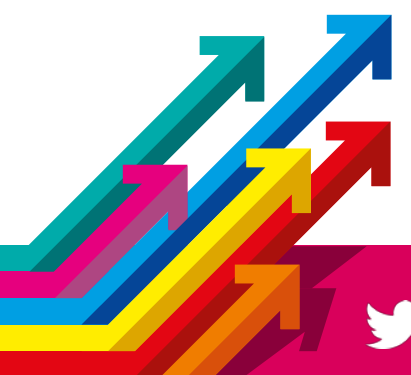


UNDERSTANDING THE COUNCIL FUNDING REVOLUTION

DAVID PHILLIPS

INSTITUTE FOR FISCAL STUDIES



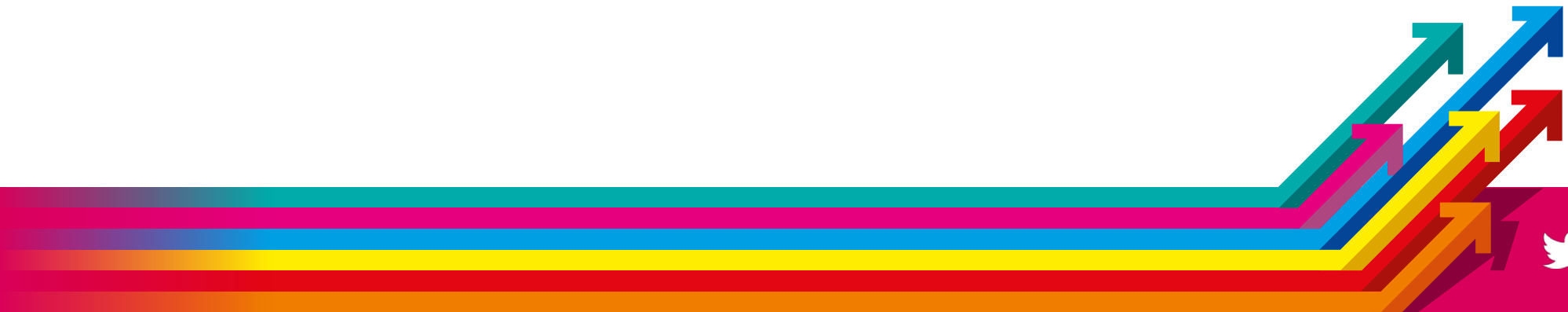
WE ARE IN MIDST OF COUNCIL FUNDING REVOLUTION

- ▶ Big cuts to overall spending power, driven by slashing of central government grants
- ▶ A major shift in emphasis from redistribution to the provision of financial incentives
- ▶ Having and will have impact on how funding is distributed between councils
- ▶ IFS has a major programme of research and analysis on this funding system revolution supported by:



- ▶ Today: the big picture and some thoughts on implications for councils investments and pensions

FUNDING CUTS

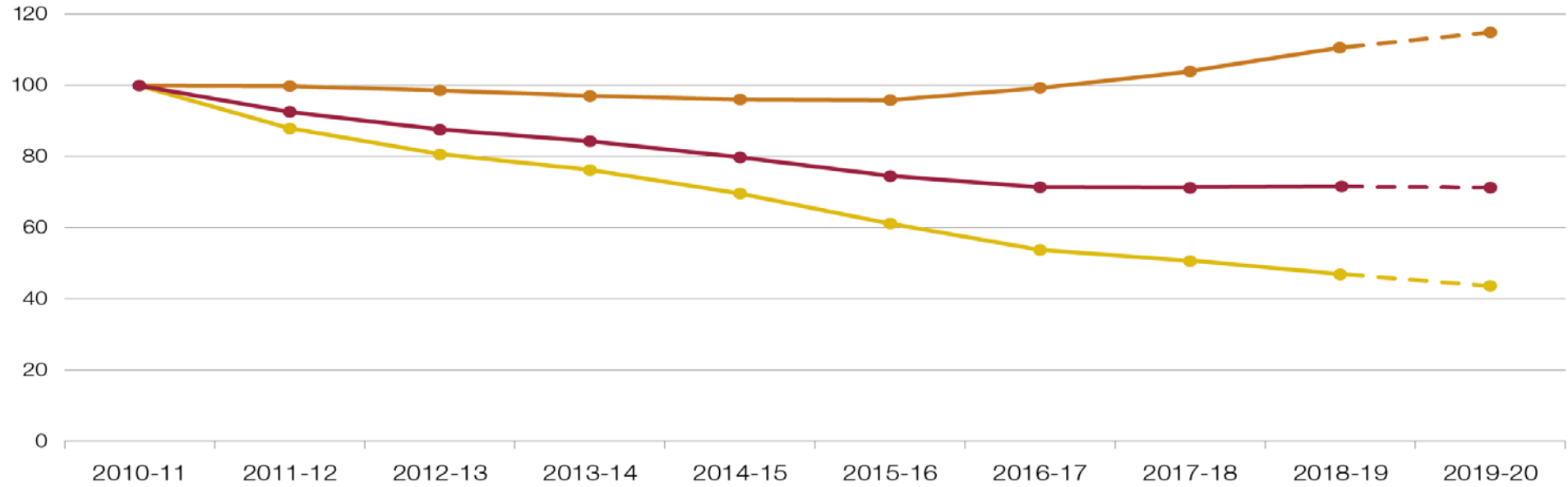


EIGHT YEARS OF CUTS...

Figure 1
Estimated change in spending power of local authorities in England, 2010-11 to 2019-20

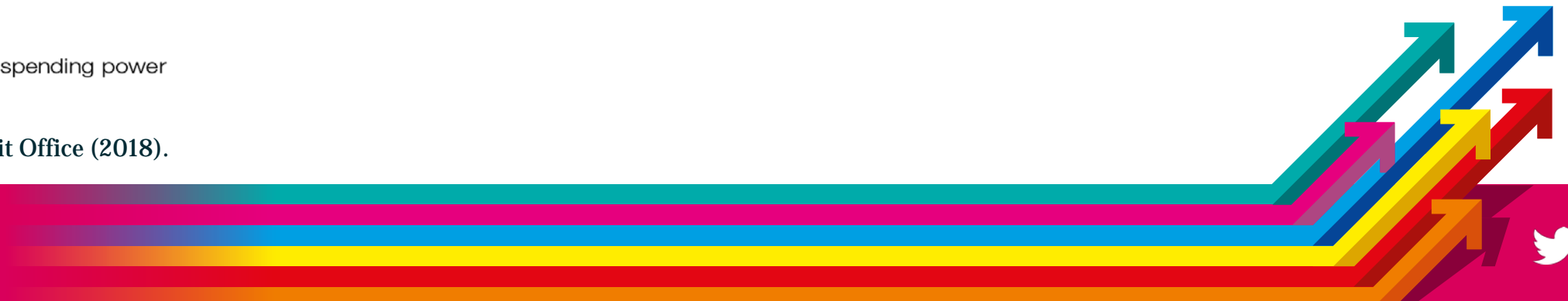
Previous reductions in spending power have largely levelled off but this is a combination of ongoing reductions in government funding and anticipated increases in council tax

Spending power (real terms in 2016-17 prices) (indexed: 2010-11=100)

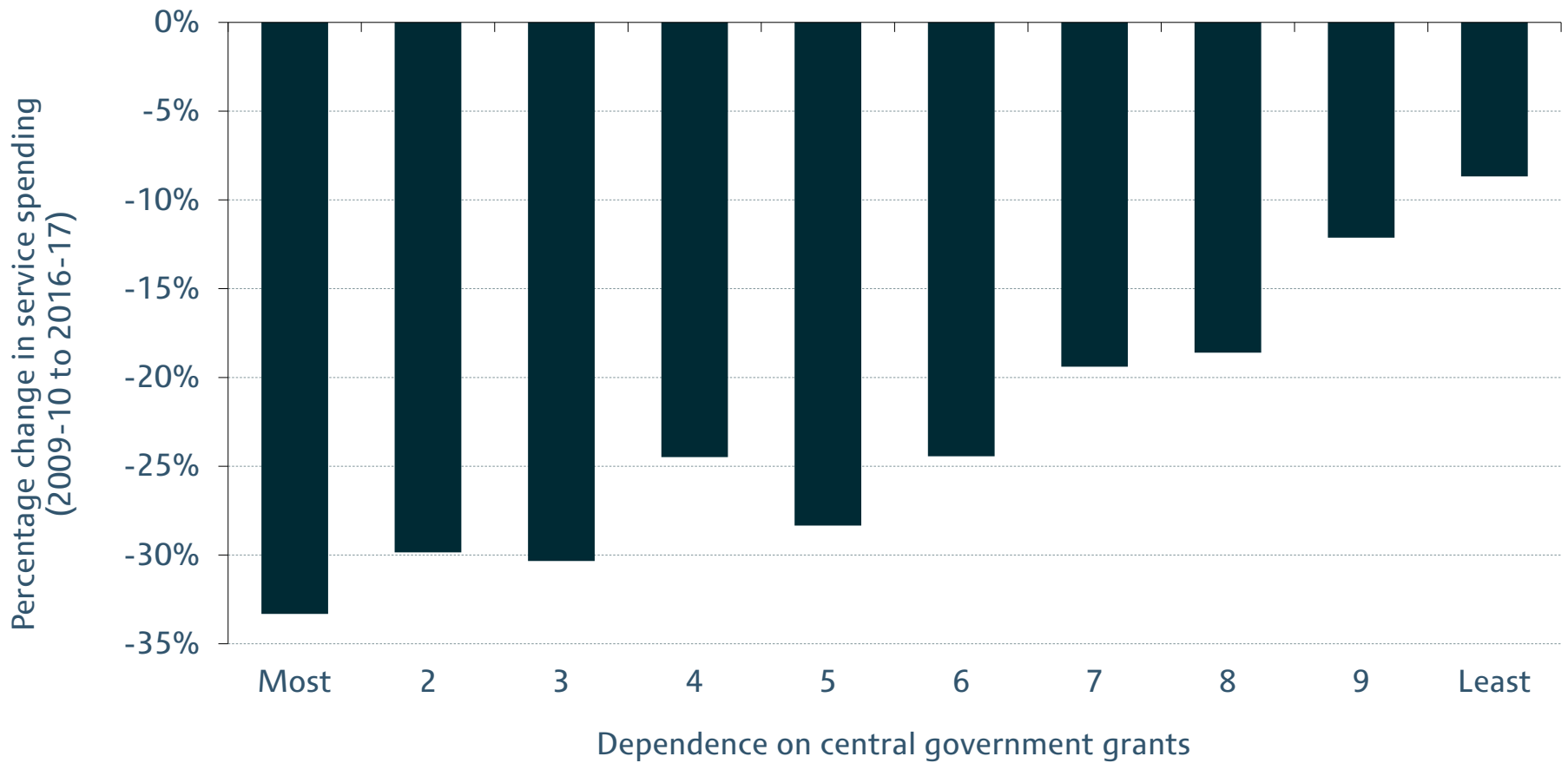


- Spending power
- Government-funded spending power
- Council tax

Source: National Audit Office (2018).



