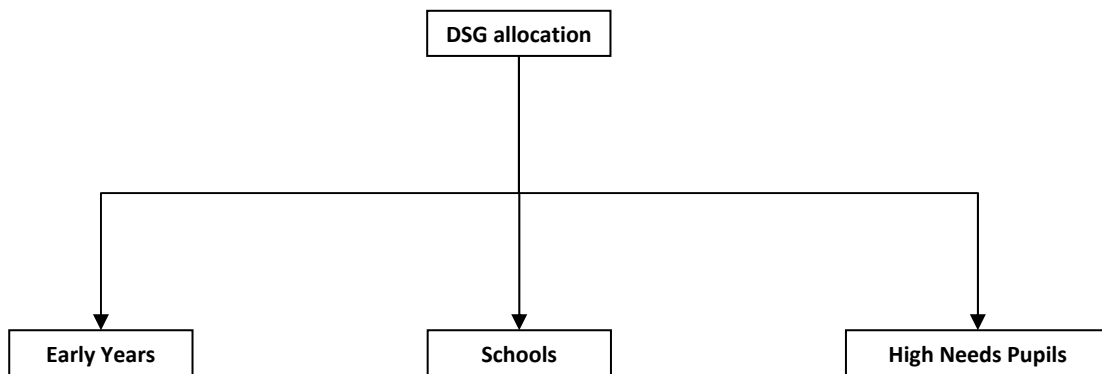
² Throughout this document, Formula Grant refers to DCLG's Formula Grant, or its successor as part of the business rates retention scheme

1. The national funding system

1.1. The Dedicated Schools Grant (DSG) currently provides funding to local authorities for schools, early years provision, high needs pupils (including SEN and Alternative Provision), and services retained centrally by the local authority. However there is currently no clarity about how each of these areas are funded at a national level, because we simply allocate a Guaranteed Unit of Funding (GUF) per pupil to each local authority to enable them to fund all these things.

1.2. In the future we want the funding system to be much more transparent and more clearly reflect need. We have reviewed the various functions funded by the DSG, and intend to bring clarity to it by allocating funding in three main blocks to local authorities. These blocks will cover:

- Schools
- High Needs Pupils
- Early Years



1.3. In addition there will be a small fourth block for services currently within the Schools Budget that are not suitable for delegation. These four blocks represent the totality of what is currently funded through the DSG. We will continue to ringfence the whole of the grant so that it is spent on the functions for which it is meant. However, the individual blocks will not be ringfenced. This will enable local authorities, in consultation with their Schools Forums, to move funding between the blocks, mirroring the current situation.

1.4. The only restrictions to the extent to which local authorities can move money between these functions are that i) money retained centrally by local authorities, including for high needs pupils, must not increase faster than the schools' budget without approval from the Schools Forum or the Secretary of State; and ii) the Minimum Funding Guarantee (MFG) limits how much money can be taken from the schools pot. We intend to keep these restrictions in place.

1.5. We will set out clearly what each block is meant to fund, by setting out the responsibilities of schools, Academies, and local authorities for pupils. Our proposal for this split is set out in Chapter 4. This split will also enable us to set the baseline for the calculation of each block, and to calculate the Local Authority Central Spend Equivalent Grant (LACSEG) – the resources which

Academies receive to carry out functions that local authorities perform for maintained schools – in the future.

1.6. We will set out the level of support for SEN that we assume nationally should be funded from schools’ delegated budgets, and the corresponding threshold for funding from the High Needs Pupils block. We will include funding for all services currently retained centrally by local authorities within the relevant blocks.

Summary of the functions covered by the main blocks

Schools	High Needs Pupils	Early Years
<ul style="list-style-type: none"> • Delegated budgets of schools for Reception to Year 11, including lower level SEN • Some current centrally retained services for school pupils 	<ul style="list-style-type: none"> • High Needs SEN including those in mainstream schools and Academies, and all special schools • Alternative Provision • SEN support services 	<ul style="list-style-type: none"> • Free entitlement to early education for 3 and 4 year olds • Current centrally retained services for early years

1.7. In addition, local authorities will continue to receive funding through DCLG’s Formula Grant (or its successor as part of the business rates retention scheme) for other education services. Again this is set out in Chapter 4. Funding for these services will be paid directly to Academies where relevant through LACSEG.

Overview of formulae

1.8. Over time we will move towards a formulaic approach to calculating each block. The starting point however will be the budgets of each local authority in 2012-13. This will reduce as far as possible the likelihood of turbulence in budgets. Further details are set out in Chapter 4.

1.9. There are two ways we are considering calculating the **schools block**:

- a) A formula based on the schools within the area and the pupils within those schools (“school-level”);
- b) A formula based solely on the pupils within the area (“local authority-level”).

1.10. Under a), we would calculate a notional budget for every school using a national formula, and then give local authorities the total local budget for all schools in their area. This would enable schools to see the funding attributed to their school through the national formula.

1.11. Under b), we would not calculate budgets for every school but simply calculate a budget for the local area based on the pupils being educated within the area.

1.12. Under either scenario, there will then be a local formula used to set the budgets of individual schools. The difference is that option a) produces a notional budget for every school, and b) does not.

Question 1: Would you prefer the formula to be based on

a) a notional budget for every school; or

b) the pupils in each local authority area?

1.13. If we introduce a formula for the **Early Years** block, it will be based on the children receiving the free entitlement to early education (currently for 3 and 4 year olds).

1.14. If we introduce a formula for the **High Needs Pupils** block, it will be based on the pupils resident within each local authority, reflecting the local authority's responsibility for securing provision for those pupils.

1.15. More detail is covered in the relevant chapters.

2. The schools block - system

2.1. This chapter sets out our proposals for how money will be passed to schools and Academies, and the role of local authorities and the Education Funding Agency (EFA).

2.2. We recognise that in times of economic uncertainty it is important for schools and local authorities to know that they have the flexibility they need in order to manage their budgets. We also recognise that moving every school on to a new formula will take a great deal of time and so there needs to be some flexibility to manage the change. We will put in place transitional arrangements which will set a limit on how much schools budgets can increase or decrease from one year to the next. It will therefore take time before schools attract their full allocation as indicated by the new formula.

2.3. The need to retain some local flexibility was voiced in the responses to the April consultation document where 38% of respondents thought there needed to be some local flexibility whilst 34% thought there needed to be a lot of local flexibility.

2.4. We have given considerable thought to how we can implement a system which enables local circumstances to be considered, yet secures national consistency so that all schools across the country are funded on a fair and comparable basis. Another important issue is the arrangements we put in place for Academies. It is a fundamental principle for Government that Academies are funded on a fair and equitable basis in relation to maintained schools and that any school wishing to convert to an Academy is neither put off nor incentivised by the financial consequences. The same principle should apply to Free Schools.

2.5. The rest of this chapter sets out the steps we propose to take in order to meet our objectives of a transparent and fair funding formula, which allows local circumstances to be considered and which enables all types of school to be treated equitably.

Local flexibility

2.6. Local authorities have a great deal of flexibility in deciding how to allocate money to individual schools. The full Schedule of the School Finance Regulations is attached at Annex A but, in broad terms, local authorities are currently allowed to allocate money to schools on the basis of the following criteria:

- Age weighted pupil units (a basic amount per pupil)
- Deprivation
- Special Educational Needs (SEN)
- Underperforming Ethnic Groups
- English as an Additional Language (EAL)
- Prior attainment
- Turnover of pupils
- Admissions arrangements
- Premises and grounds

- Rates, tax and insurance
- Teacher salaries
- Gifted and talented
- School size
- Special facilities
- Private Finance Initiative (PFI)

2.7. There are clearly some important factors listed here and some of them (such as schools on split-sites and the variations in Business Rates which are payable by schools) relate to very local, discrete circumstances which could not easily be taken into account at a national level.

2.8. However in order to achieve our aims of a funding system which is clear and comparable, we believe that there is scope to rationalise this list. This would provide greater consistency in funding across the country by limiting the degree to which local authorities can diverge from the national formula. It would also mean that, at a local level, it is easier to see how individual schools are funded.

2.9. We have discussed this issue with the School Funding Implementation Group³ and we are proposing to reduce the number of formula factors which local authorities can apply. We would allow local authorities with their Schools Forums to use the core components of the national formula (or similar) which are discussed in Chapter 3 of this document, plus a limited number of additional local factors. Therefore the local formula factors could cover:

- a) Basic entitlement per pupil (currently Age-Weighted Pupil Units)
- b) Funding for additional educational needs (e.g. deprivation, SEN, EAL)
- c) Rates
- d) Exceptional site factors (e.g. split site, PFI and rent)
- e) Lump sums for schools

Question 2: Do you agree that these are the right formula factors to retain at a local level?

Question 3: What other factors, if any, should be able to be used at local level or could any of these factors be removed?

2.10. In addition to this, we also propose limiting the amount of money which authorities can put through any of the additional localised formula factors. We would do this based on an expectation about how much funding should be linked to pupils and the core factors, and then allowing a maximum amount to be spent on exceptional factors. We will consult partners in more detail on this issue and consult further in due course.

2.11. In addition to the range of formula factors that exist, local authorities also have flexibility over how money is weighted. The main factors which are weighted are: primary and secondary school funding; and deprivation funding.

³ The School Funding Implementation Group is the Department for Education's advisory group on school funding. For more information see glossary entry.

2.12. At present, local authorities apply different weightings to primary and secondary pupils with secondary pupils often attracting significantly more money (although the difference has begun to lessen over recent years).

2.13. The national formula should contain fixed amounts for primary and secondary pupils, and deprivation. By fixing these amounts, we will have set the ratio of primary funding to secondary funding, and the amount for deprivation. We intend to do this in accordance with the current national average. However, if we were to require local authorities to use these ratios precisely as well, many schools would experience significant turbulence to their budgets. For instance, in a local authority that leaned funding more heavily towards primary schools than the national average, all those primary schools would lose funding relatively if we required the local authority to use the national average ratio.

2.14. In spite of this, we are keen to reach some level of national consistency over time and we are therefore proposing to allow authorities to apply their own primary / secondary funding ratios, as long as they are within a set range of the national average. We realise that this will cause some turbulence for local authorities and schools who are outside that range, which we will manage through transitional arrangements, but it would begin to create some national consistency over time. The national average ratio of funding between primary and secondary stages is 1.27. We propose setting the range of allowable ratios around this average to ensure that there is some convergence towards the national average.

Question 4: Do you think that setting a range of allowable primary / secondary ratios around the national average is the right approach to ensure that there is consistency across the country?

2.15. In the same way, there is currently funding in the existing Dedicated Schools Grant (DSG) for deprived pupils. However, the amount of money which is actually spent on deprived children varies across local authorities. We will therefore enable authorities to continue to apply their current deprivation weighting to avoid undue turbulence. The Pupil Premium will remain outside this and be distributed on top.

2.16. In order to ensure that local formulae are consistent and transparent, we are also proposing to require each local authority to complete a pro forma. The pro forma will set out which factors (taken from the list in paragraph 2.9 above) the authority has used to distribute money to schools and how much money they have channelled through each of the factors and how. We believe that this will be an efficient way of ensuring that local formulae are simple, readily understood and comparable.

Arrangements for Academies

2.17. Although Academies are independent from local authority control, the current allocations to Academies are based on local authorities' existing formulae – and therefore on local decisions. Academies are already required to be properly represented on Schools Forums which have a key role in these local decisions.

2.18. We have devised two options for the future of calculating Academies' budgets. Under both options below, the EFA would pay the money to Academies, and Academies' budgets would be based on the local authority formula. Under both options, academies and maintained schools will receive budgets based on the same data, removing the 17 month time lag which currently exists for Academies.

