Written evidence submitted by London Councils [FSR 065]

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London Councils represents London’s 32 borough councils and the City of London. It is a cross party organisation that works on behalf of all its member authorities regardless of political persuasion.

Executive Summary

- If lessons are to be learned from the past decade of changes to local government funding, the Government should:
  - Increase the overall level of funding for local government at SR19.
  - Fully assess the cost implications of new burdens and other responsibilities that have been passed to local government in recent years.
  - Improve transparency by being clearer about how the business rates system is used to fund different grants to local government.
  - Be less centrally prescriptive and devolve more control over funding to local government.
  - Take a longer-term funding approach to promote more strategic investment in prevention.
- London Councils urges the Government to use the Spending Review to:
  - review the sustainability and appropriateness of council tax and business rates as the primary funding mechanisms for local government;
  - broaden the incentives for pooling business rates under the full 75% scheme; and
  - consider how to broaden the range of freedoms, flexibilities, and revenue raising powers available to local government.
- Cities, and urban areas more broadly, are well placed to take advantage of smaller specific taxes that will directly support local economic growth, such as a Tourism Levy, Vehicle Exercise Duty, or the Apprenticeship Levy.
- In the long term, we continue support the recommendations of the London Finance Commission 2017 and welcome further exploration of income tax assignment.
- The SR19 process must be informed by a cross-department approach led by MHCLG but include all major spending departments.
- The key features of the SR settlement must be to address the main sector wide pressures in adult and children’s social care. However, we urge the Government to take a cross-departmental approach to addressing the unique pressures faced by London boroughs on homelessness, the costs of Unaccompanied Asylum Seeking Children and people with No Recourse to Public Funds.

Introduction
1. London Councils welcomes the opportunity to provide evidence to the HCLG Select Committee. Local government funding is at a cross roads, with two major reforms to the finance system (the Fair Funding Review and 75% Business Rates Retention) due to be implemented in April 2020, and the overall amount of funding in the system from 2020 onwards to be determined at the Spending Review in the autumn.

2. This inquiry is of fundamental importance for our member boroughs who are extremely concerned at the precarious financial situation they are facing following a decade of austerity in which they have been asked to deliver a wider range of services to more people while their overall resources have fallen by a third.

3. This is simply not sustainable: not only must the Government find an appropriate level of funding for the sector in the Spending Review – and by this we mean a significant increase in funding to meet the rising demand for adult social care, children’s services and homelessness prevention and support – but it must reform the way councils are funded, moving beyond the highly centralised and prescriptive system we currently have to one that empowers local authorities to invest in and sustainably plan for their local communities over the long term.

4. This submission is structured to address the four broad themes covered by the inquiry’s terms of reference.

TR1 - What lessons can be learned from past changes to local government funding in England, the current financial situation of councils, and how this has affected their ability to deliver services?

Past changes to local government funding

5. Local government funding has changed considerably in recent years and a number of lessons can be learned from the experience of the changes that have typified the last decade which can be summarises as:
   - disproportionate austerity;
   - growing unfunded burdens and cost shunts;
   - increasing complexity;
   - increasing centralisation; and
   - central government short-termism.

Disproportionate austerity

6. Local government has experienced a disproportionate level of austerity compared to other parts of the public sector. In the decade to 2019-20, core funding from central government to London boroughs has fallen, on a like-for-like basis, by 63% in real terms. Chart 1 below compares cumulative cuts to core funding from central government and overall spending power (as defined by government), with total public spending. It clearly shows that local government has shouldered a disproportionate share of funding reductions, while overall public spending increased in real terms.

Chart 1 – Cumulative like-for-like change in public spending - 2010-11 to 2019-20
Unfunded burdens and cost shunts

7. Over the same period, councils have been asked to deliver more. New policies and legislative changes have transferred more responsibilities and associated costs from central to local government without sufficient funding. The cumulative impact has added almost £1 billion per annum to London boroughs’ costs. These include, for example, the costs of the National Living Wage (estimated at £100 million per annum); systematic underfunding of homelessness (£170 million per annum); a £220 million mismatch between central funding and local provision for Council Tax Support schemes; an estimated £18 million shortfall in government funding for supporting Unaccompanied Asylum Seeking Children (UASC) up to the age of 25; and the completely unfunded costs of supporting people with No Recourse to Public Funds (at least £50 million per annum across London).