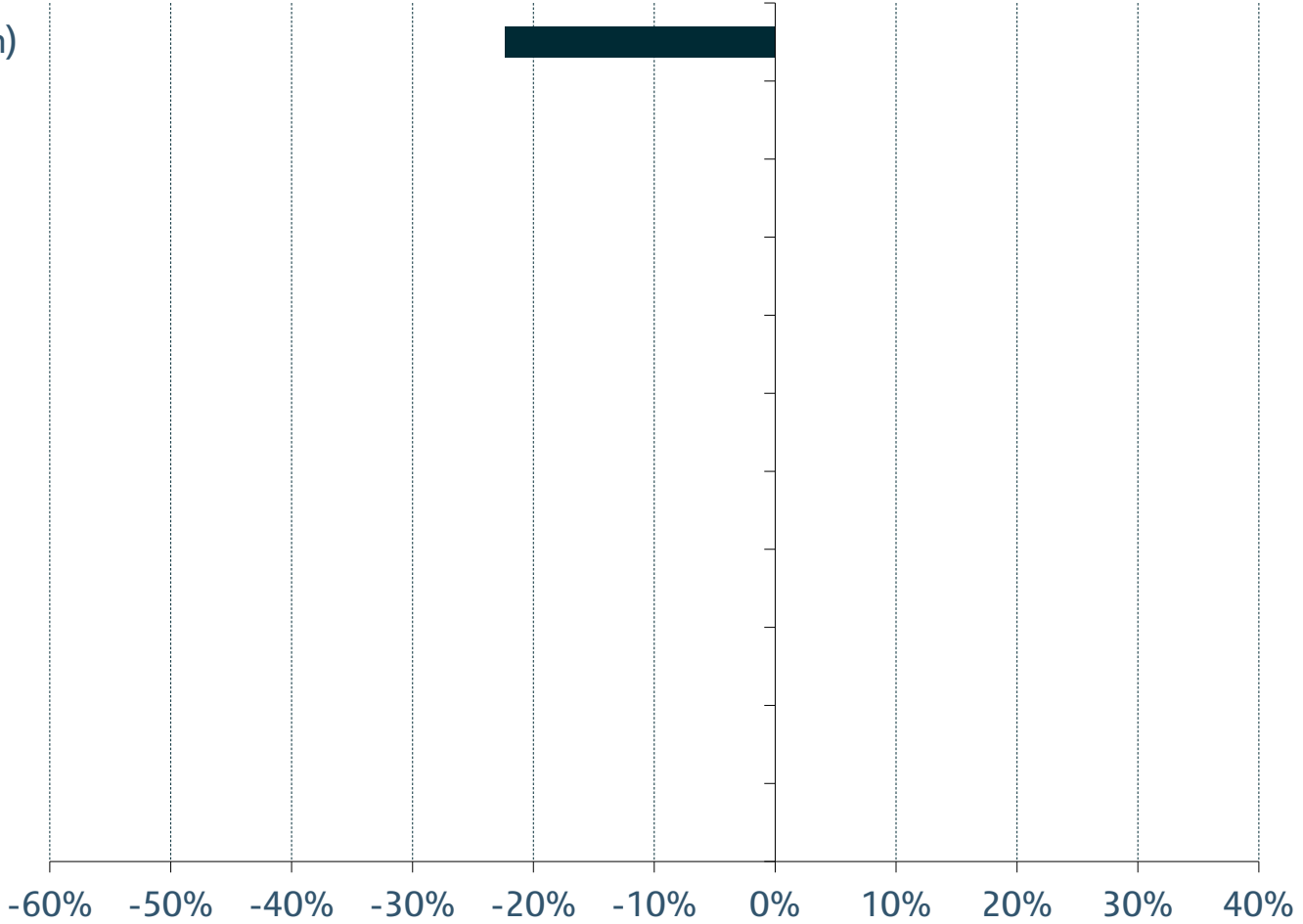
...BIGGER IN MORE DEPRIVED AREAS...



Source: IFS calculations using MHCLG revenue expenditure statistics.

...VARIED ACROSS SERVICES...

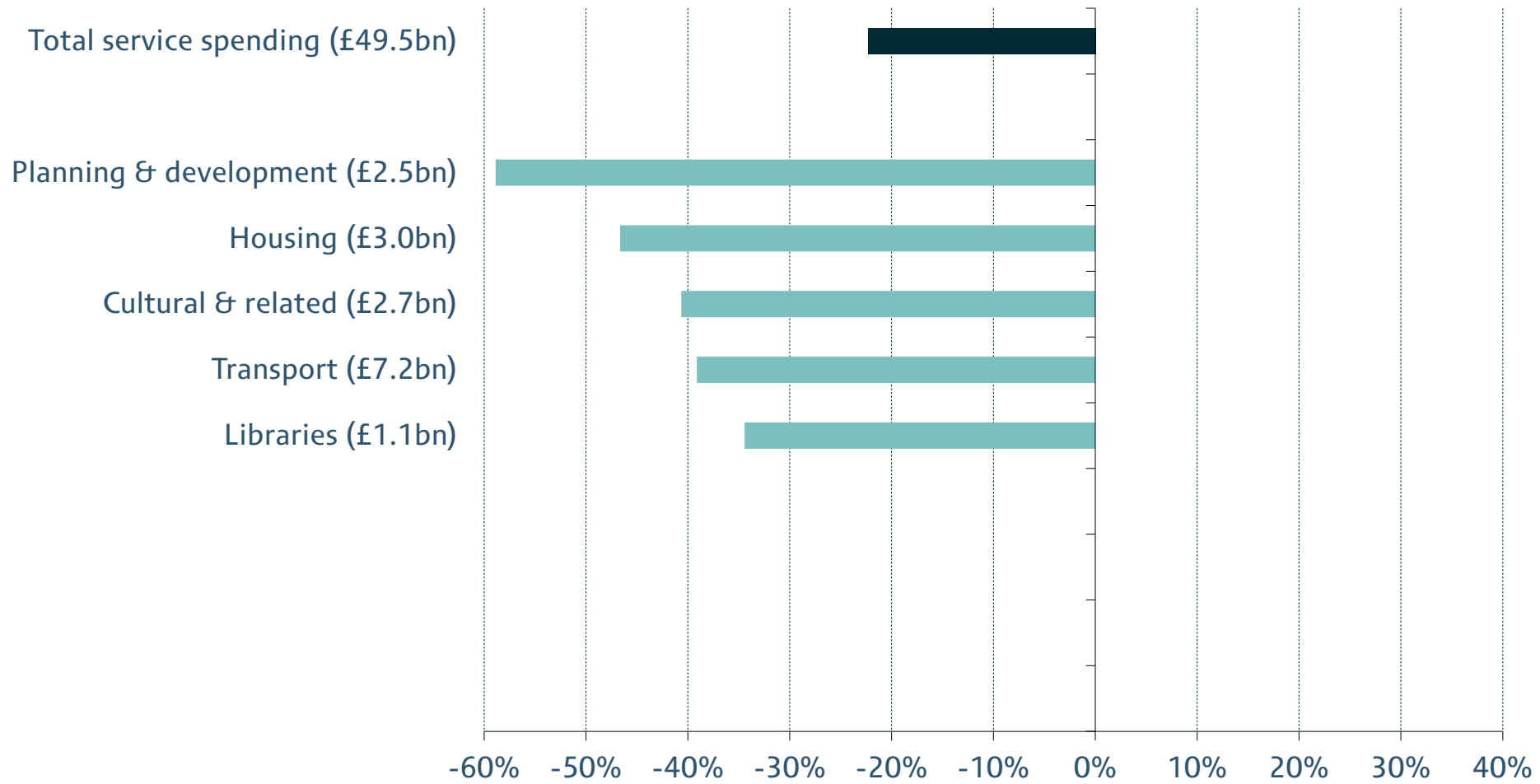
Total service spending (£49.5bn)



Note: Change in net expenditure on services, 2009-10 to 2016-17. Figures in brackets are spending in 2009-10.

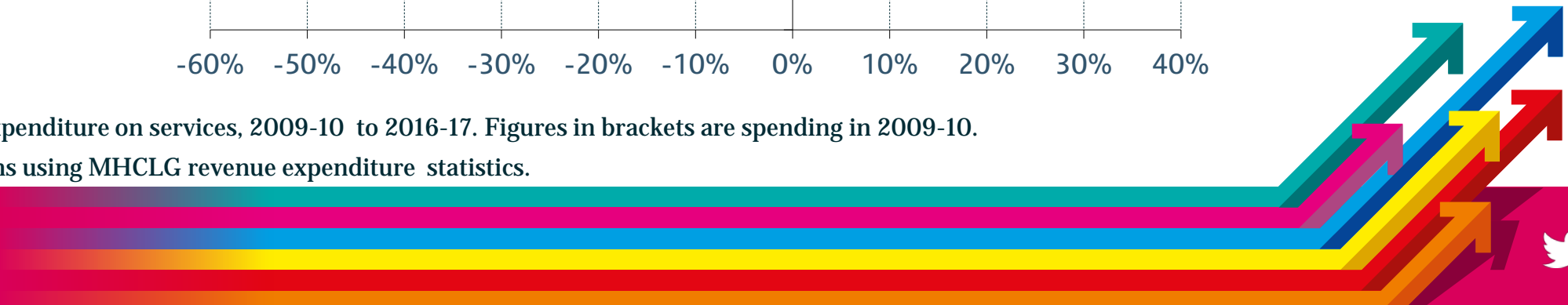
Source: IFS calculations using MHCLG revenue expenditure statistics.

...VARIED ACROSS SERVICES...