Option (i)

2.19. The most straight-forward option would be for local authorities to calculate budgets for all schools in the area and then tell the EFA how much Academies should be paid.

2.20. Our longer term aim is to give local authorities 2-3 year settlements so that they know well in advance how much money they have and can plan on that basis. This includes having the time to properly consult with the Schools Forum on a local formula and to publish draft budgets for all schools and Academies (up to 10 months in advance) so that they too have time to plan. This timetable would also allow a window for schools and Academies to raise any concerns with the local authority and / or the EFA.

Option (ii)

2.21. The alternative is that the EFA could calculate Academies' budgets using the pro-forma described in paragraph 2.16 above. The use of the pro-forma means that the EFA can readily see which local formula factors authorities have applied and their weights, and reflect those factors when calculating budgets for Academies. This approach would be more in line with the current process where Academies' budgets are calculated by the YPLA.

2.22. Our proposal to constrain and simplify local authorities' formulae, and for them to be recorded on a pro forma, means that the process for calculating Academies' budgets will become simpler and more transparent (because there will be fewer variables).

Question 5: Do you think we should implement option (i) or (ii) when calculating budgets for Academies?

Ensuring accountability and fairness

2.23. In order for a new formula to be truly fair, there needs to be some degree of scrutiny, challenge and accountability. Maintaining local flexibility is the right thing to do, but we want to ensure that decisions are taken fairly and that there are mechanisms in place to protect minority interests.

2.24. At present local authorities are required to consult with their Schools Forums on the construction of their local formulae and individual school allocations. However, this is purely a consultative duty and Schools Forums do not have the power to approve or disapprove local authority formulae. In practice though, many local authorities do take the advice of Schools Forums - often going with the majority vote. This could be detrimental to the interests of minorities (or those schools who are not represented specifically by a member of the Schools Forum).

2.25. The responses to our April consultation also raised concerns about the diversity of representation on Schools Forums and their political independence. The extent to which Academies participate on Schools Forums is variable, with some Academies playing an active part in Schools Forums and others being less involved with the local authority.

2.26. We think improvements need to be made to School Forums so that they are independent, truly representative of schools (including Academies) and that their independence is then given some force through decision making powers. We are considering:

- whether the main groups on the Forum – e.g. primary maintained, secondary maintained and Academies – should all separately have to approve a proposed formula
- whether the Forum should have more decision making powers – including the power to approve or disapprove funding formulae and allocations.

Question 6: Do you think these options would help to achieve greater representation and stronger accountability at a local level?

2.27. We also think that steps need to be taken to provide scrutiny and challenge at a national level and we believe that the EFA has the potential to fulfil this role. There are two main functions which the EFA could provide to safeguard the interests of schools and Academies. They are:

i) Checking compliance

2.28. This option would involve the EFA (on behalf of the Secretary of State) checking that the local formulae meet the required criteria. This would help provide national consistency. This is similar to the process for approving local authority allocations prior to the 1998 School Standards and Framework Act.

2.29. Approval of local authority formulae would be made more straightforward if we were to adopt a pro forma (as described in para 2.16 above) showing each local authority's simplified formula. Local authorities, once they have agreed their formula and consulted the Schools Forum on it, would send it to the EFA to check it complies with the criteria set out.

2.30. Such a process could help give confidence to all schools and Academies that they are being treated fairly.

ii) A review body

2.31. The EFA (again, on behalf of the Secretary of State) could also carry out a review function so that schools and Academies could raise issues or concerns with the EFA if they feel the decisions made by their local authority have been taken without due consultation or are unfair or biased. This would lead to particular scrutiny being given to that local authority formula as part of the checking compliance function. We would need to give detailed consideration to how this additional review function would be triggered. For example, we would need to consider whether the EFA would investigate

individual school concerns or only collective concerns. There is a risk such a system could turn into a bureaucratic process, and we would want to set the criteria for any reviews very tightly.

Question 7: Do you think we should implement option (i), (ii), both or neither?

2.32. Depending on how one or other of these proposals are taken forward, we may decide that they are best implemented using primary legislation. If so, we may introduce them informally in 2013-14 prior to giving them a statutory basis later.

Arrangements for Free Schools

2.33. A Free School's budget share is currently funded on the basis of the average school budget share for the authority they are located in. An average unit cost per pupil and an average unit cost per deprived pupil are established from looking at the budget shares of schools in that authority. Because of the complexity of the current funding system, this simple formula has been necessary so that potential Free Schools can clearly estimate the funding they might attract as they prepare their business case.

2.34. Under our new proposals, each local authority's formula will be clear and on a consistent basis. It would therefore be possible for existing Free Schools to be funded on that basis, just like Academies.

2.35. Our longer term aim would be for all schools to be funded according to the same methodology. However, we recognise that Free Schools are still in the early phase of development; that many will be increasing by whole cohorts each year and that the unusual circumstances of many would mean the local authority funding formula could produce odd effects. Therefore we think there is merit in keeping the current Free School formula for Free Schools for the remainder of this Spending Review period and reviewing again for the next SR period.

Question 8: If we introduce the new system in this spending review period, do you think that Free Schools should remain on the Free School methodology for 2013-14 and 2014-15 or move straight away to the overall funding system?

2.36. New University Technical Colleges and Studio Schools will be funded as Free Schools. We do not propose a separate funding mechanism for them. Their pre-16 and post-16 provision will be funded separately, as is the case for schools with a sixth form. Since Free Schools are independent like Academies they will also receive Local Authority Central Services Equivalent Grant (LACSEG).

2.37. The exception to this is where a Studio School is within another institution such as a maintained school or an Academy. In this case, the Studio School will need to be funded from within the institution's budget.

3. The schools block – formula content

3.1. This chapter sets out proposals for the components of a fair funding formula and seeks views on whether they are the right components and how each of the components should be allocated.

3.2. A formula set nationally cannot recognise every possible need in an individual school. Instead, it should include factors which reflect the main costs faced by schools. By enabling local authorities, with their Schools Forums, to continue to retain some degree of local flexibility (as described in Chapter 2), we can adopt a simple formula at national level.

The proposed content of a fair funding formula

3.3. This proposal can be applied to either a school based formula (which gives notional school level allocations but then aggregates the funding to give a total budget for local authorities) or a pupil based formula (which gives just a total budget for the local authority). The only difference would be the approach taken to protect small schools (this is described more fully in paragraphs 3.17 to 3.26 below).

3.4. We propose that the new formula could consist of:

- A basic per-pupil entitlement
- Additional funding for deprived pupils
- Protection for small schools (this would be applied through either a lump sum or a sparsity indicator depending on which type of formula we decide on)
- An Area Cost Adjustment (ACA)

3.5. We are also considering whether to include additional funding for pupils who have English as an Additional Language (EAL) and sometimes need additional support to help them to achieve.

3.6. Because there will be local flexibility over the final allocations to schools, we have not included specific school factors such as split-sites and Private Finance Initiative (PFI), for example. Applying these types of factors at a national level would make the formula make up and calculation considerably more complex. We believe that it is right that local authorities, in consultation with their Schools Forums, decide how to fund specific and exceptional circumstances.

Question 9: Are these the right factors to include in a fair funding formula at a national level?

3.7. Further proposals relating to how each of these factors might be measured and weighted are set out below.

A basic entitlement

3.8. This is the core per-pupil funding which will be allocated to every single pupil in a maintained school or Academy. The amount will vary depending on the age of the pupil (for example, secondary school pupils will receive more funding than primary) to reflect the additional costs associated with the different stages of the national curriculum.

3.9. In assessing the basic entitlement, we will make a judgment about how much funding to allocate to all the components of the formula at the same time and how to balance the weightings of the factors. This balanced assessment will inform the core per-pupil funding.

3.10. Whilst we are aware that there are many people who would prefer an Activity-Led Funding (ALF) approach, we believe that the balanced assessment methodology is more in keeping with our fundamental principles of school reform. The White Paper *The Importance of Teaching* set out our intentions that schools (whatever their status) should enjoy greater autonomy with their own funding, free from unnecessary bureaucracy. The mainstreaming of several grants at the beginning of this financial year reflected our commitment to give schools greater control over their budgets and enable them to spend their money where they know it will make the best impact on the education of their pupils.

3.11. An ALF approach would require us to make an assumption of the cost of all the activities which a school carries out and devise a per-pupil allocation on that basis. Presenting the basic funding in this way would prescribe how schools should be structured. This is at odds with the vision described above. It is also a more complex process which relies on detailed and accurate data being made available. We are keen not to introduce an approach which adds bureaucracy or prescription to schools.

Deprivation

3.12. The current funding system consists of several layers of funding approaches through the spend-plus methodology and the mainstreaming of many different grants. Local authorities that are more deprived do attract higher levels of funding. However, this system is very opaque and there is no clarity about how much funding is attached to deprived children. This was a key reason for the introduction of the Pupil Premium. The new system needs to reflect both the existing resources in the system, so that existing resources which support deprived pupils are maintained, as well as the additional resources being provided through the Pupil Premium. If we were to remove all of the existing deprivation weighting and rely solely on the Pupil Premium, local authorities and schools would see significant turbulence to their budgets. We therefore need to ensure the new funding system reflects the existing funding in the system for deprivation, and distributes this in a fair and transparent way. The Pupil Premium will then be in addition to this. Arrangements for the Pupil Premium are discussed in Chapter 8.

3.13. We intend to examine the current distribution of funding carefully to estimate the amount currently allocated on deprivation and use this to inform the subsequent decisions on the amount for deprivation in the main formula. We will also need to consider the basic entitlement as part of this: the more money we allocate to deprivation, the less money we will have available for

the basic per pupil entitlement. So we need to strike the right balance between allocating enough to target the most deprived pupils and, at the same time, ensuring that there is enough money left over for other pupils.

Deprivation indicator

3.14. We also need to identify a suitable deprivation indicator in order to target the deprivation funding. There are a range of measures we could use to do this and these are set out below in detail. However our longer term aim is to route all deprivation money through the Pupil Premium and so the Government's preference is to use a Free School Meals (FSM) indicator.

3.15. Chapter 8 sets out our intentions to use either an 'Ever 3' or 'Ever 6' FSM indicator to allocate the Pupil Premium. These indicators would pick up pupils who have been eligible for FSM in any of the last 3, or 6 years. Using FSM eligibility to distribute money is a readily understood and available process. Schools know how many FSM pupils they have at the beginning of each calendar year. If we were to implement a school-level formula, then it would make better sense to use an FSM indicator to target deprivation funding as it is linked to the actual number of deprived children in a particular school.

3.16. We realise however that FSM is sometimes under-reported and therefore does not provide us with a consistent national picture of deprivation. The decision to continue with local flexibility means that local authorities, with their Schools Forums, can consider whether other deprivation indicators (based on geographical area and household income) are a better solution for the pupils in their area.

3.17. The possible options are:

- Free School Meals (FSM) – This is the only deprivation indicator which uses pupil level data (rather than area level data). FSM eligibility is based on whether the child's parents are in receipt of certain non-work benefits, including Income Support, Job-Seeker's Allowance and Tax Credits.
- Ever FSM - Ever FSM covers a wider cohort as it includes pupils who have been registered as eligible for FSM at any point in the previous 3 or 6 years.
- Benefits data - This uses benefits data from HM Revenue and Customs to calculate an area based deprivation measure.
- Income Deprivation Affecting Children Index - Each Lower Super Output Area (which equates to around 1500 people) is given a score showing the percentage of children aged under 16 in deprived families (i.e. in receipt of certain benefits and with income below 60% of the median before housing costs).

Question 10: Do you agree that we should use Ever FSM to allocate deprivation funding in the national formula? Should this be Ever 3 or Ever 6?

3.18. We will also consider the impact of the introduction of Universal Credit and potential ways of using data from this for allocating deprivation funding in the future.

