Executive Summary

- The overall quantum of funding for local government is insufficient.
- Local Authorities (LAs) have generally tried to protect services. This has included through the use of reserves, and although unsustainable in the medium term, to date this has often ‘disguised’ the serious nature of the underlying financial pressure and its ultimate impact on service users and residents.
- Funding needs to be seen in the round and recognise the important role that Government departments other than MHCLG have in funding (or underfunding) Local Authorities.
- Changes to funding that significantly affect Local Authorities (irrespective of government department) should be subject to appropriate impact assessments and an implementation delay to allow for effective planning by LAs.
- The current allocation of funding is out of date and inequitable, this is evidenced both by the disproportionate number of upper tier, and in particular shire counties, facing the most significant financial problems and by the, sometimes extreme, variation in council tax levels.
- A transparent, forward looking, evidence-based system for allocation of funding is essential.
- Even ignoring the very significant issues of complexity and the existential challenges to the Business Rates system in the 21st century economy, the Business Rates Retention approach has the fundamental flaw that changes in the level of business rates income bear no relation to changes in demand for core local authority services.
- Council Tax is a broadly regressive funding mechanism with no natural ‘buoyancy’ which limits its flexibility to respond to cost and demand pressures. At a minimum there must be an urgent revaluation of the Council Tax base and consideration of increasing the number of charging bands.
- Councils are exploring other ways of raising revenue including commercial activities but these bring a higher degree of risk and uncertainty to the funding of key services and tend to increase inequity because some authorities, often simply through location, have disproportionately higher opportunities to generate this funding.
- Cost pressures as well as demand pressures are significant elements in local authority financial difficulties, there is a need to understand and reflect those in a more meaningful way. This is particularly true in relation to the higher costs of rural service delivery.
- The uncertainty about future funding makes effective medium term financial planning extremely challenging.
- Similarly, short term crisis-response government funding does not enable the long term strategic planning which is essential to sustainable local authorities. There is also now a key dependence on these funding sources (particularly Better Care Fund) but considerable uncertainty about their longevity.
- Incentive-based funding, in the context of very limited overall resources, does not always offer best value for money and diverts resources away from the areas of highest spending pressure.

Introduction

1. North Yorkshire County Council (NYCC) serves England’s largest county with an area of 8,654 km² and a resident population of 611,000. Many of the issues the county faces will be familiar to other Local Authorities such as social care demand from a rapidly ageing population, growing numbers of children with special needs and areas of significant deprivation. But NYCC also has more unique challenges, in particular the very significant extra costs of delivering services in a large, sparsely-populated rural area. These rural cost pressures arise from a number of factors which are covered in more detail in Para. 23.
2. NYCC is generally viewed as a successful council with a good reputation for service quality and innovation, including being the only LA in England to receive an ‘outstanding’ ranking for all elements of its children’s services in a recent OFSTED inspection. It is also recognised as being effective in managing its resources leading a recent Local Government Association peer group assessment to commend NYCC’s “tremendous grip on its budget”. Despite these strengths, and a leadership which identified and acted promptly on the emerging funding issues, NYCC is facing significant financial challenges.

3. The Local Government funding regime is also subject to an unprecedented level of change through CSR 19, the Social Care Green Paper, the Fair Funding Review and Business Rates Retention. Each one of these in isolation would represent a level of challenge but collectively the level of uncertainty, particularly given the many unresolved issues, makes it extremely difficult to undertake any meaningful longer term financial planning.

4. We are grateful for the opportunity to contribute to this inquiry and we commend the Select Committee for helping to raise the profile of the significant financial pressures that local authorities face.

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.

5. Since austerity began Local Government has seen some of the most severe cuts in funding of any part of the public sector. It can seem that passing the cuts (and the buck) to local authorities is easier than making difficult decisions on other areas of central government spending. NYCC would welcome a process where the Department is more explicitly held to account for performance across the whole sector which may encourage more collaborative working with local authorities.

6. Despite these significant funding reductions, as a general rule, councils have been very effective in trying to minimise the impact on residents and service users. This has included significant efficiency and transformation measures. For example, at NYCC there has been a requirement to make almost £160m of savings to the end of 2018-19. Only £40m has impacted directly on services. However, significant further savings are still required and inevitably it becomes increasingly difficult to find savings that do not impact on service users.

7. The impact on services has also been to some extent ‘masked’ to date because councils have used their reserves to maintain services, particularly in the high demand areas such as adult social care. This is clearly not sustainable in anything other than the short term and there are signs of a number of local authorities reaching a critical tipping point in terms of their financial sustainability. This has been principally in councils with upper tier responsibilities and has been particularly marked in shire counties which indicates issues around lower relative funding levels for this category of local authority. Overall the LGA estimate a funding gap of £3bn in the current financial year rising to over £8bn by 2024/25.