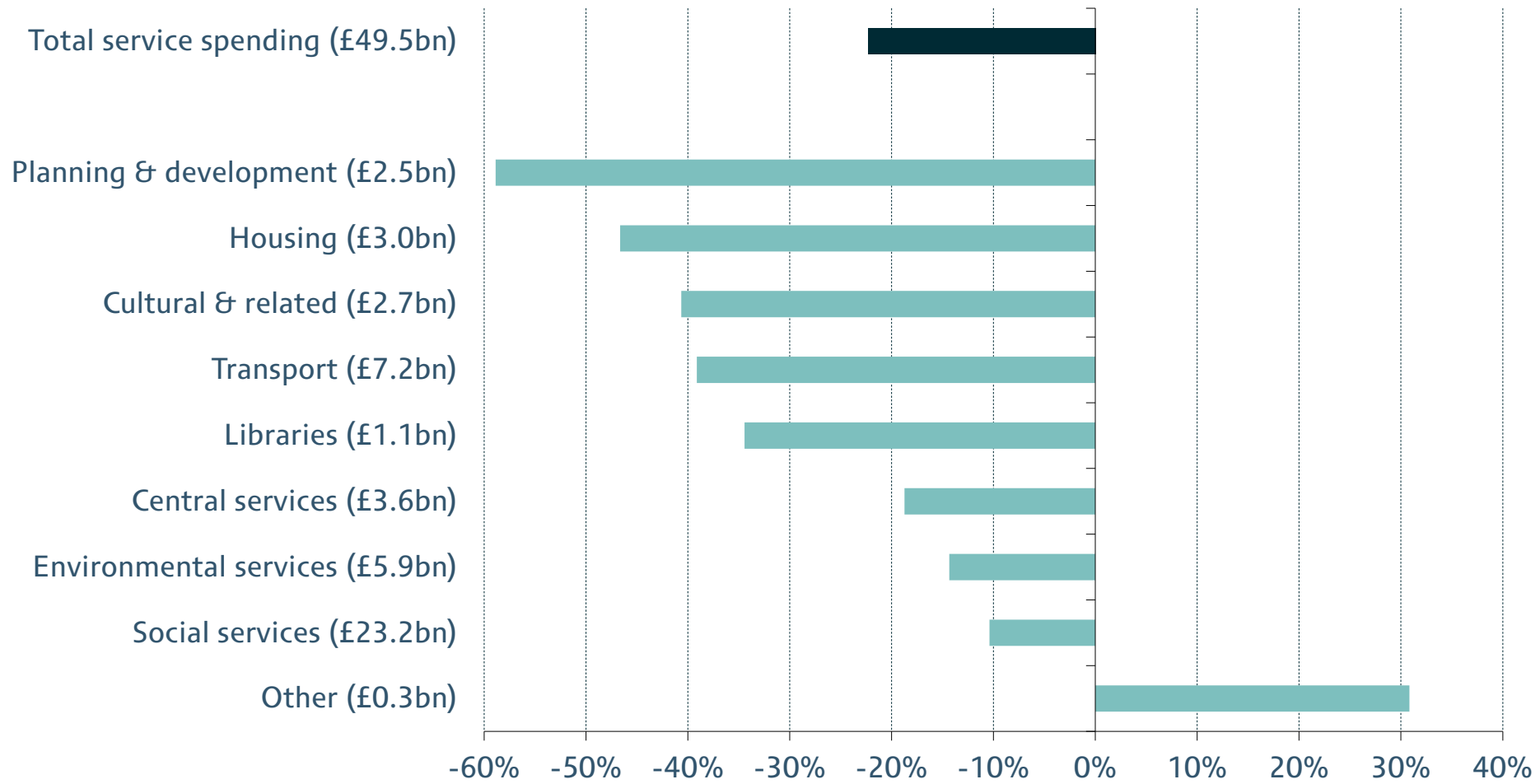


Note: Change in net expenditure on services, 2009-10 to 2016-17. Figures in brackets are spending in 2009-10.

Source: IFS calculations using MHCLG revenue expenditure statistics.

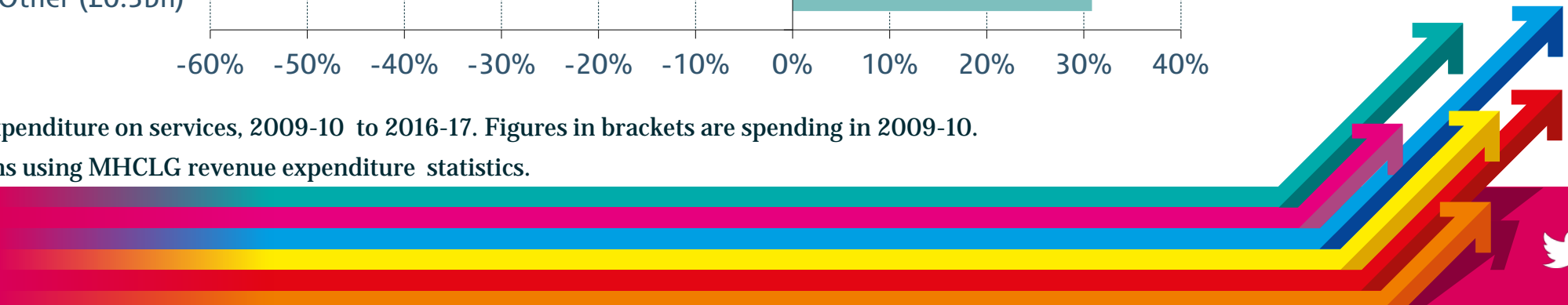


...VARIED ACROSS SERVICES...

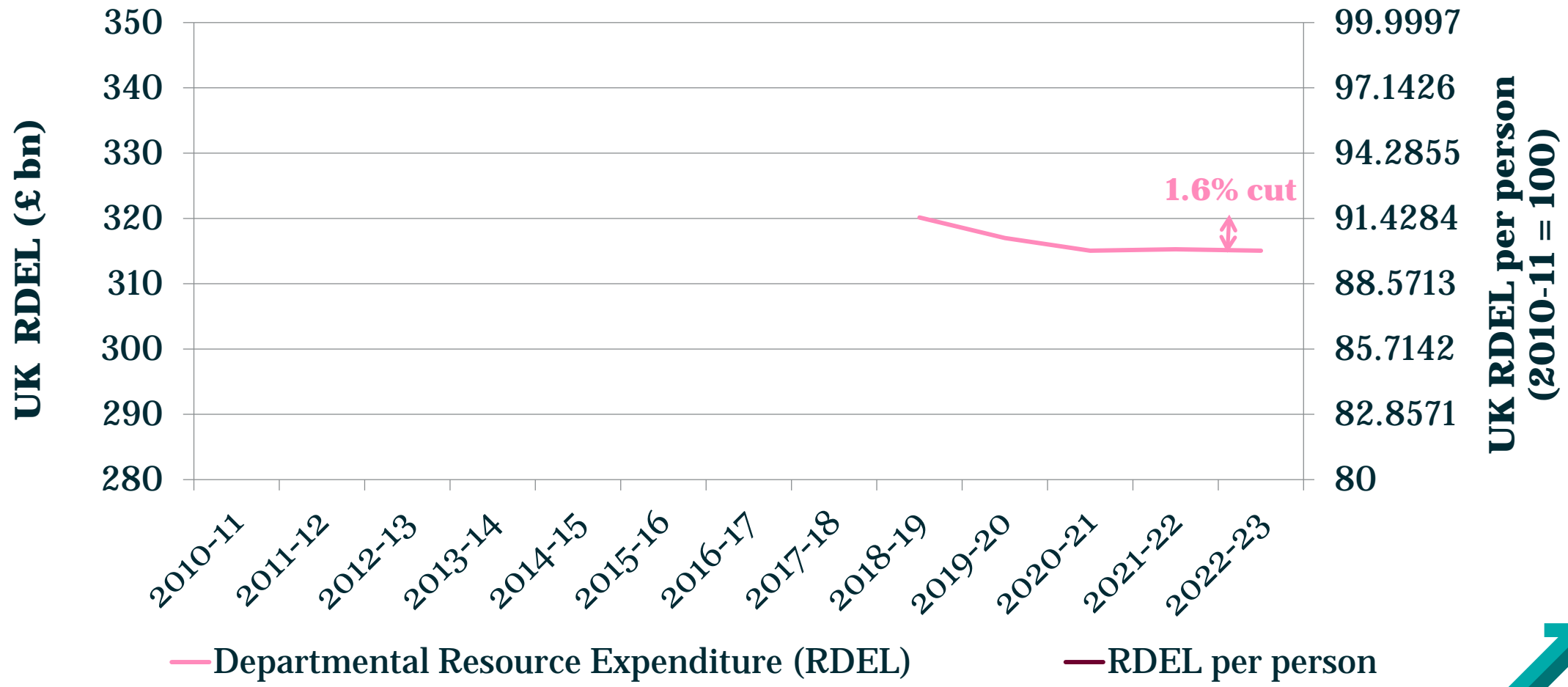


Note: Change in net expenditure on services, 2009-10 to 2016-17. Figures in brackets are spending in 2009-10.

Source: IFS calculations using MHCLG revenue expenditure statistics.