Small school protection

3.19. It is important that a fair funding formula continues to protect the viability of small schools that often face higher unit costs. These are often situated in rural areas where it is not appropriate to transport young children long distances. There is currently a presumption against closure of small rural schools⁴.

3.20. This section seeks views on the mechanism for applying protection for small schools. The mechanism we apply will depend on whether we implement a school-level funding formula or a local authority-level funding formula.

3.21. Regardless of which type of formula we implement, we do not intend to apply small school protection for secondary schools. There is no consistent evidence that secondary schools require dedicated small school protection as i) there is no real difference to the range of subjects offered at those secondary schools which could be defined as 'small', and ii) there does not appear to be a systemic method used by local authorities to support such schools. It is mainly home to school transport costs which are incurred at secondary level – and these are already funded from the general local authority Formula Grant.

3.22. The options for protecting small primary schools are:

- A fixed lump sum (for both a school-level or a local authority-level formula); or
- A sparsity measure (for a local authority level formula only)

3.23. A fixed lump sum to all primary schools would ensure that small schools receive a set level of funding, regardless of pupil numbers. Even though all primary schools would receive the same amount, that amount would represent a larger portion of the budget for a smaller school and therefore help them to tackle any diseconomies of scale.

3.24. Work carried out so far indicates that a lump sum of £95,000 would enable a small primary school to be financially viable. The £95,000 figure was reached by examining the total budget of each school (outside London) against the number of pupils in that school. The average amount left over after all the pupils had been accounted for, was around £95,000. This therefore gives us an implicit budget of a school without any pupils. The work behind the £95,000 amount is set out in further detail at Annex B, but we will do further analysis to inform the final decision on this factor.

⁴ This is set out in statutory guidance for decision makers (local authorities, the School Adjudicator, governing bodies and schools) under the Education and Inspections Act 2006.

3.25. Most local authorities have adopted a primary (Reception to Year 6) and secondary (Year 7 to Year 11) school organisation. However, a small number of local authorities have adopted a tertiary system, often known as 'middle schools'. The underlying need for small schools relates to the need to ensure young children do not have to travel long distances. Therefore, rather than extend the lump sum towards schools that cover secondary aged pupils, we could limit the lump sum of £95,000 to schools that do not have secondary school pupils i.e. a school would receive the lump sum if the highest year group was Year 6 or lower.

3.26. The formula underlying the current Dedicated Schools Grant (DSG) includes a weighting for population sparsity and we could continue with this approach instead of using a lump sum. Using sparsity addresses the underlying reason why there is a need in some areas for small primary schools because of the sparseness of the population. However, rather than use the National Census data from 2001 (as is the case at present) to assess the population in sparse areas, we would instead use pupil data from the annual school census. This will more accurately reflect the sparsity of the pupil population, presenting this information as the number of pupils per square kilometre.

3.27. At present, we use electoral wards to derive the degree of sparsity in a given area. However, electoral wards vary greatly in size and are also subject to regular boundary changes. If we continue to use a sparsity measure, we will use Middle Super Output Areas (MSOAs) to derive the sparsity measure instead of electoral wards. MSOAs provide greater consistency and greater comparability.

3.28. The current threshold for awarding sparsity funding means that money is spread fairly widely across almost two-thirds of local authorities and over 1 million pupils. If we narrowed that threshold, then it would mean that the funding would be focused on the most sparsely populated areas. For example, we could narrow the thresholds so that the number of pupils who attract sparsity funding reduced from 1 million to around 300,000 and around one-third of authorities. Annex C shows the potential impact on this change to individual local authorities using 2009 figures, although we would bring these thresholds up to date.

Question 11: If we have a school-level formula, do you agree that £95,000 is an appropriate amount for a primary school lump sum?

Question 12: Do you agree that the lump sum should be limited to schools with Year 6 as the highest year-group?

Question 13: If we have a local authority-level formula, should we use a primary school lump sum or the sparsity measure?

Question 14: If we have a sparsity measure, do you think we should narrow the sparsity threshold as described above?

Area Cost Adjustment (ACA)

3.29. Because wage costs and the cost of living vary greatly across the country, we have traditionally applied an ACA to our funding allocations. The old formula underlying the DSG uses the General Labour Market (GLM) approach, but this has resulted in generous allocations to Inner London and the M4 corridor because the index is influenced by the particularly high wages of some professions more prevalent in these areas. This uplift has resulted in Inner London authorities receiving an additional 26% funding compared to other areas⁵. In addition, further deviations are caused by the GLM areas not being aligned with teachers pay band areas. This means that there are currently 6 London authorities who are required to pay inner London weighting to teachers, whilst receiving outer London funding.

3.30. However, the salaries of teachers are not entirely market driven, since there is a national pay structure. For classroom teachers (pay scale points M1 to U3) the increase in salary between Inner London and the Rest of England and Wales pay bands varies between 15% and 25%. For school leaders (pay scale points L1 to L43) the percentage increase varies between 7% and 19%. As these pay band increases are lower than the GLM uplift for Inner London there is strong evidence for moving away from a pure GLM based area cost adjustment.

3.31. A Specific Cost approach would use the actual costs of recruiting and employing staff. However this approach requires us to have good sources of data of the direct and indirect costs related to both teachers and other staff costs. Whilst we have the data available for direct costs of teachers – through the teachers' pay bands – data on indirect and other staff costs is patchy and insufficient.

3.32. A third option is to use a combined approach. This approach would use a Specific Cost approach for the proportion of funding spent on teachers, and a GLM approach for the proportion spent on other staff. As well as providing a more accurate reflection of the variances in costs around the country, this approach would also enable us to remove the anomaly in the system whereby six London authorities are funded on a different basis than the pay scales they have to fund.

3.33. Further detail on the ACA options is contained in Annex D.

Question 15: Which option should we use to calculate the ACA: the current GLM approach or the combined approach?

English as an Additional Language and Underperforming Ethnic Groups

3.34. We have given careful consideration to the types of pupils who might need additional support to help them achieve, and who therefore require additional funding. The vast majority of underachieving pupils are from

⁵ The GLM adds an additional 26% of the **total** allocation for inner London although the increase would be higher if just considering the proportion of funding associated with pay (approximately 83% of the budget). For the 83% of the budget that is associated with pay, the GLM would add approximately 32% more funding.

deprived families and so extra support is provided to them through our deprivation funding and the Pupil Premium.

3.35. We have undertaken some detailed analysis to help us to identify what further factors of underachievement there are at Key Stages 2 and 4. The evidence is clear that pupils who only have EAL or who are only from Under Performing Ethnic Groups (UPEG) achieve almost as well as pupils who do not have any additional needs. At Key Stage 2, 75% of both EAL and UPEG pupils achieved Level 4 in English and Maths compared with 77% for those without any additional needs. At Key Stage 4, 64% of pupils who only have EAL achieve at least 5 A*-Cs including English and Maths compared with 59% for non-EAL, non-FSM pupils. Pupils from Under Performing Ethnic Groups however achieve slightly less, with only 56% achieving the same grades.

3.36. It is clear from the evidence that of the three factors it is deprived children who do least well. We are therefore confident that a focus on additional funding for economic deprivation is the key priority.

3.37. However, pupils who cannot initially speak English often require some additional support until they become familiar with the language. But once they can speak English, they go on to achieve well. The majority of children in this situation are in the primary phase.

3.38. Therefore we are considering the adoption of an EAL factor in the national formula. However, because extra support is generally only required for a few years, we propose limiting the funding so that it covers the first few years when a pupil enters the school system, for instance the first three or five years. We will consult partners further on this.

Question 16: Do you agree that we should use an EAL factor in the national formula?

Question 17: Do you agree that this should cover the first few years only? How many years would be appropriate?

Transitional Arrangements

3.39. We recognise that moving to a new funding formula may cause turbulence to the budgets of some schools. We will therefore put in place damping arrangements to minimise that turbulence and provide schools with assurance that they will not see fast and hard reductions to their budgets. However, if we were to introduce these reforms during the current spending period, those transitional arrangements would need to be cost-neutral in order to fit the overall resources for schools which is flat cash per pupil for the remainder of the period.

3.40. We have already applied a Minimum Funding Guarantee (MFG) for this financial year – meaning that no school will receive more than a 1.5% reduction in funding per pupil. If we were to maintain this for the rest of the period, then the maximum increase we could afford each year would stay at around 1%. Progress to a new formula would therefore be very slow.

3.41. The alternative would be to move faster by reducing the MFG each year so that more schools could move onto the new formula more quickly.

Question 18: Do you think we should:

(a) Continue with a maximum decrease of -1.5% per pupil each year and accept that this will mean very slow progress towards full system reform; or

(b) Continue with a -1.5% per pupil floor in 2013-14 but lower it thereafter so that we can make faster progress?

3.42. Chapter 9 consults further on when we should move to the new system.

4. Central services and defining responsibilities

4.1. To make the funding system more transparent, and to calculate Academy budgets more accurately, we are proposing to define clearly the responsibilities of maintained schools, Academies and local authorities. From this, it is then possible to construct a funding model which would reflect these by being clear what is included within each of the funding blocks. The blocks 1-4 below are the same as those described in chapter 1 and would be funded from the Dedicated Schools Grant (DSG). Block 5 is funded from the Department of Communities and Local Government (DCLG) formula grant. This chapter sets out in more detail the functions within the blocks.

4.2. The funding blocks would be:

1. Schools block
 - a. functions which must be done or paid for by all schools
 - b. functions where there is local discretion to retain them centrally (for maintained schools)
2. High Needs Pupils block
3. Early years block
4. Central services block
5. Formula grant
 - a. General local authority funding - Functions which must be done or paid for by the authority for all maintained schools and Academies
 - b. Local Authority Central Spend Equivalent Grant (LACSEG) funding block – functions which must be done or paid for by the authority for maintained schools but would be within Academy budgets – this would be split between local authorities and Academies (discussed in chapter 5)

4.3. A detailed list of the proposed functions within each block is shown at Annex E. This is a provisional split which we are seeking views on and will review further.

4.4. Most of the funding in the Schools Block is in block 1(a) and represents functions **which must be done or paid for by all maintained schools and Academies**. Funding for these functions would always be delegated. Much of the list includes what has been in delegated budgets from the start of local management, together with those services which were delegated around 1999-2000.

4.5. The functions also include some services where there is currently local discretion on whether or not they should be delegated, but where we feel it makes sense to wholly delegate these in a new system. These include primary and special school meals, where individual schools can already request delegation, together with relics of some historic grant additions to DSG. In the case of meals, a valued local authority service will still survive through buyback.

4.6. Block 1(b) includes functions **which could either be delegated or centrally retained for maintained schools (if there is local discretion) but**

would be within Academy budgets. These include services such as insurance, support services for minority ethnic pupils and behaviour support services. Under the current funding arrangements, this is broadly equivalent to what would be in the Schools Budget element of LACSEG. This block also includes functions currently within the Schools Budget where it makes sense to retain some flexibility as local authorities will still have responsibility for financial monitoring and intervention in relation to maintained schools (support for schools in financial difficulties, contingency). These budgets are not currently within LACSEG, however. We believe that Academies would need to receive a share of this to ensure comparability with maintained schools.

4.7. Under the options in this consultation, the starting point would be that all these services would be delegated to maintained schools and Academies. We could then allow the option for maintained schools to retain funding centrally for these services by local agreement through the Schools Forum or a vote of all schools if this is felt to offer better value for money or be more effective in terms of provision for vulnerable children.

Question 19: Do you agree that some of these services could be retained centrally if there is local agreement by maintained schools?

