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## What are the Priorities for Local Government Finance Reform?

### INTRODUCTION

*Roger Gough, Senior Advisor, Localis*



In this second Localis Policy Platform, two County Councils (Essex and Leicestershire), a District Council (Tandridge) and a unitary authority (Bracknell Forest) address the need for change in the local government finance system.

As the articles point out, there is no need to reinvent the wheel here. We have had the Lyons Review, the Balance of Funding Review and other studies going all the way back to Layfield in the mid-seventies. Some of the issues raised here can be traced back further still. Struggling to respond to the economic woes of the twenties, Winston Churchill urged business de-rating while Neville Chamberlain, with his experience of local government, argued that this would produce a damaging separation between local authorities and business. That debate ended in a draw: sixty years later, the loss of the business rate in 1990 confirmed Chamberlain's point. A common theme of our contributors is the need to get that financial link between business and local government back.

Another major theme is the sheer inflexibility of the current system. In spite of its wide range of functions, British local government remains a one-club golfer, dependent on a highly visible and unpopular tax that is only loosely linked to ability to pay, coupled with an opaque grant system.

A few years ago, Localis supported a Policy Exchange/ New Economics Foundation study of local government finance that argued for "radical but politically feasible" changes: a reformed council tax, access to other taxes (including a locally variable element of income tax), a relocalised business rate and changes to the grant system. The case for changes of this kind is as strong as ever; without them, we will – as Sir Simon Milton warned in a speech to Localis over a year ago – "drift inexorably towards another council tax crisis." Even if

an issue has been with us for a long time, action cannot be deferred indefinitely.

### BRACKNELL FOREST COUNCIL

*Councillor Paul Bettison, Leader*



Bracknell Forest Council is widely regarded as one of the Country's better performing Councils. This is evidenced both in its ratings by the Government's inspection regimes and by the satisfaction levels of local residents. It has consistently scored highly in its "Use of Resources" score, delivered over and above on its Efficiency Savings target and maintained the lowest Band D Council tax of all Unitary Councils. And yet this has all been achieved against a backdrop of a finance system founded on a tax that has all but lost its credibility. However it is not too late to restore the system with the confidence it so desperately needs and to put local government finance on a firm footing to support our local communities in the years ahead.

**"We do not need to re-invent the wheel"**

Bracknell Forest Council takes pride in describing itself as an innovator, as well as a Council willing to learn from others and implement best practice. We do not look to re-invent the wheel where possible and as such, the case for reform of local government finance has been made both in the "Balance of Funding" review and most recently in the Lyons Inquiry. We acknowledge that the last 5 years has seen a significant step-forward in the relationship between central and local government. The evolving Local Area Agreements are testament to the confidence both sides have on the relationship delivering for both sides. Local authorities are seen by central government as the first and obvious choice for delivering key public sector priorities locally and are trusted to do so with ever reducing guidance



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and prescription. In these forthcoming economically challenging times it is more important than ever that those decisions are taken locally. Local authorities are confident in their ability to play a vital role – this confidence should be shared by central government. This can be demonstrated by accepting and implementing the reforms recommended by Sir Michael Lyons.

The Lyons Inquiry accurately identified many of the fundamental problems with the current finance system, and as such his report is the best place to consider the comprehensive nature of these failings. This article will highlight some of those areas that are of the highest priority to Bracknell Forest. It is a fact that the growth in education and social care spending since the 1950s has outpaced that for other programmes and this is to remain a feature of future local public service delivery. However this growth has been a key factor in the pressures placed on local taxation leading to changes and compromises around the edges of the system, making it more difficult to understand and operate, undermining the trust in local government finance.

**“Our highest priority is the abolition of capping”**

As such local government is identified with a high profile unpopular tax that is being asked to do too much and which it barely controls.