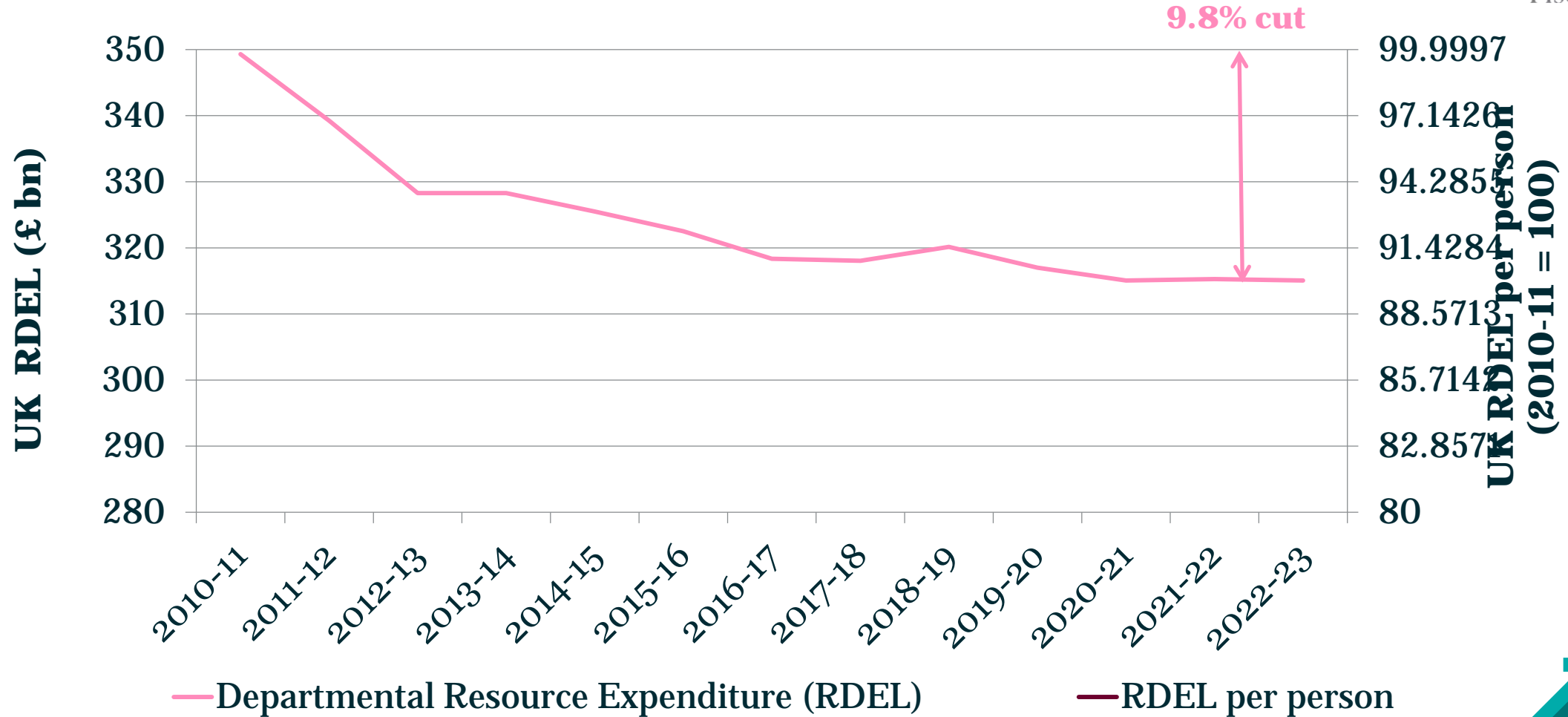
... WITH MORE LIKELY TO COME



Note: RDEL covers all departmental day-to-day spending not just local government spending.

Source: IFS calculations using OBR *Economic and Fiscal Outlook*, March 2018.

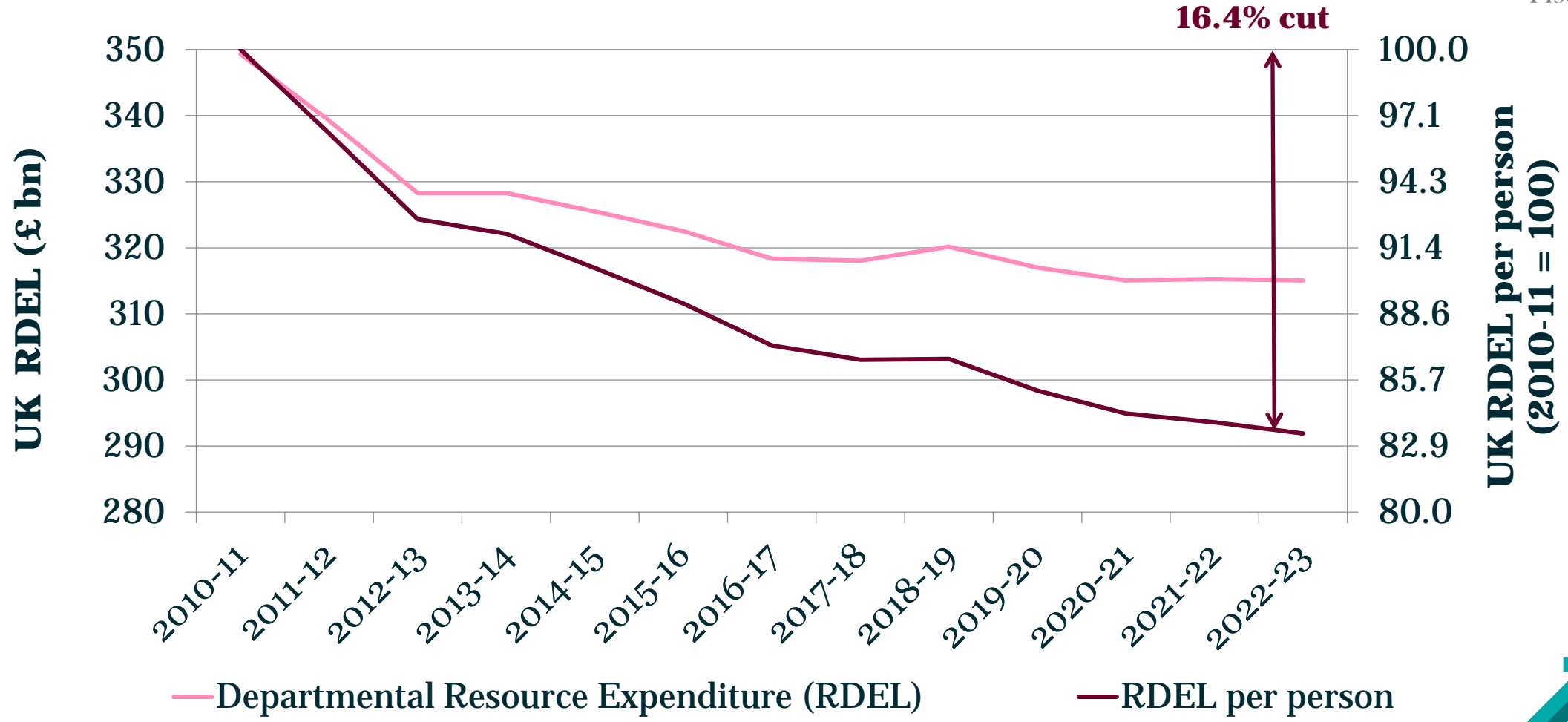
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Source: IFS calculations using OBR *Economic and Fiscal Outlook*, March 2018.

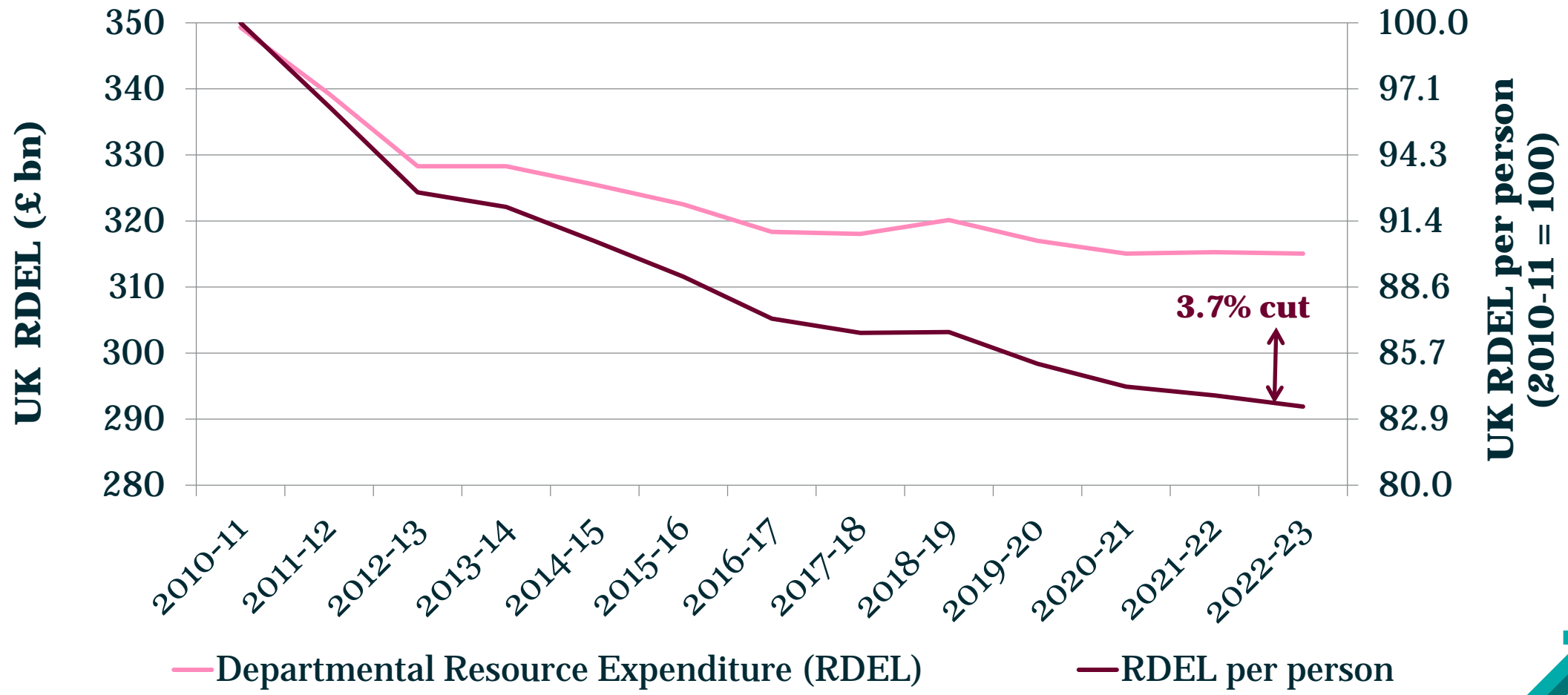
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Source: IFS calculations using OBR *Economic and Fiscal Outlook*, March 2018.