4.8. Block 1(a) would be completely within the school budget shares for maintained schools and Academies. Maintained schools would also receive delegated funding for services in block 1(b), if there is not a local decision through the Schools Forum or a vote of all schools to retain these centrally. Academies will automatically receive funding in 1(b) in their budget shares.

4.9. Block 2 is for **High Needs Pupils**. As the commissioner for provision for high needs pupils, the local authority is responsible for funding this. Much would in practice be managed directly by schools and Academies as part of their delegated budget. It is intended that Pupil Referral Units (PRUs) should also receive delegated budgets, subject to the passage of the Education Bill. There may also be a transfer of responsibility for alternative provision to schools in due course.

4.10. Block 3 relates to **Early Years**. Most of this would relate to the funding of the free entitlement and is already delegated to maintained schools and private, voluntary and independent (PVI) providers. It would also include specific centrally retained early years budgets within the DSG.

4.11. Block 4 represents the DSG funding for **central services** within the Schools Budget which cannot be delegated to schools. The block includes admissions, which is a statutory function of local authorities. We recognise that there are large variations in the extent to which DSG funding has been retained centrally with the agreement of Schools Forums and committed to services which would otherwise be outside the Schools Budget. This expenditure will also fall within the central services block.

4.12. Block 5(a) represents DCLG funding and **what must be done or paid for by the local authority for all maintained schools and Academies**. These are services which remain local authority responsibilities for Academies, or the pupils in them, as well as for maintained schools and their pupils. An example of this is home to school transport. The funding for these functions

would remain with the local authority within its Formula Grant, and would not be delegated to schools or passed to Academies.

4.13. Block 5(b) represents functions **which must be done by the local authority for maintained schools but would be within Academy budgets.** These are functions which the local authority would have to hold funding centrally for, and would not be delegated to maintained schools, but for Academies would transfer to the Academies themselves. They include responsibilities relating to financial accounts and audit, and school improvement. The functions are broadly equivalent to what should be in the local authority budget element of LACSEG.

Question 20: Do you agree that the split of functions between the blocks is correct? If not, what changes should be made?

Costing the blocks

4.14. We would then cost the blocks based on information from the most recent section 251 statements. In some cases, individual budget lines split between blocks and we will need to use information from local authorities on how this split should be calculated. The lines would then be mapped across to the four block DSG model (Schools, High Needs Pupils, Early Years and Central Services) and DCLG/LACSEG funding. This will provide the amount for each block to be distributed in the new system. Thus if reform was introduced in 2013-14, the 2012-13 section 251 statements would be used to cost the blocks and the totals would be constrained to fit the national total resources for schools available in 2013-14 (i.e. flat cash per pupil).

4.15. The same block format would be used to establish a baseline for each block for each local authority, the total of which would be constrained to match what they actually received through their DSG in that base year. The baseline is required for the purpose of applying transitional protection as the new formula is introduced.

4.16. Annex F shows how the current section 251 statement lines would split between the blocks, based on the provisional split set out in Annex E. So, for example, funding for schools in financial difficulty would be within the schools block.

5. Future arrangements for the Local Authority Central Spend Equivalent Grant (LACSEG)

5.1. LACSEG currently has elements from both the Schools Budget and local authority budget. We want to move away from the current complexity of the system and to treat these two elements differently in future.

5.2. The **Schools Budget** element of LACSEG and the variations in levels between local authorities arise because local authorities tend not to delegate all services which could be delegated, there are differential levels of delegation between local authorities, and because amounts allocated to the various services vary between local authorities. Where Schools Budget LACSEG is low, the delegated budget share will tend to be correspondingly higher because many services have already been delegated to maintained schools.

5.3. Under the options in the consultation, we would want to move away from having a Schools Budget LACSEG. Instead, the funding would initially be delegated to all schools and Academies as part of their locally or nationally determined school budget share. The main services affected by this are behaviour support services, insurance, primary school meals and support for ethnic minority achievement/underperforming groups. We also believe that Academies should receive a fair proportion of funding retained for contingencies and schools in financial difficulties, to ensure comparability with maintained schools.

5.4. With option (a) in paragraph 1.9 – the “school-level” formula – funding for the services where there is currently discretionary delegation would be included within the national total to be allocated. Schools and Academies would both, therefore, receive funding within their delegated budget share. To the extent that local authorities had local discretion to vary the formula, then this would also feed through to Academies’ budgets. The issues around comparability and protection for Academies would be the same as for the rest of the formula and not specific to these services. Depending on the extent of local discretion, de-delegation could still be an option for maintained schools, but if discretion is more constrained, then local authorities would need to offer a buyback service instead.

5.5. With option (b) – the “local authority-level” formula - we would require local authorities to calculate a formula allocation for all services which are currently centrally funded. Academies would then receive this allocation as part of their delegated budget share. If we allowed local discretion and maintained schools wanted these services to remain centrally funded, then they could collectively opt for de-delegation. This could be through either the Schools Forum or by a vote of all schools.

5.6. For the **local authority budget** element in block 5(b), we think there are significant benefits in distributing this funding to academies on a consistent formulaic basis, rather than through using local authority section 251 budget returns. The funding for these services for maintained schools within formula grant is allocated currently using a formula which, although predominantly based on pupil and population numbers, reflects factors such as deprivation or the Area Cost Adjustment (ACA). The way in which the

funding is allocated to Academies could, but would not have to, mirror the formula for distribution to local authorities. This is because a formula for distributing funding to local authorities might have factors, such as sparsity, which are less appropriate to use at the level of an individual Academy. For example, it could just have a simple per pupil basic element and a deprivation element.

5.7. We also need to consider how funding should flex between local authorities and Academies when schools convert to become Academies since responsibilities for providing central services move from local authorities to Academies. In the Local Government Finance Settlement for the period 2011-13, a transfer of funding has been made to cover these costs but we had to make deductions in local authority budgets on a pro-rata national basis as we are only able to make estimates about the growth in the number of Academies at a national level. This also provided certainty of funding to local authorities through the Local Government Finance Settlement over the period 2011-2013.

5.8. It would, however, be possible to take a different approach which more accurately relates to the actual numbers, location and growth of Academies, although this would not provide the same level of certainty in respect of local authority budgets as the current approach. It would potentially involve much more regular and variable transfers of funding from local authorities to reflect the growth in Academy numbers.

5.9. Some of the funding might also need to be retained by the Education Funding Agency (EFA) for Academy related functions which transfer to central government instead of the Academy – such as overall financial assurance.

Question 21: Do you think the funding for local authority LACSEG should be moved to a national formula basis rather than using individual LA section 251 returns?

Question 22: Do you think the distribution mechanism should be changed to one that more accurately reflects the actual pattern of where Academies are located?

6. Children and young people requiring high levels of support

6.1. In any new funding system, it is vital that we have adequate arrangements for funding those children and young people who require special, often costly, provision. These children and their parents deserve the best that we as a society can do for them in order to reach their full potential.

6.2. For the most part, this review has looked at children aged 2-15, and a separate review is taking place of the funding formula for 16-18. However, the Green Paper on Special Educational Needs and disability published on 9th March makes it clear that children and young people with SEN should be looked at on a consistent basis from 0-25, and should be funded accordingly. The high needs strand of this review therefore covers ages 0-25, since the responsibility of local authorities for commissioning and of the Young People's Learning Agency (YPLA) for funding provision for young people subject to a Learning Difficulty Assessment runs up to the age of 25.

6.3. Those children and young people who require high levels of support are a subset of children with SEN, post-school learners with learning difficulties and disabilities (LD/D) and those who require Alternative Provision (AP). While there is no precise definition of "high needs", we are concerned here with those whose educational provision costs more than about £10,000 a year in total. Pre-16, there are about 220,000 of them in England but total spend on them is around £5bn a year – on average some four to five times the cost of a mainstream pupil.

6.4. The Green Paper also states that local authorities will retain a key central role in dealing with SEN. As set out previously, we intend to fund local authorities through a High Needs Pupils block for pre-16 pupils. For post-16 learners, the Young People's Learning Agency is already working towards providing local authorities with a single budget for high needs learners with SEN or LD/D up to the age of 25 from 2013-14.

6.5. Two specific issues around SEN funding are highlighted in the Green Paper. One is that in future individual parents or young people might be given control of budgets, including those for special education provision. The second is the possible introduction of a national banded funding framework for children and young people with SEN or who are disabled, in order to improve the transparency of funding decisions while continuing to allow for local flexibility. The proposals in this chapter are designed to be compatible with these future developments. Where the chapter refers to the role of the commissioner or commissioning body, that role could be played by individuals holding a budget in relation to specific young people.

6.6. This chapter covers a range of issues connected with the funding of high needs pupils:

- a) Principles and context;
- b) Establishing a base level of funding for High Needs SEN;
- c) Funding by places or pupil numbers

- d) Funding Special and AP Academies and Free Schools
- e) Constructing the High Needs block for local authorities
- f) Issues specific to AP

Principles and context

Principles

6.7. The high level principles below have informed the proposals made in this chapter for funding children and young people with high needs. These are intended as general principles, not as a description of the current legal or administrative arrangements:

1. The funding provided should meet the impartially assessed needs of the child or young person for whom it is provided.
2. So far as practicable, the preferences of the parents or young person should be followed in placing the child or young person.
3. The interests of the taxpayer require that funding and resources should be used efficiently and to best effect.
4. The funding should not be seen as fixed, but subject to review, and may change as the child or young person's assessed needs change.
5. Where children or young people have social care needs or health needs, appropriate contributions should be made from the budgets for those services.
6. The commissioning body (usually the local authority) should meet the cost of the educational provision, in order that proper regard is given to financial considerations.
7. The commissioning body should have an open and transparent system for the allocation of high needs resources, which makes use of expert advice and is consistently applied.
8. The commissioning body should monitor the effectiveness of the provision, and that it achieves relevant and appropriate outcomes for the child or young person.
9. Because of the specialist nature and high cost of premises and staffing, funding systems need to provide some protection to institutions in which not all the places are filled. But this does not mean that indefinite protection should be given to unsuccessful institutions.
10. Pupil Premium and equivalent Post-16 disadvantage funding is additional to all other sums allocated.

Question 23: Is this the right set of principles for funding children and young people with high needs?

The Context

6.8. As with other parts of education, the high needs sector is changing to reflect the Government's aim of seeing greater diversity of provision, and the switch in the role of local authorities from providers to commissioners. The first Special Academies will open in September 2011, and by September 2012 we expect that Special Free Schools, AP Academies and AP Free Schools will also be opening. In 2011-12 and 2012-13 we will require interim arrangements for these schools.

6.9. In this context, principle 6 (that the commissioning body meets the cost of the provision) becomes especially important. We must avoid a system where there are perverse incentives for local authorities to place high needs pupils in one type of provider rather than another. But the current funding system does contain such incentives. Precise funding arrangements vary from one authority to another, but it will often be the case that, when it is necessary to make a new placement:

- a) the local authority will incur least additional cost by making the placement in a special school or Pupil Referral Unit maintained by itself, since it will already be funding places in these institutions and there may be no marginal cost to filling an empty place;
- b) next in order of additional cost will be a mainstream school place, since the school will often be expected to contribute part of the cost from its existing budget;
- c) the highest cost will be incurred through a placement in a special school maintained by another authority, or a non-maintained or independent institution, where the full cost will have to be met;
- d) high cost placements at post-16 Independent Specialist Providers can be a low cost option for local authorities as the YPLA rather than the local authority funds the provision. There has also been a practice of the YPLA funding social and health care costs for some placements as a legacy from the Learning and Skills Council responsibilities where local services are not able to fund that element of the overall placement cost. We will be exploring this with the relevant Departments to develop a consistent approach.