8. We also have major concerns that the cuts to local government have been applied with little or no evidence of impact assessments being undertaken and with no reference to, or apparent understanding of, the demands or pressures on local government. This is compounded because of the complexity of the different funding sources for LAs. This means
the decisions of a number of government departments impact on local authorities but there is no overall coordination of this funding or understanding of the interrelationship between different funding streams.

9. In terms of direct funding MHCLG itself is now a minority funder of local government. For example in the case of NYCC the authority will receive no Revenue Support Grant in 2019/20 and of the £78m (excluding Direct Schools Grant) expected in government grants only 15% will come directly from MHCLG. So decisions from other government departments, particularly the Department of Health and the Department for Education, have critical impacts on the sustainability of local authorities. Unfortunately their understanding of the wider impact of their decisions on the sector sometimes seems limited. They also do not see the consequences of their funding decisions because they often do not directly impact on the policy areas they have responsibility for, e.g. High Needs budgets. The underfunding of these budgets by the DfE is not impacting significantly on the Department’s performance or reputation because the shortfall is being ‘subsidised’ by local authorities from their core funding which in turn impacts on other service provision. For example NYCC has had to put over £11m into its base budget to offset the shortfalls in DfE funding for High Needs, a major issue because of the need to make corresponding additional savings elsewhere.

10. There has been some recognition of particular demand and funding pressures but these have usually been in the form of reactive, crisis-management short-term funding. Whilst this is generally welcome at the time, its one-off nature makes it impossible to plan effectively for the longer term. In some cases the decisions taken also show little understanding of the practical issues facing local authorities. As an example the short term funding for social care linked to winter pressures in hospitals that was transferred to LAs in autumn 2018. In the case of NYCC we received £2.4m late in 2018/19. Use of these monies in the year of receipt represented a full-year commitment of over £5.5m into 2019/20 but funding of only £2.4m was provided for that year. There is also now a key dependence on some of this ‘short term’ funding, particularly in the area of adult social care, but still significant uncertainty about whether resources like the Better Care Fund will continue into the longer term. Many, perhaps most, local authorities will be financially unsustainable if this funding is now withdrawn.

11. Whilst broadly welcoming the principle of local autonomy in funding NYCC does not believe that Business Rate Retention (BRR) is an appropriate means of funding future pressures on local government. As well as concerns about its long term sustainability (given the well documented issues round the future of the high street and competition from online business etc.) we do not see any link between the ability to generate additional business rate income and the level of demand for key services. The system is also increasingly complex which impacts on LAs confidence in forecasting and planning resources. Unless there is a credible, well-evidenced overarching funding framework which reflects a fair and objective view of funding, BRR will further exacerbate relative funding inequality.

12. Council Tax was not originally designed to do the ‘heavy lifting’ of funding local authorities but with the reductions in core government grant funding it has taken on a more and more

The efficiency, fitness for purpose and sustainability of the current system for funding local government (central government funding, council tax, business rates retention and other income); how it could be improved, including options for widening the available sources of funding; and what lessons can be learned from other jurisdictions

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significant role. However, it has major structural issues: it is not ‘buoyant’ so is not suited to flexibly responding to cost or demand pressures and it is a broadly regressive tax with bills bearing little relation to a resident’s ability to pay. At a minimum there should be an urgent revaluation of the Council Tax base and consideration of additional council tax bandings. MHCLG should also be open to a meaningful discussion of alternative funding options.

13. Local authorities inevitably show great variability, be that in terms of the wealth of their residents, their geography and the services that they require. Therefore, there will always need to be an element of redistribution within the system and it is this that becomes important in terms of achieving a fair distribution. A clear, fair and well-evidenced finance regime with explicit assumptions is the key to supporting effective financial planning by local authorities.

14. The impact of decisions by government departments other than MHCLG is another important factor in sustainable local government funding. As well as the direct issues of funding referred to in Para. 9, areas such as the Social Care Green Paper potentially have transformational impacts on local government sustainability. NYCC is particularly disappointed that the Green Paper has been further delayed but we would anticipate that, when eventually published, this should include a comprehensive analysis of alternative funding mechanisms for social care, e.g. social care insurance schemes.

15. Many local authorities are understandably turning to commercial ventures to generate additional income as an alternative to further spending reductions. This does however present a higher level of risk and uncertainty in the funding of essential services. In addition, and critical to the issues of equity and fairness in funding, some areas are disproportionately able to exploit these opportunities compared with others (e.g. poorer or more rural authorities).