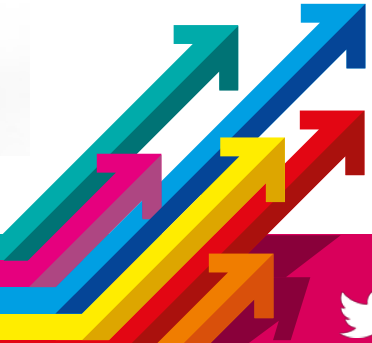
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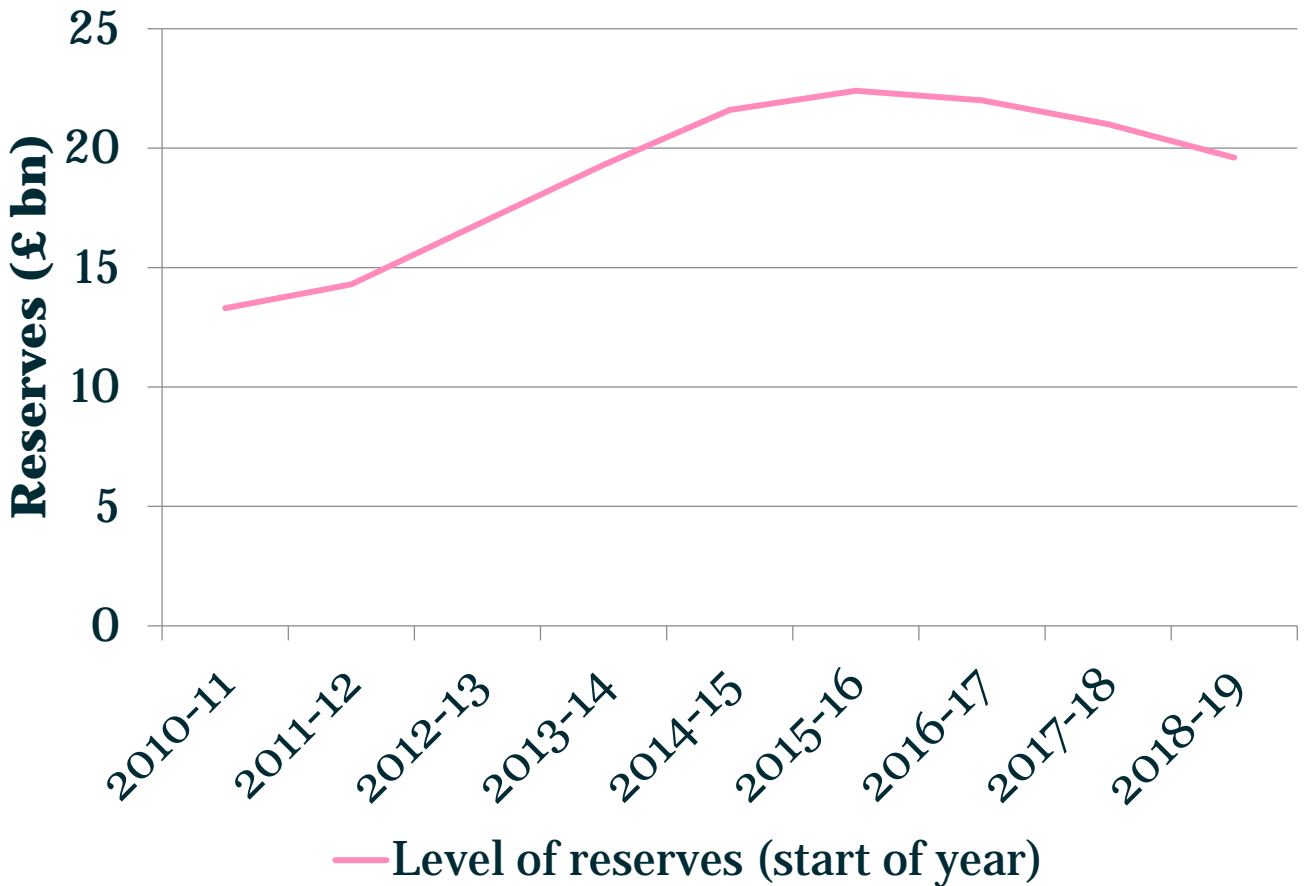
Note: RDEL covers all departmental day-to-day spending not just local government spending.

Source: IFS calculations using OBR *Economic and Fiscal Outlook*, March 2018.

COUNCILS DELIVERED CUTS DESPITE RISING COSTS

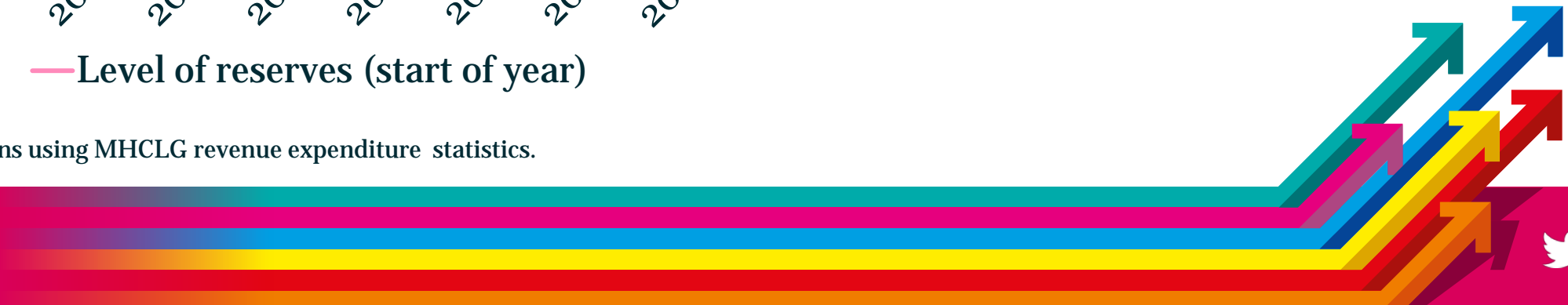


BUT EVIDENCE UPPER-TIERS FINDING IT TOUGH...



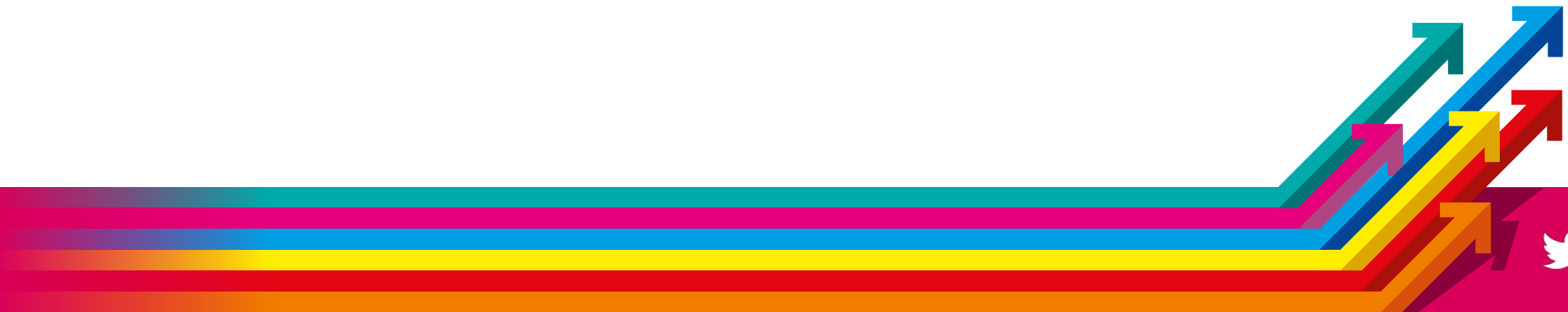
- ▶ 80% of counties, met and London boroughs drew down reserves in 2016-17
- ▶ Northamptonshire has ran out of reserves and 10% upper-tier councils could by 2021
- ▶ Only 30% of shire districts drew down reserves (paid in a net £200 million)

Source: IFS calculations using MHCLG revenue expenditure statistics.

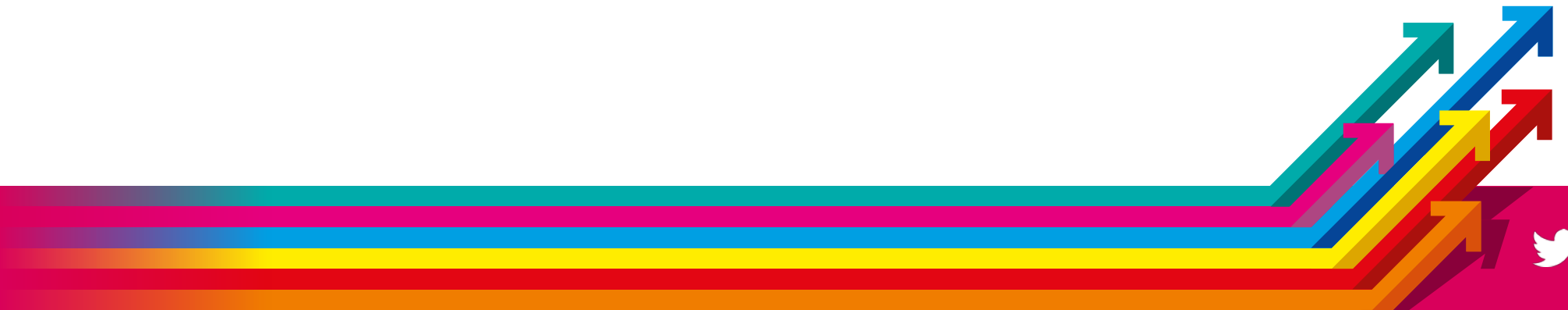


DIFFICULT TRADE-OFFS

- ▶ Squeeze suppliers?
- ▶ Higher fees and charges?
- ▶ Cut jobs?
- ▶ Hold down pay?
- ▶ Shift more pension cost to employees?



THE CHANGING FUNDING SYSTEM



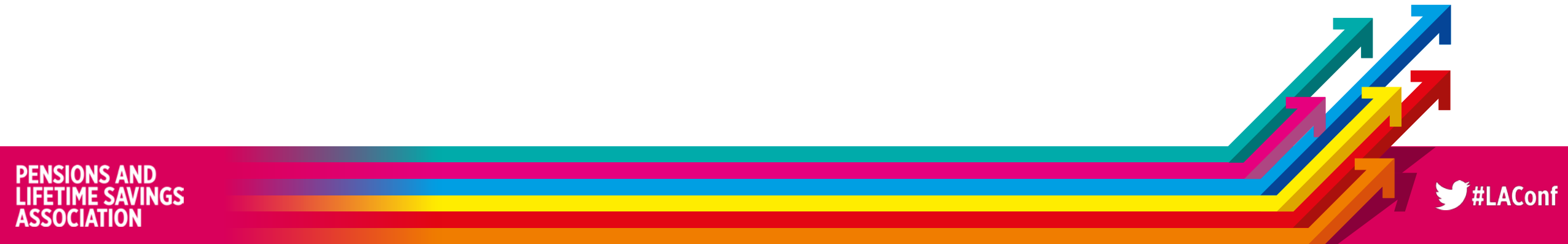
BIG SHIFT FROM REDISTRIBUTION TO INCENTIVES

- ▶ End annual updating of spending needs and revenue-raising potential
- ▶ Councils bear 50% of real-terms *changes* in business rates revenues
 - ▶ Plan for 75% in 2020 and half of England is piloting 100%
 - ▶ Plan to abolish general grant funding in 2020
- ▶ Councils pay low-income residents council tax bills
- ▶ Aim to incentivise councils to support economic growth, encourage development, boost business and tackle poverty
- ▶ But also risk of divergences in revenues that are outside councils' control
 - ▶ Factories and shops do close and people do lose jobs