6.10. We make a number of proposals below to address these issues in the new funding system from 2013-14.

A Base Level of Funding for High Needs SEN

6.11. We want to remove perverse incentives for the commissioner (usually the local authority) described above. We propose to do this by enabling high need institutions to be given a basic sum per place or per pupil, with top up funding from the commissioner for individual pupils. This will also help

support transition to a diverse market where many providers are not maintained by the local authority.

6.12. All local authorities expect mainstream schools to provide for the needs of some pupils with SEN without specific additional funding. An indication of notional funding associated with SEN is included in each school's budget, though this does not imply any kind of ring-fencing. The level beyond which additional resources are made available varies from place to place. This indication of the level of funding for lower level SEN within mainstream funding will continue in the new system. The Green Paper says that local authorities will set out a local offer, including what is "normally available" in schools – what is normally available in schools will in effect be the local definition of lower level SEN.

6.13. In any future funding system there will be a distinction at national level between mainstream funding for schools and the High Needs Pupils block. For this purpose, it will be necessary for us to make a general assumption about the notional funding for low cost SEN within the mainstream funding blocks, and therefore the level beyond which the local authority would be expected to make additional funding available to schools and other providers. It would be open to local authorities to vary the way in which they operated the system locally, but there will have to be a national assumption for the purpose of making a division between the mainstream funding blocks and the High Needs Pupils block.

6.14. Work done by PricewaterhouseCoopers⁶ for the last funding review in 2009 arrived at a proposed dividing line for a pupil to be defined as high needs of about £6,200, in addition to the basic cost of a pupil without SEN (which is around £4,000). The YPLA uses a dividing line of £5,500 in its arrangements for additional learning support post-16. This suggests that a dividing line of around £6,000 could be appropriate – the round figure of £6,000 would be easy to understand.

6.15. This would mean that pupils whose needs cost less than £10,000 in total (the £6,000 additional needs and £4,000 basic) would not, for the purpose of the national formula, be deemed to be high need and the assumption would be that the funding would be found from the mainstream funding blocks. Locally this level could be flexed. It would then follow that mainstream schools should meet from their base budgets the first additional tranche of cost for any actual high needs pupils, which might be set at around £6,000: above that cost they would receive additional marginal funding from the local authority. This is how most local authority funding systems work now, though the figures vary.

6.16. This has implications for other settings where the pupil could be placed. If we leave it at that, it would cost a local authority £6,000 more to place a pupil in a special school or other setting than in a mainstream school, which would constitute a clear perverse incentive.

⁶ PWC research for DSG Review, 2009:
<http://webarchive.nationalarchives.gov.uk/20100603155746/http://www.teachernet.gov.uk/doc/bank/index.cfm?id=14194>

6.17. We believe this could be avoided by giving special schools and units base funding reflecting this additional £6,000. This would not depend on the needs of particular pupils, but would be given per pupil or per place (which of these is preferable is discussed below). The £6,000 that mainstream schools would be expected to contribute from their base budgets to any high needs pupil is on top of the basic mainstream funding schools would spend on any pupil, which we might expect to be approximately £4,000. Thus the base funding for specialist SEN settings would be about £10,000 per pupil or per place. We believe that all special schools are funded above this level per pupil or place now, though the same is not true of AP (issues specific to AP are considered later in the chapter).

6.18. This would mean that all institutions effectively had the base funding of £10,000. Funding above the base level would be determined on a basis of individual pupils' needs by the local authority as commissioner, and paid by the authority to the providing institution. It would mean decisions about placements would only relate to costs above the £10,000 base and would therefore result in a level playing field for providers. We think that this proposal has particular advantages for the funding of special Academies and Free Schools, which is discussed further on in the chapter.

Question 24: Would it be appropriate to provide a base level of funding per pupil or place to all specialist SEN and LD/D settings, with individualised top up above that?

Question 25: Is £10,000 an appropriate level for this funding?

Applying this approach post-16

6.19. As with low cost SEN and LD/D, we would want the same basic principles to apply pre and post 16 and across both schools and Further Education (FE) sector providers. There is currently an awkward divide post-16 according to whether a young person stays in a school or enters FE. We need to address this through the new funding approaches.

6.20. Post-16 currently has three budget pots, all with different funding rules and regulations, for learners with SEN and LD/D. We know that learners experience different levels of provision or support depending on where they live for the same level of additional learning need. The current pots are:

a) Post 16 SEN Block Grant – distributed to local authorities to cover expenditure on post-16 pupils with statements at maintained mainstream and special schools, non-maintained and independent special schools;

b) Additional Learning Support (ALS)– allocated to providers for direct support for learning to assist individual learners to reach their goals. ALS is split into two levels:

- lower level ALS is that below £5,500 (paid to school sixth forms and FE colleges). It is calculated via a formula for school sixth forms and via a mix of formula and historical trends for FE

providers. The future of these arrangements is being considered in the review of 16-19 funding;

- higher level ALS is that between £5,500 and £19,000. This is paid to FE providers based upon historical trends in volumes and funding per learner. The first £5,500 of the ALS amount for those requiring support of between £5,500 and £19,000 is included within this higher level ALS payment and therefore removed from the lower level ALS calculations for FE providers. Higher level support costs in school sixth forms are covered by the post-16 SEN Block Grant;

c) The LD/D placement budget pays for ALS costs above £19,000 in FE colleges and for the full cost of specialist placements in Independent Specialist Providers. All funding is calculated and allocated to providers on an individual learner basis.

6.21. As noted in paragraph 6.4 above, the YPLA is already working towards providing local authorities with a single budget for high needs learners with SEN or LD/D up to the age of 25 from 2013-14. This would give local authorities discretion and allow them to build AP (including non-mainstream options) which would give choice to young people and their parents, drawing in the voluntary sector and allowing students to live at home, participating in their community and work placements where they wish to do so. This needs to be balanced, however, with maintaining high quality specialist provision and residential provision. One way of tackling this might be for the Education Funding Agency (EFA) to develop three building blocks to pay for places for high needs learners:

a) Post-16 revised National Funding Formula to cover learners attracting a low level of additional learning support and no higher level support – paid by the EFA direct to non-maintained providers, and to maintained providers via local authorities. This element is being considered in the review of post-16 funding

b) providing a baseline budget of £10,000 for high needs students – paid directly to providers by the EFA (but via the local authority for schools maintained by them)

c) high level costs over £10,000 – transferred by the EFA to the local authority which in turn funds providers as a commissioner, or paid directly by the EFA to the provider on advice from the local authority as commissioner. The latter would provide a mechanism to minimise the administrative burden for providers of services to a number of local authorities.

Question 26: Is the idea of a base rate of funding helpful in the post-16 context?

Question 27: Should local authorities be directly responsible for funding high level costs over £10k for young people in post-16 provision in line with their commissioning responsibilities?

Question 28: Do the proposed funding arrangements create risks to any parts of the post-16 sector?

Funding by Places or Pupil Numbers

6.22. A further important issue is whether institutions providing for high needs children and young people should be funded on planned places or actual numbers of pupils. It is traditional to fund most such institutions on places, but we wish to conduct an open consultation about whether there should be more emphasis on actual pupil numbers.

Places

6.23. Funding by place is the traditional way of funding special schools and most AP, including Pupil Referral Units (PRUs). The argument is that provision of this cost and complexity cannot readily be switched on and off, so it is necessary to pay for the place and staffing and then look to fill the places so far as possible. Institutions are often expected to work to a tolerance above the planned number without extra funding, in return for getting funding when they are below the planned number.

6.24. This does mean, however, that the public purse is paying for empty places – the average level of occupancy of maintained special schools appears to be about 90%. It also means that local authorities have a financial incentive to place pupils in a vacant place in a special school maintained by them rather than in a place elsewhere that could be more suitable.

Pupil Numbers

6.25. This is the traditional way of funding mainstream provision. There is an argument for extending it into the special and AP areas to give schools more of an incentive to fill their places, and to equalise the financial consequences of different placements for local authorities. But the downside is a risk to provision where places nonetheless remain empty and a school gets into financial difficulty. It would be possible to allow in the unit cost for a small expected percentage of empty places, but this would not help schools with a high percentage of such places.

Options

6.26. Given the various benefits and risks of these choices, we should consider how changes might be made over time, or develop a compromise position to reduce risks:

- a) Given that special schools (other than non-maintained special schools and independents) and some AP providers are not used to the idea of being paid for the numbers they actually attract, it would be possible to continue funding places in the short term but declare an aim of moving to fund actual numbers over time. This could either be on the basis of moving over to actual numbers from a particular date for everyone; or on the basis that new providers would be funded for a certain period on places to give them a start, but then switch to actual numbers.

- b) Another possibility might be to fund on places, but reduce the number of funded places automatically if there is a high percentage of unfilled places for a certain period – this could be just one year, as for most post-16 provision now, or it could be a longer period such as two or three years.
- c) A further variant would be to fund the larger providers on pupil numbers, on the basis that they should be more able to cope with fluctuations, while leaving the smallest schools and units on a planned place basis.
- d) Another would be to give the base funding of about £10,000 discussed in the previous section on a per place basis, while giving additional funding only for actual pupils.

Question 29: Should institutions providing for high needs children and young people be funded on the basis of places or pupil numbers?

Question 30: Are any of options a-d desirable?

Funding Special and AP Academies and Free Schools

6.27. The first Special and AP Academies and Free Schools will be opening under the current education funding system which will continue up to April 2013. We will therefore need to make short term arrangements for that period, as well as looking for arrangements for the longer term when the numbers of Academies and Free Schools will be growing rapidly. The short term arrangements may need to differ between different categories of schools.

The Short Term: 2011-12 and 2012-13

6.28. For the first Special Academies opening in September 2011, we will be basing funding on the budget they already had from their local authority for the financial year 2011-12, plus the additional funding they require as Academies. We will expect the local authority where the Academy is located to continue to recoup money from other authorities who send pupils to the Academy, and the Department will recoup the whole budget from the authority where the Academy is located.

6.29. This arrangement was discussed with local authority interests in relation to 2011-12, but as we are not now proposing to change the general school funding system for 2012-13, we will seek to negotiate a one year extension where the Academy's funding is based on its local authority budget and the local authority continues to recoup money from other local authorities. However, we do not see this as a stable system, both because local authorities will not be willing to play this role indefinitely and because it locks the independent Academy closely into one local authority's system. As we look at more prospective Special Academy converters, we are also increasingly coming across variations in the way local authorities fund their maintained special schools, which are going to be very hard to handle in a school by school system of funding and recouping expenditure.

6.30. By 2012-13 the first Special Free Schools, AP Academies and AP Free Schools will open. Establishing a funding level and funding arrangements for

these will be more difficult. Special Free Schools may be new or existing providers which do not have an equivalent in the local authority where they are located, and are therefore not dealt with in its formula. On the AP side, local authority-maintained providers such as PRUs are not part of the delegated funding system as yet so local authorities will not have formulae for them. But if a provider converts to an Academy, it should be possible to establish how it has been funded by the local authority. For a new AP Free School provider, there may well be no obvious comparator. It is also already the case that some AP provision is commissioned directly by schools rather than by local authorities.

6.31. We propose to deal with this by getting a group of experts together to consider the costings in Free School proposals, and the short term method of funding these schools. But as with special Academies, we do not see this approach as creating a stable longer term position. There will be no previously maintaining local authority from whom we can recoup the full cost and whom we can ask to bill other local authorities for their pupils. We will have to work out temporary solutions for this in 2012-13, but for the longer term we believe we will need a new approach. Proposals for this are set out below.