Therefore control is our highest priority and the abolition of council tax capping can hand back that control to local government. The characteristics of an optimal funding system should include accountability, fairness, sustainability, flexibility for local decisions and delivery of national priorities. Using this criteria capping fails on all these accounts, save perhaps for the delivery of the last! But even this is confused as demonstrated by the constraints placed on Bracknell Forest. Historically a low-taxing authority, the Council

has been widely praised for its financial stewardship. It has done this against a back-drop of a £0 Council Tax prior to becoming a unitary authority, and continues to

set the lowest Band D tax of any English unitary authority. Yet a crude and universal cap of 5% raises considerably less resources and places a much lower real increase on our residents than a 5% increase by the highest Band D unitary authority.

**“As long as the government retain responsibility for whatever formula is in place, there will always be the accusation that the allocation of resources is politically motivated”**

Whilst this demonstrates the perverseness of the regime at a local level, fundamentally the capping regime sucks the life-blood out of local accountability and Sir Michael Lyons was right to recommend that

the Government should cease to use, and then abolish its capping powers. Local authorities should have to account to local taxpayers for their taxing and spending decisions through the ballot box.

Given the complexities of designing a method to distribute government funding it is unlikely that such a system will ever be developed to which all parties are completely satisfied. Whether we move to three-year or five-year settlements, there will always be the background clamour for formulae to be revised, cohorts reviewed and proxies realigned. And as long as the industry of statisticians and accountants are kept occupied and the Government retain responsibility for whatever formula is in place, there will always be the accusation that the allocation of resources is in some way politically motivated. The now widely welcomed decision to create an independent Monetary Policy Committee should be followed up with an independent Public Finance Commission to provide evidence, evaluation and advice to both local and central government on the issues of local government funding. It is unlikely that the panacea of a grant distribution system will ever be developed, we would be happy with

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fair and equitable!

Once this has been put in place, our third priority would be for the finance system to recognise the “costs of doing business” for smaller authorities (particularly Unitary authorities) and to incorporate real incentives to own and grow their tax bases. The first can be done

**“We need to a finance system which recognises the ‘cost of doing business’ for smaller authorities”**

through reviewing the influence of deprivation within the current formulae and by increasing the fixed amount within the calculations to reflect the underlying infrastructure and capacity needed to provide a sustainable local service. The need for a more buoyant tax base and one which can incentivise local authorities has been widely discussed and addressed by the Lyons Inquiry. This could be achieved by being bolder on the implementation of the Supplementary Business Rate proposals and returning the funds distributed through LABGI to their previous levels, in the £bn not the £m. Again there is no need to reinvent the wheel, just the courage, trust and confidence of central government to relax its grip on Councils and let them decide how resources can be best raised and spent locally.

**ESSEX COUNTY COUNCIL**  
*Lord Hanningfield, Leader*



English local government labours under a funding regime which militates against engagement, accountability, and transparency at the local level. What we need is a system of local government finance that is fit for a 21<sup>st</sup> century pluralist democracy.

Local authorities are best placed to provide community

leadership, but current funding structures limit fiscal flexibility and stifle innovation. As a result, it is difficult for many councils to make the most of their place-shaping potential.

Simply put, local services need to be better aligned to local desires and local needs. When they are, public services become more responsive. To help embed this responsiveness across the local government family, local government finance needs to be reformed.

Local authorities must have the tools to shape local fiscal policy. To many in local government this will be self-evident but it is even more apposite given the current economic climate.

As a minimum, local government finance needs to be reformed so that we see:

- an end to capping and the abolition of ring-fenced grants;
- a viable alternative to Council Tax; and
- the relocalisation of business rates.

**“Locally funded, locally accountable local government can help revive local democracy”**

There is no doubt that greater financial freedom would support local authorities’ community leadership role. Locally-funded, locally accountable local government can help revive local democracy.

**An end to capping and the abolition of ring-fenced grants**

The framework within which local authorities and central government currently operate exemplifies the exercise of central control. Formula Grant presupposes the centre is best placed to recognise, and respond to, local needs and aspirations. In today’s world, no one can still believe this is true.

Centrally allocated grants and centrally controlled redistribution do little to persuade the electorate of the capacity of local authorities to represent their



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aspirations and desires. They also fundamentally weaken the relationship between taxation and services.