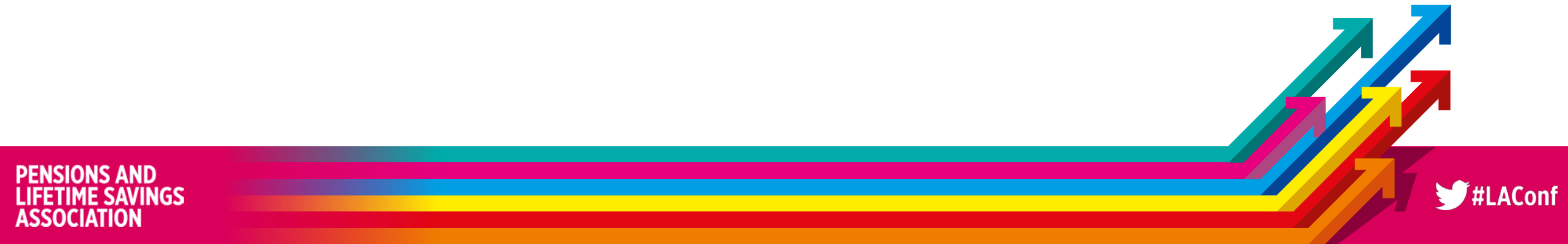
WHAT ARE THE IMPLICATIONS OF THESE CHANGES

1. Inconsistency between finance and other policies (e.g. adult social care)
2. Changed incentives for investments and possibly pensions

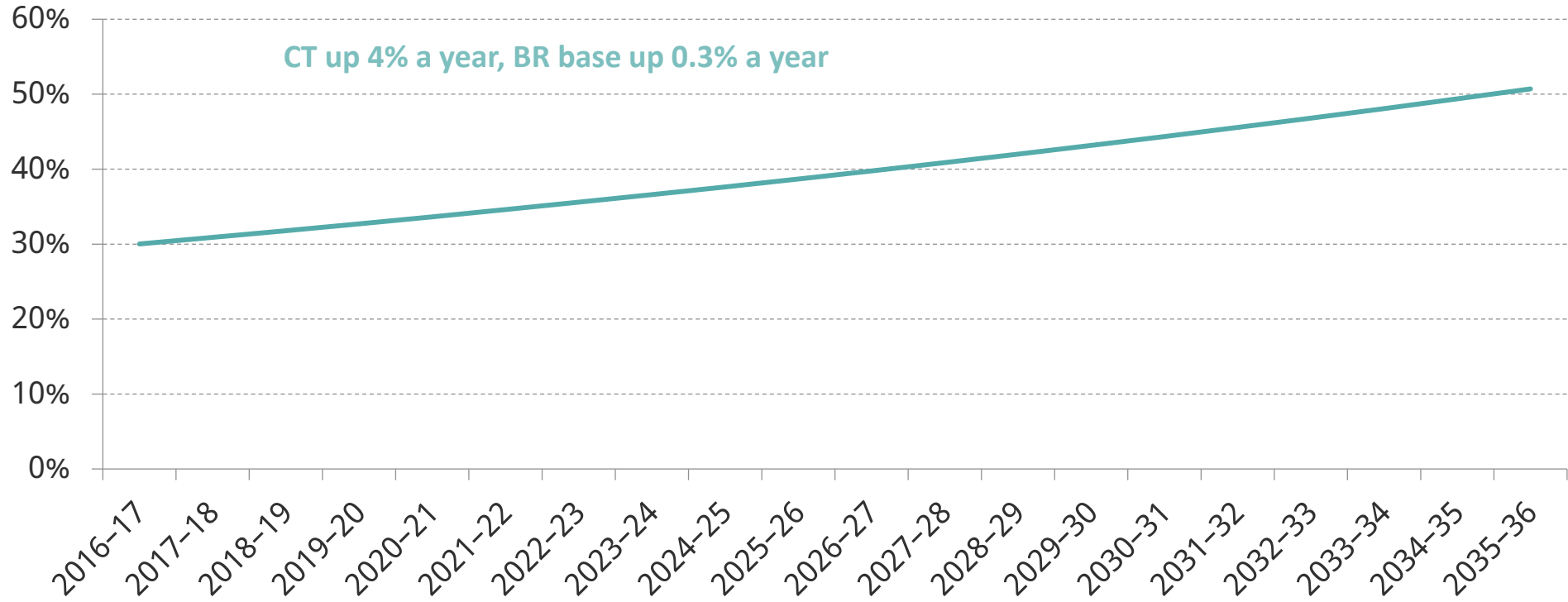


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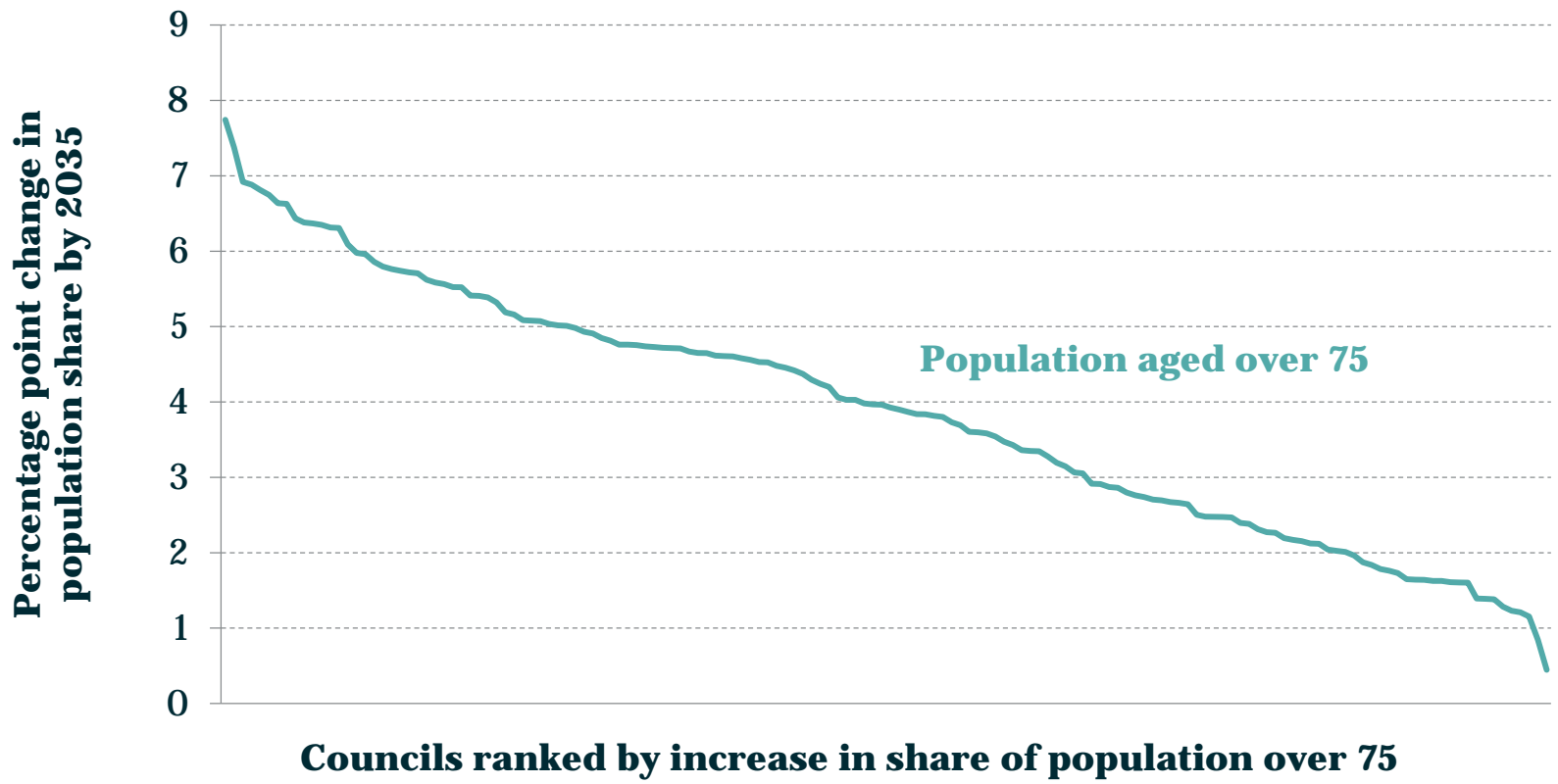


ADULT SOCIAL CARE SET TO TAKE UP MORE AND MORE OF COUNCIL TAX AND BUSINESS RATES REVENUES

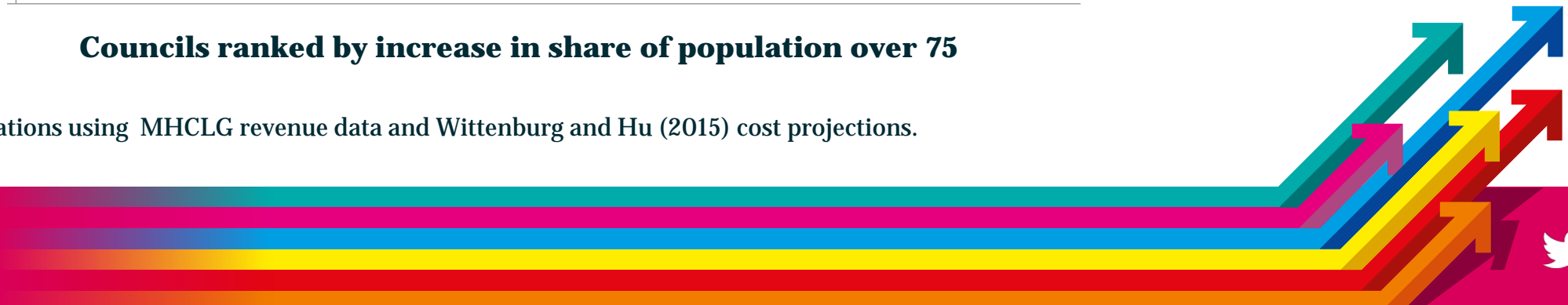


Source: IFS calculations using MHCLG revenue data and Wittenburg and Hu (2015) cost projections.

REVENUES AND DEMANDS LIKELY TO CHANGE DIFFERENTLY IN DIFFERENT AREAS



Source: IFS calculations using MHCLG revenue data and Wittenburg and Hu (2015) cost projections.