The Longer Term: 2013-14 Onwards

6.32. For the longer term, we see essentially three routes by which funding could reach Special and AP Academies and Free Schools:

- a) entirely through the EFA, as with most funding for mainstream Academies and Free Schools;
- b) entirely direct from the commissioner of particular placements, which in most cases would be a local authority but for some AP could be a school (either through the existing school referral powers or once schools take responsibility for PRU-style provision). Mainstream Academies currently get funding for statemented pupils direct from local authorities;
- c) a combination of these two routes, with the EFA paying the basic sum of around £10,000 per place or pupil discussed in paragraphs 6.11-6.18 above and the commissioner paying top-ups for individual pupils. We think this is a particularly promising approach for funding high needs Academies and Free Schools, and on balance is the one that we favour.

a) Funding through the EFA

6.33. If all funding were to come to the school from the EFA, we would still need to find a way of aligning funding with responsibility, so that the commissioner does not get a free good for one type of provision. This is inevitably going to be complex for these institutions, where more than one local authority is involved (sometimes 30 or more for one institution). As noted above, local authorities are unlikely to be willing to collect this funding indefinitely on behalf of independent Academies and Free Schools. A centralised system of collection would therefore be needed.

6.34. One way of dealing with this might be to make the high needs block a notional sum in the first place, and for the EFA to act as a broker for making payments to providers. Instead of passing the cash budget to local authorities, the EFA would hold the budget in the first instance. The responsibility for commissioning would remain with the local authority and they would retain control over the whole notional budget. The EFA would then pass funding to the local authority or to non-maintained providers as appropriate. A substantial administrative system would be needed to account for each high needs pupil and make sure the right charge was made against the local authority's notional sum.

6.35. Another way of dealing with the issue would be to give all the cash to local authorities but for the EFA then to recover it for non-maintained providers through a recoupment system. This would also require administrative machinery in the EFA as well as local authorities.

b) Funding direct from the commissioner

6.36. As well as building on the direct relationship between provider and commissioner that should already exist for educational reasons, this option would align Special Academies and Free Schools with non-maintained and independent special schools, and would be consistent with the way in which statemented pupils are funded in mainstream Academies now. There would also be no need for a middleman to be involved in assessing or recouping funds for individual pupils.

6.37. On the other hand, it would be different from the general method of funding Academies and Free Schools direct from central Government. It would create an extra administrative burden for the Academies and Free Schools (which would be more substantial if the school has high turnover, as with AP or hospital schools). It would not provide financial certainty for the Academy or Free School, and in particular no funding for empty places by this route, which could create financial difficulties. But this would be mitigated if EFA paid a basic sum for each place, as discussed in the next section. Finally, it would be difficult to distinguish Academies and Free Schools in their operation from Non-maintained Special Schools/independents.

c) A combination of these approaches

6.38. On balance we think the best approach is the one in which the EFA would pay a basic sum of around £10,000, and the commissioner would pay top-ups for individual places. This combines:

- a financial relationship with the EFA, and the certainty of base funding for the school; with
- adding a financial dimension to the relationship the school already needs with the commissioner; ensuring that top-up funding is paid by the commissioner without the need for complex recoupment arrangements; and giving the school an incentive to secure pupils.

6.39. A further variant is that we might pass all funding through the EFA for a limited period while the school was establishing itself – say 2 or 3 years for a

Special or AP Free School; perhaps less for an Academy which is already well established as a school, with the EFA undertaking the necessary recouplement for that period; but then expect the school to deal direct with the commissioners for funding above the basic sum which the EFA would pay.

Question 31: For the longer term, should we fund Special and AP Academies and Free Schools:

- a) **with all funding coming direct from the commissioner?**
- b) **with all funding coming through the EFA and recouped from the commissioner?**
- c) **through a combination of basic funding from the EFA and top-up funding for individual pupils direct from the commissioner?**

Question 32: If we go for the combination funding approach, should we pass all funding through the EFA for a limited period while the school is establishing itself before moving to this approach?

Constructing the High Needs Block for local authorities

6.40. As set out in chapter 1, we will allocate a High Needs Pupils block for local authorities. We need to decide how to construct it, in terms of the quantum and formula for its distribution.

6.41. The previous funding formula which was introduced in 2003 included a high needs block. The formula for it was based on resident child population (because responsibility lies with the home authority), income support to reflect deprivation, and low birth weight. As with the whole of the old formula, this block was indicative and did not determine what local authorities spent on high needs pupils.

6.42. Since 2003 the amount spent on high needs pupils has grown rapidly compared with other education expenditure and the new block will be considerably bigger – about £1bn more than in 2003. In calculating the size of the block we will need to start from what is actually being spent, as set out in chapter 4.

Building the formula

6.43. In 2009, PricewaterhouseCoopers carried out research for the Department on the costs of high needs pupils in mainstream schools, and the links between high needs pupils and proxy formula factors. The main finding of this work was that the link between high needs pupils and deprivation, which had strongly influenced the 2003 formula, no longer appears to be valid. The incidence of high needs pupils appeared to be much more random than we had thought. The research also suggested that 66% of pupils with Statements of SEN and 7% of pupils recorded as School Action Plus had high needs although this may not be representative for every local authority because of varying statementing and recording practices.

6.44. Using the above estimate for the incidence of high needs SEN pupils by local authority, the following proxy indicators have been explored to determine their suitability for use in a new funding formula: rate of Disability Living Allowance (DLA) claimants aged under 16, rate of pupils with English as an additional language (EAL), health and disability domain of the child wellbeing Index, local authority population of 3-15 year olds and deprivation (rate of FSM pupils and local authority residency mean IDACI score). To establish which of these proxy indicators most accurately reflect the location of high needs pupils, we have compared the local authority level proxy indicators with local authorities' 2010-11 spend on high needs pupils⁷.

6.45. The analysis suggests that the rate of pupils with EAL and the health and disability domain of the child wellbeing Index do not sufficiently explain the estimated incidence of high needs, but that the rate of DLA claimants aged under 16 and the population size of 3-15 year olds offer scope for producing a funding formula. The inclusion of a small deprivation factor is also a possibility; alternative incidence rates of high needs pupils using very low attainment rates were considered which lead to the inclusion of a deprivation factor. There is also some reason to think that deprived groups are less likely to secure DLA for their children.

6.46. Those pupils in Pupil Referral Units (PRUs) also have high needs albeit of a potentially very different kind to high needs SEN pupils. Analysis suggests that the incidence of pupils in PRUs is mostly predicted by the youth population size and deprivation.

6.47. In conclusion we now believe that the funding formula for the high needs block should contain a much smaller deprivation element, which would be more heavily linked to AP rather than to SEN. A formula most closely linked to the apparent numbers of high needs pupils with SEN in local authorities would primarily contain two factors: numbers of resident young people in the relevant age group, and the rate of resident young people in receipt of the DLA. Once 2011-12 data is available, the analysis will be revisited which may result in alternative proxies being appropriate.

Question 33: Given there is no absolute method of determining which pupils have high needs, and given local variation in policy and recording, is this approach to determining proxy variables acceptable?

Question 34: Do you agree that deprivation is linked more to AP rather than the wider SEN needs?

6.48. However, we know that any formula will fail to reflect closely the spend of individual local authorities on high needs pupils, partly because the incidence of such pupils appears to be largely random and will therefore vary from place to place; partly because the families of pupils with SEN often move to places where they think the provision is good; partly because of the cost of the provision available locally; and partly because local authorities' own decisions and judgements on how much funding pupils require vary a great deal.

⁷ Budgeting on high needs pupils was defined for this purpose as funding for maintained and other Special Schools and Individually Assigned Resources in mainstream settings.

6.49. Consequently, as with the schools block, we will need substantial damping arrangements in place as we move to the new formula and thus the actual allocations local authorities receive after damping will be closely based on what each local authority has been spending. Anything else would create instability in the system. Movement towards a new formula will therefore have to be slow.

Question 35: Do you agree that in the short term we should base allocations to local authorities for the high needs block largely on historic spend?

Post-16

6.50. The proposal above relates to pre-16 funding, but we need also to consider funding for high needs pupils and students aged 16-25. In principle this funding should also be going to local authorities, who have the statutory responsibility to secure provision for these young people; and there is clear advantage, and consistency with the Green Paper, in giving local authorities flexibility over funding for high needs children and young people from 0-25. However, some issues are emerging with the plans that the YPLA is working on to pull all high needs funding for 16-25s together and pass it to local authorities. On the one hand, some local authorities may have concerns because they think the funding for the formula will be inadequate and they will be forced to pull in funds from elsewhere. On the other hand, some providers are concerned that local authorities may cease to make the current level of placements with them because of the cost compared with more local provision. These sensitivities need to be worked through, and while funding should clearly in principle be brought together over time, there may be a particular need for post-16 transitional arrangements which may last for some years.

Question 36: Do you agree that post-16 funding should also become part of the local authority's high needs block over time, but that there might be a particular need for transitional arrangements?

Question 37: What data should ideally underpin the funding allocations both initially and for a potential high needs block arrangement?

Issues Specific to AP

6.51. The amount of funding going into Alternative Provision (AP) is much smaller in size than high needs SEN, but has traditionally been funded alongside it as high needs provision. It currently applies to pre-16 children only, though the concept is likely to become more relevant post-16 with Raising the Participation Age. The nature of AP is very variable – while much of it comprises PRUs and other provision for pupils excluded from mainstream schools, it also includes longer term provision for pupils who cannot go to school for any reason. For this reason, the cost is also highly variable – though according to local authority returns of spend and numbers it is on average £15,000 or more, it can include provision such as placements in FE colleges which are much cheaper.

6.52. The law intends for AP to be short term provision for children with the intention that they will be reintegrated into mainstream schooling as soon as

possible. However, it is believed that increasing numbers of children have been placed in AP for long periods in recent years. There is therefore an issue of avoiding incentives (including financial incentives) to keep such children in AP for the longer term.

6.53. The short term character of the provision can also lead to rapidly varying numbers, making the funding of such provision on actual pupil numbers rather than places more problematic than for special schools.

6.54. A further issue with AP is the forthcoming trial of the approach of giving schools continuing financial responsibility for pupils whom they exclude. This will be the subject of pilot projects over the next three years, and could then be made universal. This approach would create the need for a financial relationship – direct or indirect – between the excluding school and the PRU or other institution that received the pupil (we understand that some local authorities have already been experimenting with this). This could take the form either of direct payments from the excluding school, or of an intermediate arrangement where the local authority (or in the case of Academies, the EFA) reduced the school's budget and passed the money on.

6.55. Giving AP institutions a base budget of around £10,000 per pupil could be more problematic than for SEN because:

- a) We do not think all AP costs this much (but have limited information on the costs involved in the various types of settings);
- b) It could cut across the financial responsibility of mainstream schools and local authorities for these pupils.

6.56. Despite these issues, we think that it is probably appropriate to continue to treat AP alongside SEN as an element of high needs provision for funding purposes. There will be many differences of detail which will need to be worked through.

Question 39: Should AP continue to be treated alongside high needs SEN for funding purposes? What differences between them need to be taken into account?

7. Early Years

7.1. This section deals with funding of providers delivering the universal free entitlement of 15 hours a week early education for three and four year olds. This is currently funded by local authorities through the newly introduced early years single funding formula (EYSFF). Funding for this comes from central Government as part of the Dedicated Schools Grant (DSG). In the previous consultation, we sought views on improving the delivery of this funding for free early education.

7.2. We asked how important an element of local flexibility is in free early education funding. The feedback from the consultation was that overall local flexibility was important. This was so that funding could respond to local needs and priorities, and because the role of local authorities in funding free early education was considered a crucial part of wider local authority early years responsibilities. It is for these reasons that we intend to retain a model of local discretion in funding free early education, retaining the responsibility on local authorities for operating the EYSFF.