Any new financial settlement needs to be grounded in the principle of local autonomy. Central grants, capping, and Whitehall imposed definitions of 'acceptable' limit the capacity of democratically-accountable councils to

**“Grants fundamentally weaken the relationship between taxation and services”**

deliver the local government local people want. Most people now acknowledge the truism that 'one size does not fit all', but we are still some way off from recognising local variation in services as a sign of vibrant pluralist democracy.

We need to move beyond the idea of uneasy balance of power and instead develop a parity of esteem between central and local government. The removal of capping and a substantial reduction in the use of ring-fenced funds – hypothecation could, of course, still be used when central government wants to buy a distinct outcome from a willing local authority – would show that central government recognises local councils' competence and mandate.

### **A viable alternative to Council Tax**

From a technical perspective, the reliance on a single locally-raised and retained tax has created a situation where Council Tax is as overworked as it is disliked.

By focussing on the value of a house over the ability to pay, the tax is ill-tuned to England's changing demography. There is a relatively weak relationship between the value of a house and the ability to pay. Pensioners on fixed incomes are penalised for electing to live in their family homes. This cannot be right. I've already committed Essex County Council to offset the burden of Council tax by offering financial support to some of the county's most vulnerable residents. While this programme will alleviate suffering in the short-term, it cannot be a sustainable approach.

Given that property taxes are typically easy to collect, it makes sense to retain some form of property-based tax – what is clear is that it cannot be the sole method by which local government can raise revenue. If property tax were accompanied by one or more additional local taxes, the property element of the tax-burden could be reduced.

### **A reallocation of business rates**

2007 was not so long ago. Yet when one considers that one of the few elements of the Lyons Inquiry not kicked into the long grass was the idea of a supplementary business rate of up to 4 pence in the £, it becomes clear how much has changed.

Today, local authorities need to do more to help their local business – particularly those small and medium sized businesses that are the backbone of the UK's real economy. I for one would like to cut business rates given the economic downturn, but with rates levied nationally, local authorities are not able to respond as they would like.

**“I would like to cut business rates given the economic downturn”**

Since the business rate was removed from local authority control in 1990, the link between local business and local government has been weakened. Returning business rates to local government would strengthen the relationship between councils and commerce. It would also go some way to providing local government with a buoyant tax base – something that it lacks at the present time.

### **Conclusion**

To conclude, it is clear that a self-funded local government sector would be in a stronger position to place-shape and provide the community leadership some authorities struggle to deliver under the current system. By making explicit the relationship between local public services and local taxes, accountability, transparency and fairness could be improved.



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Some may find the idea of an entirely self-funding sector a step too far. For those that do, there must at least be the recognition that local government must be able to raise a greater proportion of its expenditure locally.

A broader range of tax options, including an alternative property tax, and relocalised business rates – and potentially scope for other innovations such as local income and sales taxes and access to bond markets - would offer a range of fiscal levers and help revive local democratic accountability. When at the top of its game, local government can achieve great things – the shame is that the current system of local government finance serves to hinder more than it helps. This cannot be allowed to continue.

**TANDRIDGE DISTRICT COUNCIL**  
**Councillor Gordon Keymer, Leader**



In China there is a saying: “May you live in interesting times”. It is as much a curse as anything and we are currently living through interesting times as the global recession tightens its hold and starts to affect public sector finance.

From a Tandridge District Council perspective, some of the reforms which would greatly enhance the level of local service provision include the following:

### Rates Support Grant changes

Tandridge District Council receives approximately £460,000 below the Surrey average in terms of Rates Support Grant (RSG), owing to the complex formula and its application locally. This represents the equivalent of almost 8% in council tax

In addition there are unrealistic floor levels set and the latest Comprehensive Spending Review (CSR07) unrealistically provided Tandridge District Council with a 1% increase in RSG for 2008/09 and only 0.5%

increase for 2010/11 and 2011/2012.

“Additional services are being transferred for delivery by district councils with no additional resources”

This has occurred at a time when inflation is still running at a high level while interest receipts are plummeting. At the same time additional services are being transferred for delivery by district councils with no additional resources in many cases. A realistic recognition of the importance of district council services should be forthcoming in this annual financial settlement.