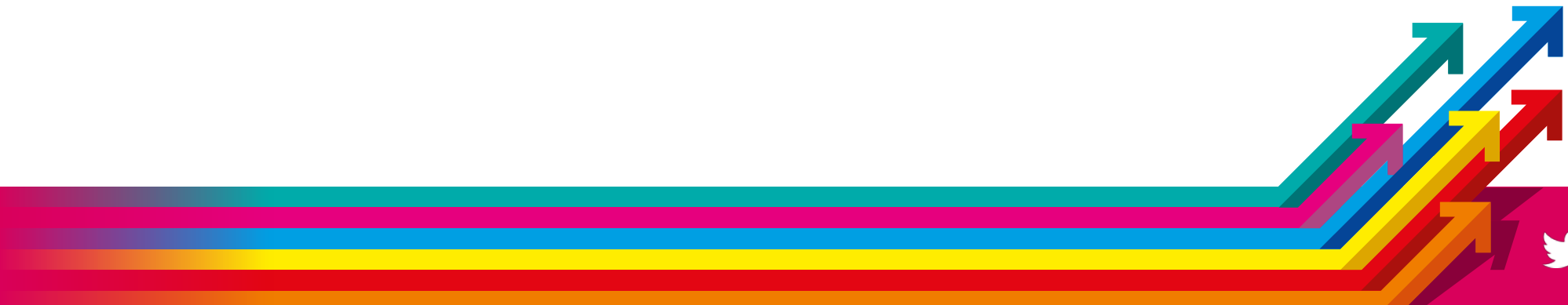


BUT GOVT WANTS MORE CONSISTENT SERVICES



Part of [our plan] will be tackling the unacceptable variations in quality and outcomes between different services and different parts of the country

Jeremy Hunt,
Health and Social Care Secretary



RECONCILING TENSIONS COULD LEAD GOVT TO CENTRALISE ADULT SOCIAL CARE SERVICES...

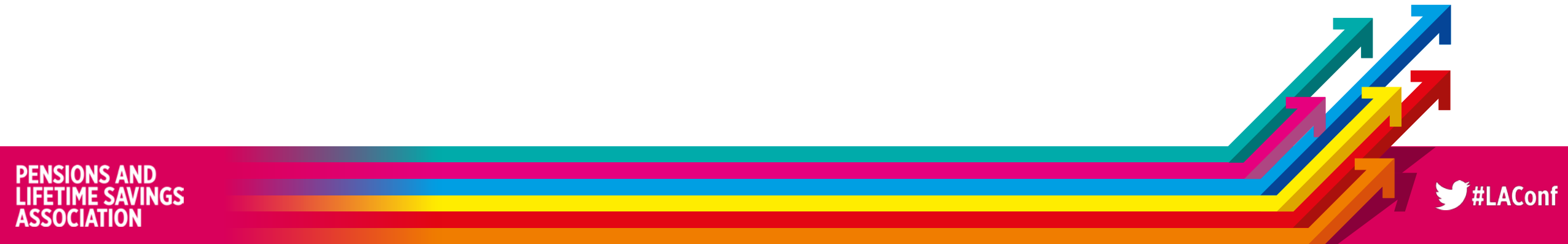
- ▶ And could similar tensions between funding and desire for high and consistent standards across the country affect other services?



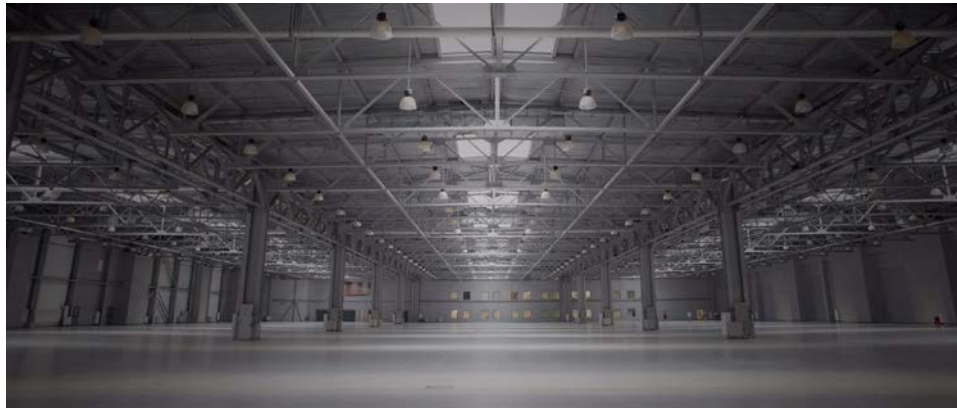
- ▶ Could local government end up as a pension fund with a side-job in bin collection?

WHAT ARE THE IMPLICATIONS OF THESE CHANGES

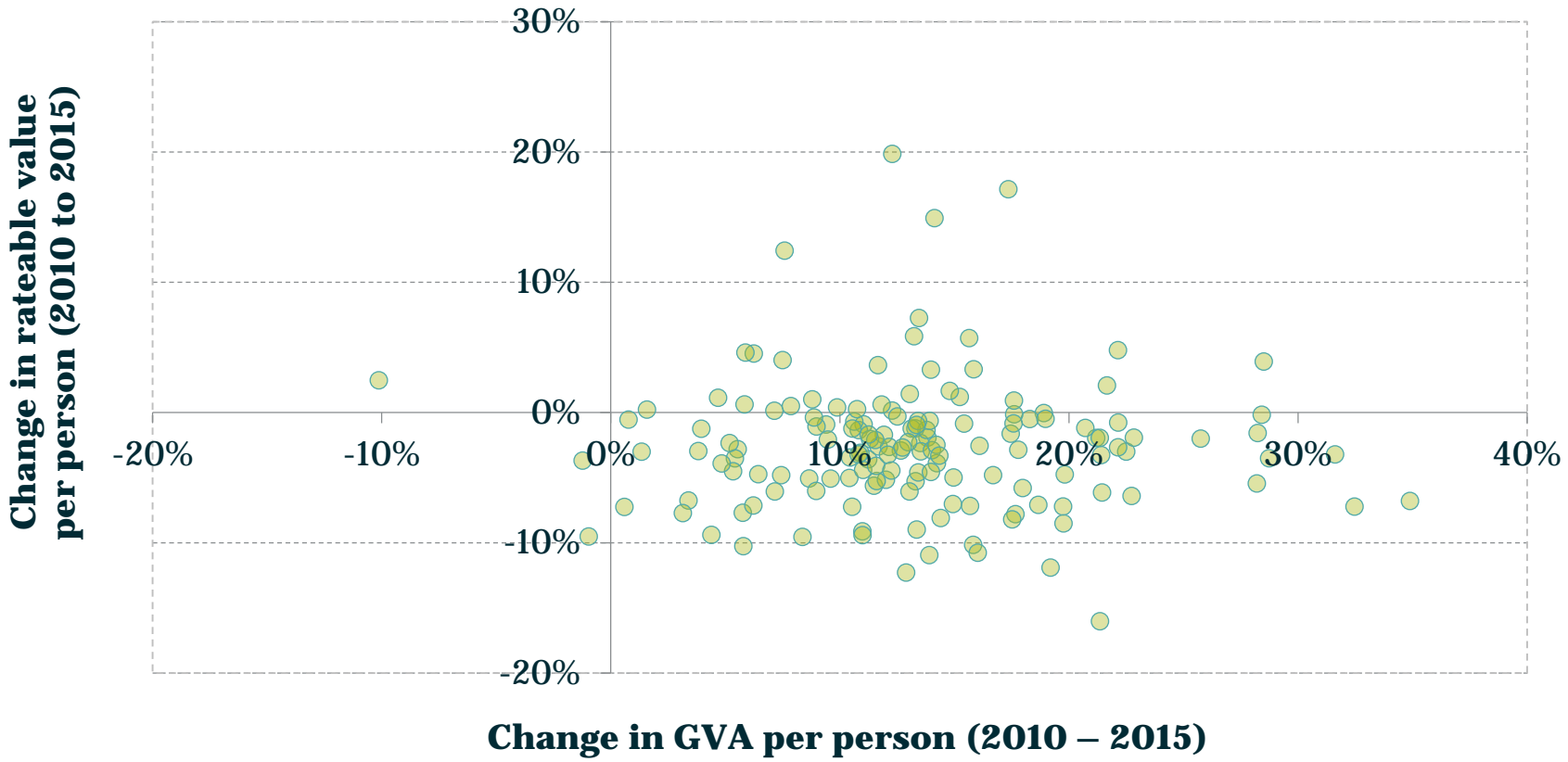
1. Inconsistency between finance and other policies (e.g. adult social care)
2. Changed incentives for investments and possibly pensions



WHAT DOES BUSINESS RATES RETENTION INCENTIVISE?



LITTLE LINK BETWEEN PROPERTY AND ECON GROWTH



Source: IFS calculations MHCLG and ONS data.

COUNCILS HAVE BEEN INVESTING IN COMMERCIAL PROPERTY

- ▶ Regeneration and economic development
- ▶ And income generation?
- ▶ Often in their areas but not always...



Birchwood Park, Warrington
Warrington Council



Mersey Way Shopping, Stockport
Stockport Council



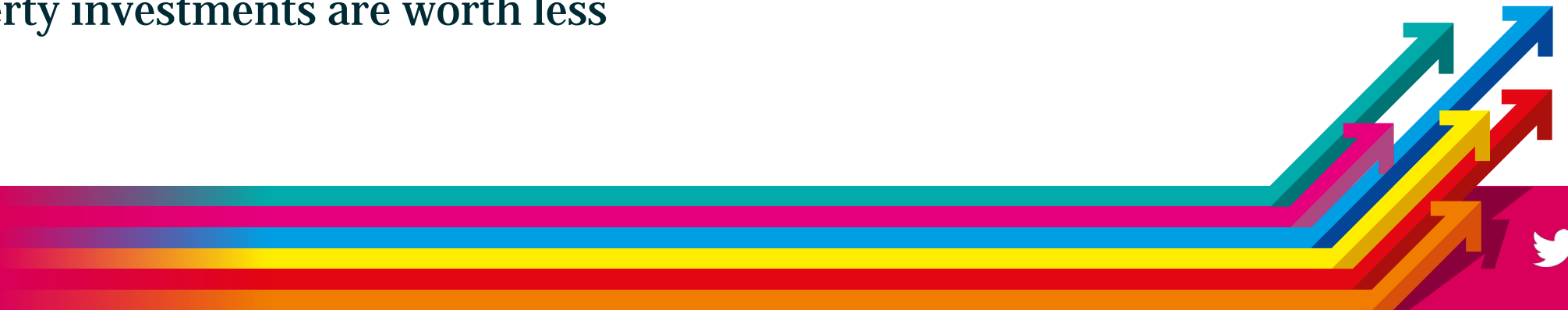
Malvern Shopping Park, Worcestershire
Surrey County Council

TENSIONS BETWEEN DIFFERENT OBJECTIVES

- ▶ Invest locally to support local regeneration efforts?
- ▶ Invest elsewhere to diversify risks and earn greatest returns?