8. Other significant changes to legislation have not been accompanied by requisite funding to cover the rise in demand for services. In particular, the Children’s and Families Act 2014 has driven a huge increase in demand for SEND provision creating a funding shortfall of around £100 million in 2018-19; and the Homelessness Reduction Act 2017 is estimated to increase homelessness costs across London by £80 million per annum, while only £14 million of new burdens funding was awarded.

Complexity and a lack of transparency

9. The local government finance system has become increasingly complex over the last decade, enabling government to make changes to funding allocations that are often extremely difficult to understand. At the heart of this is a general lack of transparency in how local government funding is determined. The 1988 LG Finance Act states that the entirety of business rates collected in England must be used to fund local government. However, the Government does not publish how the central share of
business rates (i.e. the 50% share that not directly retained locally) is returned, merely that it funds “other grants” to local government. It is, therefore, unclear how the overall level of Revenue Support Grant (RSG) is set each year and is extremely difficult to verify when supposedly new funding is found.

10. The 2019-20 settlement, for example, found £16 million of new funding for rural areas, £153 million to eliminate “negative RSG”, and £650 million of funding for social care. Without detailed publication of central government funding to local government, it is unknown how much of this funding would have come back to local authorities as other grants anyway.

Centralisation

11. The last decade has also seen a greater tendency towards central government control over local government funding. The clearest example is in council tax policy, which has seen the effective capping through the referendum requirement, a series of “freeze grants” between 2011-12 and 2015-16 which undermined the tax base, and, since 2016-17, hypothecation of council tax to fund adult social care.

12. There is also a high degree of central control over business rates, with government retaining control over the parameters of the tax, such as the valuation process, the setting of the tax rate, and a growing set of complex mandatory reliefs. As described above, government retains a tight grip on how business rates revenues are returned to local government through RSG and a series of centrally prescribed ring-fenced grants.

13. Where the Government has allowed more local discretion and flexibility to raise funding and pool spending across local areas - such as through the Troubled Families Programme, the Better Care Fund, and the London business rates pilot pool - better outcomes have been delivered.

Short termism

14. Finally, the past decade – and particularly the current 4-year Spending Review period – has been typified by a short-term approach to local government funding. The scale of the funding crises in Adult Social Care in recent years has required six major policy interventions in three years. Had the Government provided an appropriate level of funding to begin with, the emergency measures may not have been required, and councils could have spent the funding in a much more strategic and effective way.

15. Similarly, the annual settlement process stifles a strategic approach to funding local services, hindering councils in developing long-term plans. Longer term funding certainty would provide the platform to deliver transformation plans and long-lasting efficiencies through prevention and invest-to-save initiatives.

The impact on service delivery
16. The impact of these changes to the finance system is clear. One council has already issued S.114 notices in 2018. Others may follow unless appropriate levels of funding are found in the Spending Review. No S.114 notices have been issued in London yet. However with a £2 billion funding gap to close over the four years to 2022, including almost £400 million in 2019-20 alone, and boroughs planning to reduce earmarked reserves by a third, it is clear that without a real-terms increase in funding in the next Spending Review, more councils could start to fail.

17. London boroughs have managed by protecting their most vulnerable residents from the consequences of austerity, continuing to invest in children’s services and have insulated spending on adult social care as far as possible. However, other areas have seen major cuts in spending; for example, planning and development, and highways and transport services have seen cuts of around 60%.

18. London boroughs have reduced the number of employees by 46,464 (25%) since 2010, implemented radical restructuring and transformation plans, invested in demand reduction, renegotiated contracts, shared back and front office services and embraced commercial opportunities. The limit of what is possible through efficiencies is drawing closer.

19. In summary, if lessons are to be learned from the past decade of changes to local government funding, the Government should:
   - Increase the overall level of funding for local government at SR19.
   - Fully assess the cost implications of new burdens and other responsibilities that have been passed to local government in recent years.
   - Improve transparency by being clearer about how business rates revenues are used to fund different grants to local government.
   - Be less centrally prescriptive and devolve more control over funding to local government.
   - Take a longer-term funding approach to promote more strategic investment in prevention.