7.3. We also sought views on how successfully the EYSFF had been implemented and how it could be improved. Feedback on implementation of the EYSFF conveyed a range of views, but the main theme which emerged was that implementation had been a challenge – both for local authorities and providers – but now that it had been implemented it should be allowed time to bed in. Correspondingly, many respondents considered it too early to give feedback on the success of the EYSFF in achieving its aims of bringing greater fairness and transparency.

7.4. There was strong feedback on how the EYSFF could be improved, focusing on the themes of variability between areas, complexity and lack of transparency. This consultation sets out and seeks views on proposals for how these could be addressed. It also explains other action being planned to help address these issues. It also consults on how the funding system from central to local government will work.

Simplifying funding for free early education

7.5. The EYSFF was not intended to be complex. The intention was to ensure all providers were to be funded for the hours of free early education they deliver, and in doing so reflecting their costs of delivering these hours. Alongside this, key policy objectives such as increasing the quality of provision, tackling disadvantage and increasing flexibility were to be supported. However, many felt that in operation the EYSFF was unnecessarily complex, with some providers not understanding the funding they receive. We believe this may be due to several factors which are addressed here.

Simplifying local formulae

7.6. In addition to funding through base rates, local authorities are able to offer additional financial supplements. Local authorities are required to operate a deprivation supplement and many local authorities choose to operate other supplements, including for flexibility and quality of provision.

These can be confusing to providers, and in some cases providers did not understand how they operated.

7.7. Local authorities are also able to differentiate within elements of the formula by applying banding. Banding is where local authorities can fund on varying levels within a single element of the EYSFF, such as different base rates depending on provider capacity, or different levels of supplements based on varying definitions such as the quality of provision. Banding can enable local authorities to be more specific in setting funding rates and encouraging progression within supplements. However, this level of differentiation – and the definitions behind it – can also bring confusion for limited impact.

7.8. We are therefore interested in how we can make the EYSFF simpler. Some possible options include:

- Reducing the complexity of the formula by removing the ability to have supplements (other than the disadvantage supplement) and removing or limiting banding.
- Consolidating all funding through a single base rate and deprivation supplement, and enabling local authorities to allocate other funding as they see fit, perhaps through clearly identifiable lump sums.
- In revising guidance to make it clear that local authorities should operate supplements in a clear and simple way, with a clearly communicated purpose.

Question 40: Do you agree we should aim for a simpler EYSFF? If so, how?

Targeting disadvantage

7.9. Local authorities are required to operate a deprivation factor as part of the EYSFF. This is intended to support the impact of free early education on tackling disadvantage by targeting more resources at disadvantaged children. The Government is firmly committed to continuing this policy. However, from analysis of available data, there appears to be considerable variation in how the deprivation supplement operates. This analysis points to large differences in the financial value applied to the supplement. It also indicates significant differences in the level at which the eligibility criterion is set. Whilst most local authorities used geographical deprivation measures (e.g. Income Deprivation Affecting Children Index), the size of local populations considered to be eligible was very variable.

7.10. There are several options to improve the focus on tackling disadvantage and make the support offered to disadvantaged children more consistent. One option could be to identify centrally the value of the disadvantage supplement, either in cash terms or as a percentage of overall free early education spend. Another option would be to seek greater consistency in the eligibility criteria, perhaps by aligning the disadvantage supplement more closely with those for free early education for two year olds

and the Pupil Premium. This would capture a similar level of population, using either child level or geographic based criteria.

7.11. A different approach entirely would be to focus resources at setting level rather than on individual children. This approach would mean financial investment in settings in the most deprived areas over time could be sustained, giving settings the security to use funding for longer-term investment, such as hiring more qualified staff.

Question 41: How could we refine the EYSFF so that it better supports disadvantaged children?

Bringing more consistency to free early education funding

7.12. The response to the consultation was clear that there were differences in funding paid to different types of providers as well as between different local areas. The Government understands that significant variation in funding, especially in neighbouring local authorities, causes confusion and uncertainty. However, given different area priorities, costs and characteristics, some variation in funding is inevitable. The challenge remains, though, as to whether action should be taken to reduce or limit variation. Part of this requires looking at how local authorities are funded.

7.13. We believe there are two options for continuing to fund local authorities for free early education. The first is to lock in the Spend Plus methodology, by funding local authorities on the basis of their current level of spend. Whilst this option avoids any turbulence, we do not think it is fair, and it does not enable greater consistency.

7.14. The second option is to allocate funding to local authorities on the basis of a formula, thereby ending for early years as well as schools the spend plus system. A formula would more fairly and more understandably distribute funding between local authorities. However, any change to how funding is allocated will over time mean redistribution between local authorities: this is the case for early years just as it is for schools. We will therefore again need substantial damping arrangements in place as we move to a new formula. This would be done through applying floors and ceilings (maximum annual decreases and increases) to budgets as the formula is introduced. This means that in the short term, allocations will be largely based on what local authorities are currently spending.

7.15. The introduction of funding by formula would be alongside the introduction of a fair funding formula for schools.

Question 42: Do you agree we should allocate funding to local authorities on the basis of a formula?

7.16. Any decision to introduce a formula would of course require decisions on the content of the formula to be used. Given the Spending Review settlement for free early education has been secured, the formula itself would need to be cost neutral, and operate without recourse to additional resources. The formula would then be used to allocate to local authorities the nationally available funding for free early education for three and four year olds.

7.17. We would anticipate such a formula would be largely derived from the school formula. This would mean a formula based on child numbers, with factors to reflect the deprivation of the area as well as an area cost adjustment (ACA). There is potentially a case for including a sparsity factor to recognise the potential higher costs in rural areas.

7.18. We would not however seek to develop a national formula based on settings, which would result in notional budgets being calculated at setting level.

Question 43: Do you agree a formula should be introduced based largely on the same factors as the schools formula?

Bringing greater transparency to free early education funding

7.19. The introduction of the EYSFF has been a major step forward in increasing accountability for local spending on free early education. It has required all providers to be funded on a participation basis, meaning providers are funded for the hours provided, not their capacity. The EYSFF has also enabled providers to see how much they are funded and how this funding is calculated. It also enables providers to compare funding with other local authorities and hold local authorities to account for these funding rates. But we believe more can be done to increase this transparency. We are exploring how best the Department for Education can make this information available on our website, enabling comparisons across local authorities. We are also exploring the possibility of benchmarking EYSFF rates in more detail. This work is being taken forward separately to funding reform. We will be in a position to know more once a thorough analysis of section 251 financial returns from local authorities has been completed.

7.20. In order to increase transparency further, we would like to develop a pro forma, alongside that for schools, which local authorities must use to set out their early years formulae. We would want local authorities to be able to explain in the pro-forma how their EYSFF operates, including the level of funding for supplements and how these supplements operate. We will then ask local authorities to publish them.

Question 44: We would be grateful for views on whether anything else can be done to improve transparency.

8. Pupil Premium

8.1. We are also consulting on how to distribute the Pupil Premium from 2012-13. We intend both to increase the amount available per pupil and to increase the number of pupils that attract the premium.

8.2. For 2011-12 we are using current known eligibility for Free School Meals (FSM) to determine eligibility for the premium. FSM is currently our only pupil-level measure of deprivation. We have however said we would consult on increasing the coverage of the premium from 2012-13 to include pupils who have previously been eligible for FSM. The benefit of using existing FSM eligibility for the allocation of the premium is that it is clear and simple; schools will know how many FSM pupils they have on school census day in January and so can work out how many pupils will be eligible. For this reason it was chosen for the first year of the premium's introduction. It is however generally considered to under-report the actual level of deprivation as not all parents with eligible children register them for free school meals and the proportion of eligible pupils claiming drops the older pupils get.

8.3. We are offering two options for extending the coverage of the premium. We believe it is right to retain a pupil based deprivation indicator to determine eligibility for the premium, so that it can continue to reflect the characteristics of the individual pupil. FSM is the only such indicator currently available. The options to extend the premium are:

- a) To include pupils eligible for FSM in one of the last three years (known as "Ever 3"); or
- b) To include pupils eligible for FSM in one of the last six years (known as "Ever 6").

8.4. These options were first set out in last July's consultation on school funding for 2011-12, which included options for the introduction of the Pupil Premium. As the analysis in that consultation showed, there is a strong link between FSM eligibility and educational underachievement. Eligibility for FSM at any point is associated with underperformance as children who have previously been eligible for FSM have consistently lower educational attainment than those who have never been eligible.

Deciding between an Ever 3 or an Ever 6 measure

8.5. Either of the options will further the aims of the Pupil Premium by including a higher proportion of underachieving children than at present. Both would address some of the issues of under-reporting but would not cover pupils whose parents have never claimed. Using an Ever 6 measure would better address the issue of the declining proportion in secondary schools as those eligible in Year 6, the last year of primary education, would continue to be eligible for the pupil premium throughout secondary education to Year 11.

8.6. There is a balance to be struck between the size of the cohort and the level of the Pupil Premium for each pupil. Using an Ever 3 measure would increase coverage from the 17% who are currently eligible for the Pupil Premium to around 21% of pupils, adding some 250,000 more pupils (based

on January 2010 numbers and assuming no population growth) and an Ever 6 measure would cover around 24% of the school cohort, adding over 500,000 pupils to the total. The increase in the overall quantum will be sufficient to allow for the additional pupils, and enable an increase in the level of the Pupil Premium for all pupils.

8.7. Moving from current FSM eligibility to an Ever FSM measure will affect local authorities differently in terms of the proportional increase in their FSM eligibility. Annex G sets out the impact on individual local authorities and shows that moving to an Ever 6 measure can result in a percentage increase of around 15% in one local authority to an increase of over 60% in another.

8.8. For looked after children, the intention is to increase the premium in line with the main deprivation premium.

Question 45: What is your preferred option for determining eligibility for the Pupil Premium from 2012-13? Should it be based on the Ever 3 or Ever 6 measure?

Calculating the Pupil Premium

8.9. A single, flat rate premium currently applies with no adjustment to reflect differences across the country in the cost of providing services (Area Cost Adjustment) or to reflect different levels of funding. This has resulted in a simple and transparent premium which is clearly understood by schools and parents. The roll out of the premium is still in its early stage and the priority as the premium is fully implemented is to ensure that funding is effectively targeted to raise the attainment of deprived pupils. There are also issues around how best to reflect area costs which are considered as part of our wider review of school funding.

8.10. As we consider how the Pupil Premium should be taken forward in future years, we will consider whether the distribution methodology for the premium should be amended to recognise differences already in the system or kept at a flat rate. The approach which recognises existing differences in the system would compensate for differences in funding by providing higher funding for schools with deprived pupils in the areas that currently receive lower levels of funding. However, keeping the Pupil Premium as it is currently distributed would mean it remains simpler and more transparent. We will consider these options further in light of responses to this consultation, and on the basis of the timing and nature of broader reform. We are not proposing to apply an Area Cost Adjustment to the premium before 2014-15.

Question 46: What is your preferred approach for calculating the Pupil Premium?

9. Timing for implementation

9.1. In the previous consultation we asked when we should start moving towards a fair funding formula. 43% of respondents said 2012-13, and 23% of respondents said 2013-14. The majority of the remainder were unsure. We have therefore decided to maintain the current system in 2012-13 to enable further consultation and sufficient time for local authorities, Schools Forums, schools and Academies to interpret the reforms and the settlement.

9.2. In order to enable further full and detailed consultation, and to enable schools, local authorities and Academies to plan, we intend to issue a “shadow” settlement in 2012-13. This will illustrate the potential allocations under the new system for the financial year 2012-13 in respect of local authorities and maintained schools, and the academic year 2012/13 in respect of Academies. As well as allowing final consultation on the detail, this will help to identify any problems that need to be resolved both locally and nationally in advance of full implementation of the new system. We expect to publish this “shadow” settlement in the spring of 2012.