### Gershon Savings

Central Government and the Audit Commission should recognise efficient authorities more and not implement a “one size fits all” programme of savings targets. Tandridge in common with all councils is expected to achieve a year-on-year efficiency saving in real cash terms of 3% with no account being taken of previous low levels of council tax increase, savings/efficiencies achieved or base level of resources/staffing levels.

### Non National Domestic Rates

The South East of England produces considerable wealth for the whole of the country and yet Tandridge is only given 35% of the NNDR it collects.

“NNDR should be returned to the local authorities where it is collected”

Many businesses do not understand this and consider themselves to be the golden geese, laying the golden eggs from which their local authority benefits. They do not realise that their cash is taken by Government and distributed on a per capita across the country. I have always believed that NNDR should be returned to the



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local authorities where it is collected though there would need to be some form of equalisation. Until that happens, a change in formula reallocation for Tandridge District Council would make a considerable difference, particularly at this challenging time for local businesses.

### Capping

I do not believe in capping and particularly so for small district and borough councils. In Tandridge the average council tax for a Band D property is just £3.50 per week or under £200 a year for all local services. This is such a small sum and an increase of just £12 a year would put us at risk from capping and all of the expensive bureaucracy involved. If the Government insists on capping then district councils should be exempt due to their low level of spend.

### Planning fees and Local Land Charges

There have been significant changes to planning with applications decreasing because of the changes in planning legislation, but also due to the economic downturn.

**“Planning fees should be set locally at least to reflect service costs”**

This is having a negative impact on income locally where planning charges are set nationally, along with local Land Charges, which reduces local freedoms and the opportunity for local authorities to cover the costs of the service. Planning fees should be set locally at least to reflect the service costs.

### Negative Housing Subsidy

Tandridge District Council, along with other councils, loses significant funding through the current Housing Subsidy policy.

In Tandridge this adds up to around £3.5m a year being taken out of our local economy and would seem to fly in the face of the government's current priority in

terms of providing affordable social housing.

A change in the Housing Subsidy rules will allow local councils to reinvest Housing Subsidy, in partnership with the private sector and others to into the local economy while at the same time providing additional affordable social housing properties. This single change would enhance the housing agenda significantly locally and thereby also improve the national shortage.

**“A change in the Housing subsidy would enhance the housing agenda...and improve the national shortage”**

### Track record of delivery

Districts and borough councils have a good track record of delivery measured by improved performance through the Audit Commission, but also in terms of managing resources.

These councils have taken on new responsibilities and implemented new legislation, often within existing resources and still meeting the Gershon levels of efficiency savings.

Those most significant to Tandridge District Council include the Electoral Registrations Act, Licensing Act, Gaming Act, Concessionary Bus Fares, recycling targets and increased recycling and smoke free legislation.

Financial reform should recognise these additional responsibilities and the resources required for their delivery, rather than asking councils to take on more, while still insisting on a 3% saving and restricting the raising of taxes and other income locally.

### National unfunded initiatives

Finally, I would like to see reform of Government initiatives which impose national issues on local councils, do not always meet local priorities and are



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certainly not affordable in many cases. These can have significant negative affects on communities and on local authority funding.

Two recent examples include the "free swimming" initiative for the under 16s and over 60s. The actual cost of providing free swimming far outweighs the funding from the government.

We do live in very interesting times where change is swift and unpredictable. District and borough councils in particular are facing additional pressures as they are the first port of call for residents and businesses needing help and support. District and borough councils run tight ships and so their budgets are put under great pressure when Government puts forward underfunded initiatives. What amazes me is the way district and borough council leaders continue to provide good services on such limited resources.

### LEICESTERSHIRE COUNTY COUNCIL

*Chris Tambini, Deputy Head of Strategic Finance*

Leicestershire County Council is a large council serving 635,000 people in the heart of England. It has a gross budget of £850m and is characterised by low levels of Government funding, low unit cost and high performance. It receives the lowest level of Dedicated Schools Grant (DSG) of any of the 150 upper tier authorities in England. If Leicestershire was funded at the county average, it would receive £22m in additional funding. The picture is similar for other services and the county received £31 (18%) less formula grant per person than the average for counties with Fire. If it was funded at the average it would have received £20.2m in additional funding. Despite low Government funding council tax is lower than average and the council is one of the highest performing councils in England.