20. As the sector moves to 75% retention of business rates, and with the implicit government expectation that councils will now raise council tax, the future sustainability of local government funding is increasingly about the sustainability of council tax and business rates. Arguably, neither tax is fit purpose.
Council tax

21. There has been a growing chorus of voices calling for reform of council tax in recent years. The key criticisms of the tax include: its regressive nature; the continued use of 1991 valuations; the lack of buoyancy of the tax and responsiveness to changes in property values; the lack of transparency – with few people understanding where their tax goes; hypothecation through the Adult Social Care Precept (ASCP); and the fact it taxes occupancy not ownership of property – leading to anomalies such as with students, who have mandatory exemptions, while their commercial landlords pay no tax.

22. London Councils is opposed to the principle of capping council tax increases and urges the Government to remove the referendum limit completely, allowing councils to address spending pressures as locally appropriate. No central government tax is subject to the same referendum principle. We are also concerned that the ASCP represents unnecessary central control over local policy-making and urge the Government to fund adult social care appropriately through the spending review rather than any further hypothecation of the tax.

23. We recognise that fundamental reform (e.g. full revaluation) is unlikely in the near future. However, we urge the Government to consider some smaller technical reforms that could potentially benefit the sector including:

- revaluation of CT bands or the ability to determine additional bands locally;

- greater flexibility over CT Support which, despite being “localised” in 2013, continues to include central government prescriptions over eligibility.

Business rates

24. In an increasingly online retail world, the business rates system is becoming less sustainable as a business tax and, arguably, as the basis for funding almost half of local government spending. The tax base has been consistently eroded at successive fiscal events in recent years. For example, the change in indexation from RPI to CPI in 2017, reduced the potential tax take - and therefore funding of local services - by a cumulative £80 billion over the next 20 years.

25. As such, London Councils believes that any further reforms of the tax – or consideration of long-term replacements such as an online tax - must take the impact on funding for local government into consideration.

26. With regard to the business rates retention, London Councils and the GLA have long called for greater devolution of business rates. Our long-term goal is to have full control over the setting and distribution of business rates in the capital. London

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1 Including from LGA/CIPFA, the London Finance Commission, SOLACE, the Resolution Foundation and IPPR amongst others.

2 In particular see our joint response to the 2016 consultation on 100% retention: https://www.local.gov.uk/sites/default/files/documents/london-councils-and-gla-j-fde.pdf
Government has shown it can work collaboratively by delivering a successful business rates pilot pool that has delivered almost £200 million of direct strategic investment – and leveraged a further £650 million that would not have happened otherwise – in housing, regeneration, skills, transport and digital infrastructure across the capital. We see the current pilot pool as stepping stone to 100% retention in the next parliament. As such, we are concerned that the current proposals for the “full” 75% retention scheme from 2020 do not hold enough of a direct financial incentive for areas to pool business rates.

27. London Councils urges the Government to:
   - use the Spending Review to review the sustainability and appropriateness of council tax and business rates as the primary funding mechanisms for local government; and
   - ensure there are incentives for pooling under the full 75% scheme.

Options for widening the available sources of funding

28. Simply transferring more funding from central to local government or reforming the two main taxes is not enough. We believe local government should have access to a broader range of freedoms, flexibilities, and revenue raising powers, rather than exposing them to the flaws of any one, centrally prescribed, tax. This is the only way London will be able to manage the expected growth in demand for public services as the population grows to over 10 million by 2035.

29. The Spending Review provides the opportunity for the Government to devolve more to areas that have a track record of collaborating across boundaries and have robust governance arrangements in place. Cities, and urban areas more broadly, are well placed to take advantage of smaller specific taxes that will directly support local economic growth, such as a Tourism Levy, Vehicle Exercise Duty, or the Apprenticeship Levy.

30. In the long term, we continue support the recommendations of the London Finance Commission 2017, which called for London Government to have access to a greater range of taxes including the full suite of property taxes. More radically, it recommended assignment of a proportion of national taxes, such as income tax and VAT. The Institute for Fiscal Studies also recently concluded that the income tax is a good candidate for local assignment\(^3\), and we would welcome further exploration of this idea with government.