16. Charging and user income are other factors and NYCC would welcome an open debate about the limits of discretionary charging and, in addition, how exceptionally high levels of ‘inelastic’ income such as car parking fees are reflected in financial allocations.

17. Within the context of limited public funding NYCC would also question the use of incentive funding, most notably New Homes Bonus. It is not clear if these are an effective use of limited resources and whether the results are driven by geography or providence as much as direct action leading to greater inequity in overall funding. New home building is already incentivised through higher council tax receipts so the double incentive of NHB does not seem a prudent use of limited funds particularly as the majority of the funding, in shire areas at least, does not go towards the service areas under the greatest pressure. The lack of certainty around these sources of funding also makes them largely unsuitable for funding core services.

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.

18. The current funding needs mechanism is outdated, complex and opaque. NYCC welcomes the commitment to the Fair Funding review although we remain concerned that it still relies on using past spending as a proxy for ‘need’, in many cases this simply reflects the relative level of funding available at that time. Therefore, it becomes a circular argument that the
factors explaining variations are those that influenced the original funding allocations. Linked to this, because shire areas were relatively underfunded through past funding mechanisms this has often meant a higher level of unmet need. By using past spend there is a danger of locking-in this inequity. Some of the anomalies of the current funding mechanism are shown in the graph below:

19. Much of the recent debate on Fair Funding within the sector has centred on arguments around the relative weighting of factors such as deprivation. Deprivation is clearly a factor in driving demand for some services but the fact it has a reduced potential weighting in the new funding formula is not in itself an argument against the new approach. It is important to recognise that the ‘status quo’ in terms of the current funding formulae does not represent an optimised model built on a solid evidence base. So, for example, the cost weighting for density is some eight times higher than for sparsity with little objective evidence for this comparative weighting. NYCC would welcome and support high quality research which attempted to objectively identify service need measures for different client groups. This should also be sensitive enough that it recognises specific pressure points for sub-sets of local authorities, e.g. high winter road maintenance costs for some, predominantly northern, councils.

20. The change to the methodology of distributing Revenue Support Grant in 2016/17, where actual council tax was substituted for notional council tax in the calculation, also had a major impact on funding. This effectively locked in the advantage of those, mainly London, authorities who through very high levels of government funding and other income were able to set very low council tax rates. NYCC, along with the vast majority of local authorities, would strongly support a return to notional council tax values in the calculation of net funding requirements.
21. If councils are to have confidence in understanding and planning their finances then there must be a transparent funding mechanism with explicit assumptions. As an authority NYCC would like to be able to clearly see how its allocations have been calculated and to be able to replicate that calculation and model it for different scenarios.

22. Cost pressures as well as demand pressures are a significant factor in local authority financial difficulties, there is a need to understand and reflect these in a more meaningful way in the overall funding arrangements (e.g. within the Area Cost Adjustment). For example, significant upward pressure on the cost of residential and nursing provision is one of the drivers of the escalating overspend pressures on many social care budgets. The average cost of a new nursing placement in NYCC in 2019 is 14% higher than an existing one. Factors such as these should be recognised in understanding the future funding needs of LAs, e.g. through a measure of the proportion of the registered beds in a local authority area that are purchased by the LA.

23. There has been a particular under-representation of the higher costs of service provision in rural areas. These arise from a number of factors including:

a) Higher unit costs because of the direct transport costs and higher unproductive time linked to longer distance travel. For example, social care teams covering urban areas in North Yorkshire cover seven clients for every four in the sparse rural areas
b) Workforce issues linked to an ageing population and the costs of rural living
c) The loss of economies of scale through the need for more, and smaller, specialist units
d) The lack of developed, competitive markets for service provision in many rural areas.

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.

24. Delays in the announcement of the 2019 Spending Review further exacerbate the difficulties for LAs in trying to undertake effective financial planning for the future so NYCC would encourage early publication ahead of the Autumn Budget.

25. The overall quantum of funding remains the most pressing issue in the context of financially sustainable local authorities and so we would anticipate additional real terms funding going in to the sector in the 2019 CSR. This should be based on an informed understanding of the key financial pressures on councils. This should be over and above the consolidation of the key time-limited funding sources (e.g. BCF) into the long term base funding for LAs.

26. There also needs to be a genuine multi-year settlement that allows local authorities to effectively plan for the longer term.

27. In future we would suggest that any proposed reductions in funding have a lead-in time before implementation to allow local authorities to properly plan their response

April 2019