Given our starting point you would expect us to press for a fairer distribution of Government grant. This is indeed the case, as we do not believe the current system is fair and there is the perception that the

formulae are manipulated to ensure that the Government achieves the desired result whatever that may be. As such we are very much of the belief that the distribution of grant should be both transparent and overseen by a body independent of Government.

**"The distribution of grant should be both transparent and overseen by a body independent of Government"**

Local taxation is a political hot potato - changes create winners and losers as evidenced by the poll tax. As such any radical changes are likely to be resisted especially in a time of economic recession where people's ability to cope with changing tax levels is limited and stability is required. Although criticised, the current system does work and there is a place for a property tax. Steps should be taken to make sure it becomes a more efficient mechanism for wider policy objectives. Examples could include encouraging single people to live in smaller houses thus freeing up houses for families by offering family discounts, offering discounts when certain energy efficiency ratings are met or recycling rates achieved. We need the flexibility to react to important local and national issues such as global warming and housing shortages. We understand the need for a capping regime but again believe that it is best overseen by a more independent arm of Government such as the Conservative proposal for an Office of Budget Responsibility.

**"Steps should be taken to ensure Council tax becomes a more efficient mechanism for wider policy objectives"**

We believe that the links and accountability between local businesses and local councils could be enhanced by at least putting an element of business rates back into local control. In Leicestershire we recognise the



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important role we have in fostering economic growth and are establishing a economic development company with our partners. We believe if a local council creates an environment within which businesses prosper, at least some of the benefit from increased business rates should accrue to the locality. This would also mean that gearing effects are more limited (this is when a small increase in spending can translate into a large increase in council tax because of the high proportion of funding received through Government grant). If this more radical solution is not adopted, the recent tentative steps of introducing some local accountability for business such as business improvement districts and the supplementary business rate should be encouraged and developed. The important relationship with business needs to be strengthened.

“One of the main barriers to more radical co-operation and integration of services is the fact that the financial regime has not kept pace with the performance management framework”

The Local Area Agreement in Leicestershire has been a successful way of getting organisations to work together to improve services and generate savings. However, one of the main barriers to more radical co-operation and integration of services is the fact that the financial regime has not kept pace with the performance management framework. This means that although targets are joined up, individual organisations can be reluctant to pool budgets as a result of a perceived loss of control. This could be improved by automatic pooling of a proportion of all organisations' budgets – in a two tier area such as Leicestershire this could include County and District Councils, Fire, Police and local NHS. This could be done through Area Based Grant. Another alternative would be to pool areas where it is clear savings or service improvements can be made by a more collaborative approach. An

example could be to pool budgets that relate to council tax collection as it is clear from Audit Commission studies that economies of scale would be achieved by joint service provision. The democratic framework for partnership working is being developed through the introduction of local improvement networks and the wider role of scrutiny. However, further developments especially with regard to joint executive decision making between health and local government may be required if this more radical approach is to work.

“There is a case for pushing funding straight to the local level”

The final priority for reform is the continuing plea for a reduction in regulation, guidance, inspection and the wide variety of demands placed on local government from central and regional government. There is a case for pushing funding straight to a local level, with local and multi area agreements providing a good mechanism, rather than routeing it through Government Offices, central initiatives or other bodies such as Government created Regional Improvement and Efficiency Partnerships. The current method is both bureaucratic and expensive to operate and can result in top-down, imposed priorities, rather than a bottom-up approach where funding is best allocated to meet local priorities.

### FOR MORE INFORMATION

**Localis** is an independent think-tank dedicated to issues of local government and localism more generally. For more information on the work of Localis, please visit [www.localis.org.uk](http://www.localis.org.uk), or phone 0207 340 2660. For more information on the individual Councils, please follow these links:

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