9.3. We intend to continue the existing practice of providing multi-year settlements for local authorities within the spending review periods to enable greater predictability of budgets for both local authorities and schools. We will explore how these could work and which aspects would be updated, such as pupil numbers, as we develop the new formula.

9.4. We are aware that despite the strong reasons for reforming the system, it is essential that we take time to get it right given the likely redistribution and the need for schools, Academies and local authorities to plan for changes. We are therefore consulting on when we should begin this process. We could either implement the new system from 2013-14 or we could wait until the next spending period (from 2015-16). We will use responses at this stage to help shape the development of the formula but will seek further views on timing when we publish the shadow settlement.

Question 47: Do you think we should implement the proposed reforms in 2013-14 or during the next spending period?

9.5. If we introduce the reforms during the next spending review, then we would need to consider how we could improve the system and deal with some of the problems we have identified in the shorter term.

9.6. Our immediate priority would be to make the system more transparent, by making it much clearer how the budgets of individual schools are calculated. Even without the wider changes suggested, this would represent a substantial improvement on the current system.

9.7. Therefore, whilst we would intend to reform the system fully during the next spending review period, for this period we would:

- Improve the transparency of the calculation of schools’ budgets by restricting allowable local factors;

- Require local authorities to put their formulae in the pro forma set out in paragraph 2.16 in order to aid understanding of schools budgets and allow comparison of local formulae by schools and local authorities;
- Fund Academies through the EFA, who will do so by using the local authority pro forma which sets out the formula. Academies and maintained schools will receive their budgets based on the same data, removing the 17 month time lag for Academies;
- Amend the School Finance Regulations so that all the services set out in paragraphs 4.4-4.7 in block 1 are automatically delegated to schools. Maintained schools can then decide whether to have the funding un-delegated. This will eliminate the need for Schools Budget LACSEG.
- Make changes to the calculation of the local authority LACSEG (as described in paragraph 5.6).

9.8. We would also introduce a number of the proposals within the chapter on high needs pupils, for instance establishing the base unit of funding for high needs settings, and developing the method for funding Special and AP Academies and Free Schools.

9.9. We would then look to introduce the wider reforms in the next period and use the intervening period to continue to consult on the new system and support local authorities, schools and Academies to plan.

9.10. We do not anticipate there will be new burdens associated with these reforms. The policy intention is to streamline and simplify the system. We will, however, work with local authority and school partners to ensure that the financial implications for local authorities and schools are fully addressed and ensure that the new burdens guidelines are fully adhered to.

Next Steps

9.11. This consultation will run for 12 weeks. We will then do further work during the autumn with a view to publishing a 'shadow settlement' in the spring of 2012, alongside further options for the timings for reform. We suggest that local authorities begin to consider what changes could be made to their local formulae in order to make them simpler and transparent in line with the proposals for the future.

Glossary of Terms and Acronyms

Academies

Publicly funded independent schools that are free from local authority control. Other freedoms include setting their own pay and conditions for staff, freedoms concerning the delivery of the curriculum, and the ability to change the length of their terms and school days.

Additional Learning Support (ALS)

A grant paid by YPLA directly to post 16 learning providers for support to assist individual learners with SEN or LDD.

Age weighted pupil unit (AWPU)

A factor used in local authorities' local school funding formulae to distribute different amounts of funding for pupils of different ages or at each key stage.

Area Cost Adjustment (ACA)

A factor used in the local government finance system to reflect the higher cost, mainly pay, of providing services in some parts of the country.

Central Expenditure Limit

The maximum increase in expenditure that can be incurred on a local authority's budget for centrally managed items within the Schools Budget. The limit can be exceeded only with the approval of the schools forum.

Department for Communities and Local Government (DCLG)

The central government department responsible for the distribution of general (non-schools) funding to local authorities.

Dedicated Schools Grant (DSG)

The ring-fenced specific grant paid by the Department to local authorities from April 2006 in support of the Schools Budget. The money has either to be delegated to schools or used for centrally managed provision for pupils. It can only be spent on other children's services with the approval of the schools forum and where an educational benefit can be justified.

Disability Living Allowance (DLA)

A tax-free benefit for children and adults who need help with personal care or have walking difficulties because they are physically or mentally disabled.

Early Intervention Grant

A grant from Government to local authorities in England to fund early intervention and preventative services. The grant is not ring-fenced and, subject to local decision making, the EIG can be used to support a full range of services for children, young people and families.

Early Years Single Funding Formula (EYSFF)

The single local funding formula that each local authority is required to develop and implement to fund all free entitlement to early education and care for 3 and 4 year olds.

Education Funding Agency (EFA)

Education Funding Agency (EFA) - a new DfE executive agency that, from April 2012, will be responsible for capital and revenue funding for 3-19 education and training. The EFA will directly fund Academies, Free Schools, and 16-19 providers; it will fund local authorities for maintained primary and secondary schools; and it will be responsible for the distribution of capital funding and advice on capital projects.

English as an Additional Language (EAL)

Term used to define a pupil whose mother tongue is not English. It is one of a number of factors that may be taken into account in a local authority's formula under regulation 18 of the School Funding Regulations.

Free schools

All-ability state-funded schools set up in response to what local people say they want and need in order to improve education for children in their community. These new schools have the same legal requirements as Academies and enjoy the same freedoms and flexibilities.

Free School Meals (FSM)

Known eligibility for Free School Meals is commonly used as an indicator of deprivation. FSM eligibility is based on whether the child's parents are in receipt of certain non-work benefits, including Income Support, Job-Seeker's Allowance and Tax Credits.

General Labour Market (GLM)

A methodology used in the past to calculate the weight of an Area Cost Adjustment to the Dedicated School Grant, based on costs within the labour market as a whole (as opposed to just schools).

Guaranteed Unit of Funding (GUF)

The per pupil amount of money allocated to each local authority through the Dedicated Schools Grant (DSG)

Her Majesty's Treasury (HMT)

The United Kingdom's economics and finance ministry.

High Needs Pupils (HNP)

Pupils with very specific needs, mainly those with high cost Special Educational Needs (SEN) and in Alternative Provision. It is defined roughly as children whose provision costs around £6,000 more per annum than the average.

Income Deprivation Affecting Children Index (IDACI)

A measure of financial deprivation that affects children: a score and rank is provided for each Lower Super Output Area.

Local Authority Central Spend Equivalent Grant (LACSEG)

A grant paid to Academies in recognition of the fact that as independent schools they no longer receive a number of services from local authorities, and must make appropriate provision for themselves.

Key Stage

There are four distinct stages of schooling:

Key Stage 1: pupils aged 5 to 7 - year groups 1 to 2

Key Stage 2: pupils aged 7 to 11 - year groups 3 to 6

Key Stage 3: pupils aged 11 to 14 - year groups 7 to 9

Key Stage 4: pupils aged 14 to 16 - year groups 10 to 11.

Maintained Schools

A school which is funded via the local authority and therefore subject to local government control.

Minimum Funding Guarantee (MFG)

The MFG stipulates the minimum amount by which a school's budget must increase (or maximum decrease) when compared with its budget for the previous year, before allowing for changes in pupil numbers. Some specific items of expenditure (such as rates and resources specifically assigned to individual pupils with special needs) are excluded from the coverage of the MFG. The local authority can modify the operation of the MFG with the approval of the Secretary of State.

Private Finance Initiative (PFI)

The main vehicle for delivering Public Private Partnerships (PPPs). Design, Build, Finance and Operate (DBFO) is the main PFI model used in local government. The local authority purchases services from the private sector in association with a capital asset such as a school. The private sector owns the asset through a freehold or long lease and provides the services over the contract period, usually 25 to 30 years. At the end of the contract the assets return to local authority ownership. The underlying rationale for PFI is that the private sector is assumed to be able to deliver efficiencies that more than offset the higher financing costs. The PFI started in 1997-98.

Pupil Premium

Targeted funding (in addition to the DSG) paid to schools via the local authority, specifically aimed at the most deprived pupils to enable them to receive the support they need to reach their potential and to help schools reduce educational inequalities. In 2011-12, the premium was distributed to pupils known to be eligible for Free School Meals and was £430 per pupil.

School Funding Implementation Group

The Department of Education's main advisory group on school funding. Groups represented on it are:

- Association of Directors of Children's Services (ADCS)
- Association of School and College Leaders (ASCL)

- Association of Teachers and Lecturers (ATL)
- Foundation, Aided Schools and Academies National Association (FASNA)
- Independent Academies Association (IAA)
- Local Government Association (LGA)
- National Association of Head Teachers (NAHT)
- National Association of School Business Management (NASBM)
- National Governors Association (NGA)
- National Association of Schoolmasters / Union of Women Teachers (NASUWT)
- New Schools Network (NSN)
- National Union of Teachers (NUT)
- Special Education Consortium (SEC)
- Young People's Learning Agency

Schools Forums

A statutorily required body which represents the governing bodies and head teachers of local authority maintained schools and Academies, together with other members. The purpose of the forum was originally to advise the local authority on matters relating to schools budgets. The membership and role of the forum has been progressively extended.

Section 251 (S251)

Refers to the section of the Apprenticeships, Skills, Children and Learning Act 2009 which requires local authorities to publish annual budget statements relating to their education spending. The statements (often referred to as section 251 statements) are the means of informing schools and the public in general about the education funding plans and spend of the local authority.

Sparsity

The term used to reflect areas of low concentrations in pupil population and which recognises the additional costs required to run an (often small, rural) school in an area of low pupil density.

Special Educational Needs (SEN)

Children have special educational needs if they have a learning difficulty, which calls for special educational provision to be made for them.

Spend Plus

The method of allocation of DSG to local authorities in the period 2006 to 2012. It comprises a fixed percentage uplift in per pupil funding plus additional amounts allocated in accordance with ministerial priorities.

Studio school

A school model for 14-19 year olds which teaches the national curriculum alongside enterprise themed projects and real work, designed to better prepare pupils for the world of work.

Super Output Areas

Super Output Areas (SOAs) are a geography designed for the collection and publication of small area statistics. SOAs are thought to give an improved basis for comparison across the country because the units are more similar in size of population than, for example, electoral wards.

Lower Layer Super Output Areas (LSOAs)

LSOAs were built using 2001 Census data from groups of Output Areas. They had a minimum size of 1,000 residents and 400 households, but average 1,500 residents. Measures of proximity (to give a reasonably compact shape) and social homogeneity (to encourage areas of similar social background) are also included.

Middle Layer Super Output Areas (MSOAs)

The MSOAs were built using 2001 Census data from groups of LSOAs and had a minimum size of 5,000 residents and 2,000 households. They also fitted within the boundaries of local authorities as at the end of 2002.

Underperforming Ethnic Groups

Those ethnic groups that evidence shows perform less well than others. Factors including deprivation, socio-economic background, and pupil / family characteristics such as aspirations and attitudes, may at least partly explain the attainment gap between the underachieving ethnic minority pupils and their peers. Ethnicity is one of a number of factors that may be taken into account in a local authority's formula under regulation 18 of the School Funding Regulations.

University Technical College

A college for students aged 14 to 19 which specialises in technical studies and is sponsored by a university and a local business. They offer full time courses which combine practical and academic studies.

Young People's Learning Agency (YPLA)

The organisation responsible for funding learning opportunities for 16-19 year olds; funding and supporting academies; and for funding support for young learners. It will be closed and replaced by the Education Funding Agency in April 2012.

List of Annexes

A	Current allowable factors: Schedule 3 of the School Finance Regulations
B	Derivation of the £95,000 lump sum
C	Sparsity thresholds
D	Area Cost Adjustments – explanatory note
E	Proposed functions within each funding block
F	Proposed split of section 251 lines to the determine size of the funding blocks
G	Levels of deprivation in each local authority by FSM, Ever 3 and Ever 6

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