TR3 - How funding needs of local government are assessed. The current and forecast funding needs of local government and how these needs can be better understood at both a national and local level.

31. It is clear that the way in which previous assessments of funding need have happened between government departments and HM Treasury prior to recent Spending Reviews have failed to take a holistic view of the needs of local

\(^3\) [https://www.ifs.org.uk/publications/13991](https://www.ifs.org.uk/publications/13991)
government. The failure to adequately fund adult social care over the current Spending Review period is clear evidence that the process of assessing needs has not been sufficiently robust and suggests the Ministry (and other spending departments) have not carried enough weight in their representations to HM Treasury.

32. The NAO report into the financial sustainability of local authorities in 2018 concluded that the approach taken by MHCLG had improved at SR15, but found the Government does not have a long-term funding plan for local authorities, and that the funding landscape following the 2015 Spending Review has been characterised by one-off and short-term funding initiatives.

33. We urge the Government to learn the lessons of the current SR period, and in particular for MHCLG to work closely with the other key departments that fund local government, namely: DHSC; DWP; the Home Office; and DfE. The new and unfunded burdens and cost shunts (described in paragraph 7) must be reassessed and the impact of legislation, such as the Children and Families Act 2014, should be revisited as they will continue to adversely impact on the financial health of the sector if left unaddressed.

TR4 - The approach the Government should take to local government funding as part of the 2019 Spending Review, what the key features of that settlement should be, and what the potential merits are of new or alternative approaches to the provision of funding within the review.

The approach the Government should take at SR19

34. As stated above, it is imperative that local government sees an increase in funding at SR19: anything otherwise would risk widespread financial and service failures. This must be informed by a cross-department approach led by MHCLG that includes all major spending departments.

The key features of that settlement

35. The key features of the funding settlement should be to prioritise the sector-wide funding pressures in children’s services and adult social care so as to avoid having to repeat the emergency funding interventions required over the SR15 period.

36. In addition, there are a range of specific pressures facing urban areas like London that require the Government to take a more nuanced approach. These include the costs of homelessness, and those associated with greater population migration (for example the UASC and people with NRPF).

37. With 55,000 households in temporary accommodation (68% of the national total) London’s homelessness crisis is driven by a complex and unique mixture of factors

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5 More detail, and London Councils’ key priorities for the Spending Review, can be found in London’s Local Services: Investing in the Future: https://www.londoncouncils.gov.uk/our-key-themes/local-government-finance/london%E2%80%99s-local-services-investing-future/london%E2%80%99s-local
including the rapid rise in house prices and private sector rents, cuts to benefits, rising in-work poverty and a significant increase in the duties owed by local authorities to a broader range of individuals in need of help. This requires the Government to take a cross departmental approach at the Spending Review that takes account of welfare reform and other longstanding polices that impact on homelessness numbers. We are calling on the Government in the Spending Review to work with London Government to deliver London-specific solutions to its homelessness crisis and meet the funding shortfall of at least £170 million in London.

**Merits of new or alternative approaches to the provision of funding**

38. We believe that councils are best placed to take decisions about the services that impact their local communities and that given more responsibly for their own destiny, and more accountability for their own success, would design better taxes and provide better services.

39. Evidence from the OECD suggests that fiscal decentralisation can help reduce regional imbalances as it provides a strong incentive to use available economic resources more efficiently. Other international evidence suggests that fiscal devolution also has positive impacts on accountability, business mobility, resilience, fairness and efficiency\(^6\).

40. With the capacity of the civil service likely to be reduced for the medium term at least as the UK national government takes on new responsibilities following exit from the EU, we believe it is more important than ever for central government to change how public services are delivered locally by devolving power, lifting central constraints and taking a place-based holistic approach to funding public services.

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\(^6\) [https://www.london.gov.uk/sites/default/files/devolution_-_a_capital_idea_lfc_2017.pdf](https://www.london.gov.uk/sites/default/files/devolution_-_a_capital_idea_lfc_2017.pdf)