- ▶ Business rates retention changes the incentives
 - ▶ Invest locally and (part of) the business rates will be paid to you
 - ▶ Invest elsewhere and it will flow to other councils

- ▶ Risk of councils suffering double whammy if local economy takes downturn?
 - ▶ Fall in rates revenues, increase in spending needs
 - ▶ Property investments are worth less

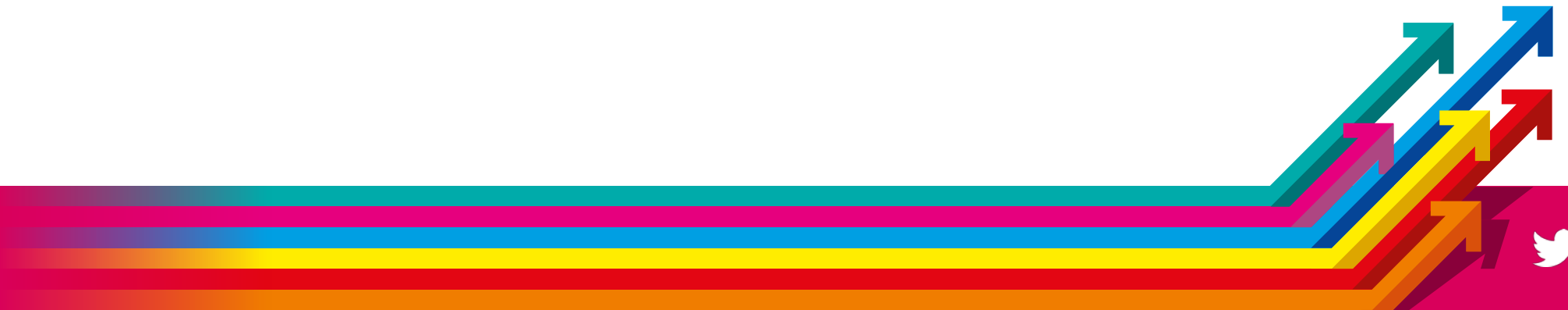


GOVT. CONCERNED ABOUT INVESTMENT RISKS

“The prime duty of a local authority is to provide services to local residents, not to take on disproportionate levels of financial risk by undertaking speculative investments, especially where that is funded by additional borrowing”

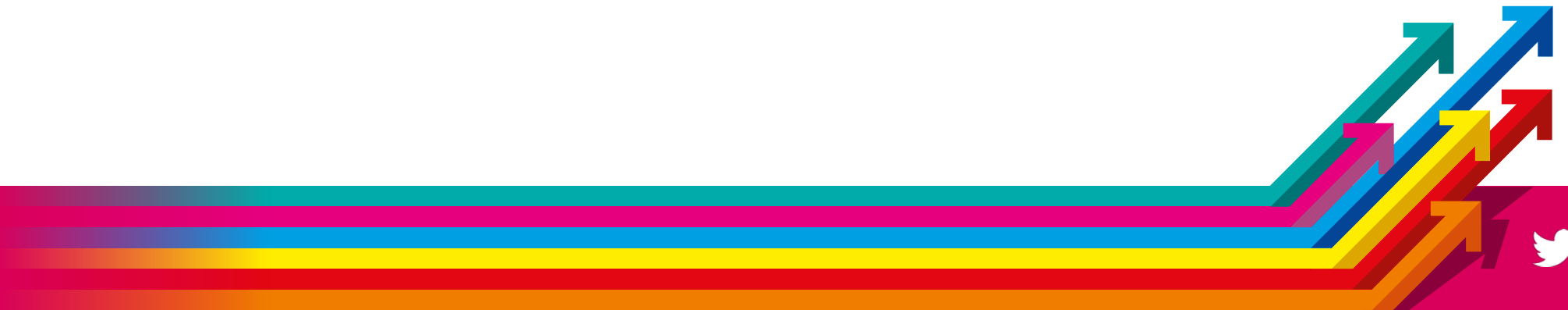
HM Government, February 2018

- ▶ Tightened up the rules so cannot borrow to fund investments that are solely for the purpose of generating income
 - ▶ More encouragement to invest locally rather than spreading the risk?



GOVT WANTS PENSIONS TO INVEST MORE IN PROPERTY AND INFRASTRUCTURE

- ▶ Encouraging pooling so as to take advantage of scale
 - ▶ Eight asset pools proposed and schemes working on governance arrangements
- ▶ Unlike councils' general investments, LGPSs are required to focus on income generation so as to:
 - ▶ Deliver returns needed to pay scheme members' pensions
 - ▶ Protect local taxpayers and employers from high pension costs



DOES BUSINESS RATES (AND POSSIBLE BROADER TAX DEVOLUTION) CHANGE CALCULUS?

Invest in pool area

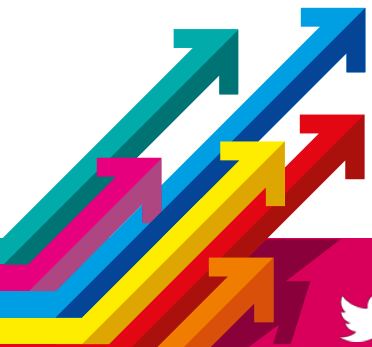
Invest outside pool area



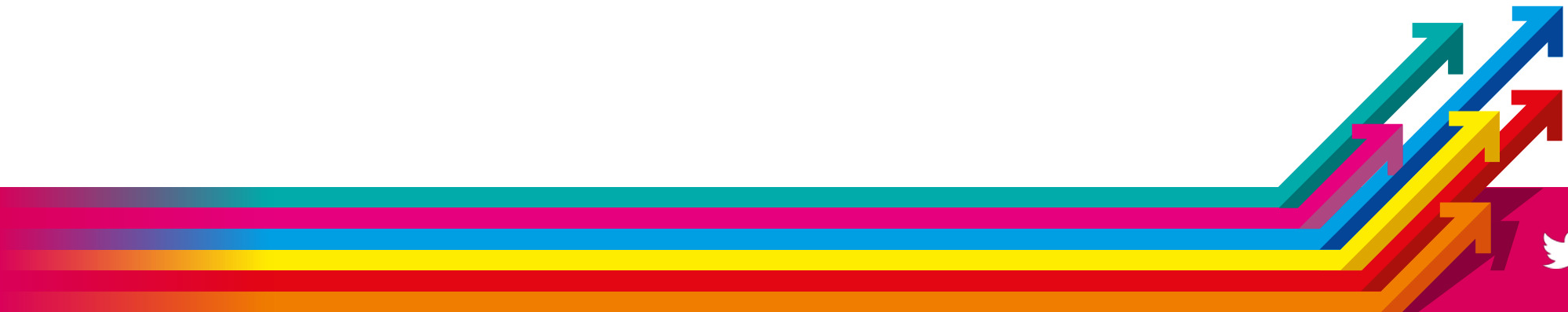
Investment returns



Tax receipts



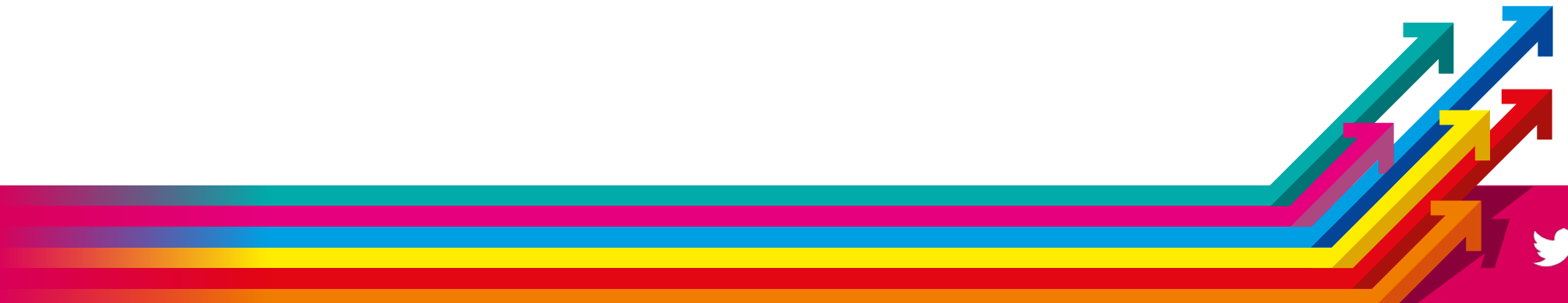
SUMMARY

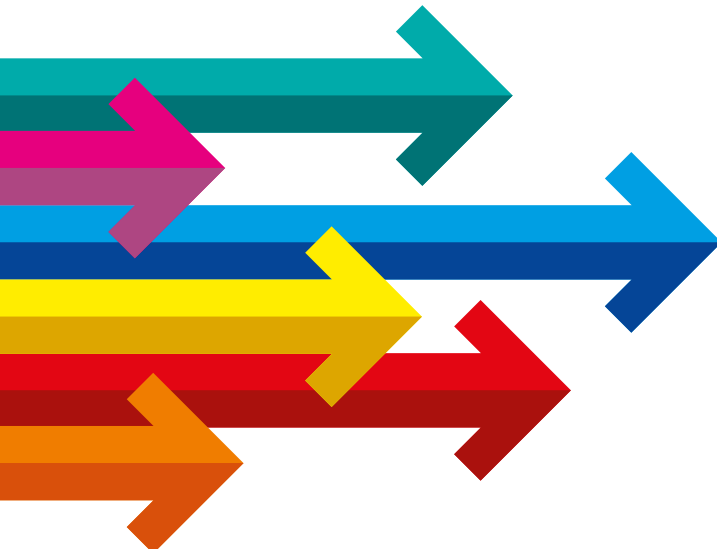


BIG CHANGES TO COUNCIL FUNDING

- ▶ Ongoing austerity will mean budgets will be under growing pressure
 - ▶ Unless large increases in taxes or borrowing or an unforeseen economic boom
- ▶ Tensions between desire for stronger financial incentives and consistent service standards across the country for key services
 - ▶ Could this mean some services are effectively centralised (even if LAs still involved)
- ▶ Could changes to financial system affect investment and pensions decisions?

- ▶ And I didn't mention Brexit once!





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