

Written evidence submitted by Associate Professor Henry C Midgley, Durham University<sup>1</sup>, Professor Laurence Ferry, Durham University<sup>2</sup>, & Honorary Professor Aileen Murphie, Durham University<sup>3</sup> [FSF 018]

***Reason for submission***

Our knowledge and expertise in local government finance is set out in the footnotes below. Our aim is to aid the committee in its inquiry.

***Is the local government finance system fit for purpose? If not, what needs to change?***

**Summary and overall conclusion:**

1. **No, the local government finance system is not fit for purpose for a variety of reasons.** Local authority income from council tax, retained business rates, government grants and commercial income has not kept pace with demand for services, leading to a predicted gap of some £4 billion<sup>4</sup> over the next two financial years. Central government grant to local authorities fell by 49% between 2010-11 to 2017-18, equating to a real terms drop in spending power of 28.6%; local government spending power has increased since then but has not been restored to 2010 levels. The overall picture is that there is not enough money in the system to cope with rising demand for services for the vulnerable as well as funding neighbourhood services and other key service areas like housing. Authorities also face cost pressures including inflation, rises in the living wage and employers' national insurance. There are problems and issues with all of the components of local authority income: council tax, government grant, retained business rates and income from fees and charges and commercial income. The finance system is overly complex, and been subject to several single year financial settlements, multiple system changes and one off, short term funding initiatives that have damaged the sector's financial sustainability and hindered good value for money in decision making. The strength of the local government sector including its senior finance staff and their determination to meet their statutory obligation to balance their accounts each financial year, has meant that only 6 authorities out of some 353 have had to issue at least one section 114 notice indicating that the authority is forecast not to be able to meet their liabilities. The Ministry of Housing, Communities and Local

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<sup>4</sup> *Financial distress in local authorities*, HCLG Committee, HC 56, 2023-24, summary <https://committees.parliament.uk/publications/43165/documents/214689/default/>

Government has improved its understanding and oversight of the sector's finances but other government departments need to understand the distributional and geographic aspects of policy and delivery. Central government needs to develop an integrated understanding of local government and its pressures. The sector as a whole needs a long term plan for financial sustainability and what local government is there to do, which should underpin its sources of income. In principle these need to be buoyant; progressive; fair; efficient and predictable.

**The main reasons why the local government finance system is not fit for purpose comprise:**

2. Revenue spending by local authorities is funded by council tax, retained business rates, central government grants and other income including fees and charges and commercial income. Local authorities have little influence over the various sources of their income.
3. The **finance system** does not reflect the differing needs of populations in different places, because the allocation formulae seriously out of date and reform (termed the Fair Funding Formula) has been repeatedly delayed from when it was first announced in 2016<sup>5</sup>.
4. **Council tax** was introduced in 1992. It is charged on domestic property in 8 bands based on the property's value in 1991 and is therefore considerably out of date. The tax is increasingly regressive as property values have risen much more in some areas than others and out of date as no revaluation has taken place since its introduction. The amount any authority can raise varies significantly as it depends on the types of properties it has; an authority with a majority of band A properties raises much less than those with a majority of band C<sup>6</sup>.
5. Authorities are constrained in how much they can raise from **council tax** as they cannot increase council tax further than the percentage rate which MHCLG sets within the local government finance system (the 'referendum limit') without holding a referendum locally which would cost much more than a rise in council tax would raise. This means that this source of income is tightly constrained. This matters because council tax is an increasingly large proportion of council income. See chart below<sup>7</sup>.

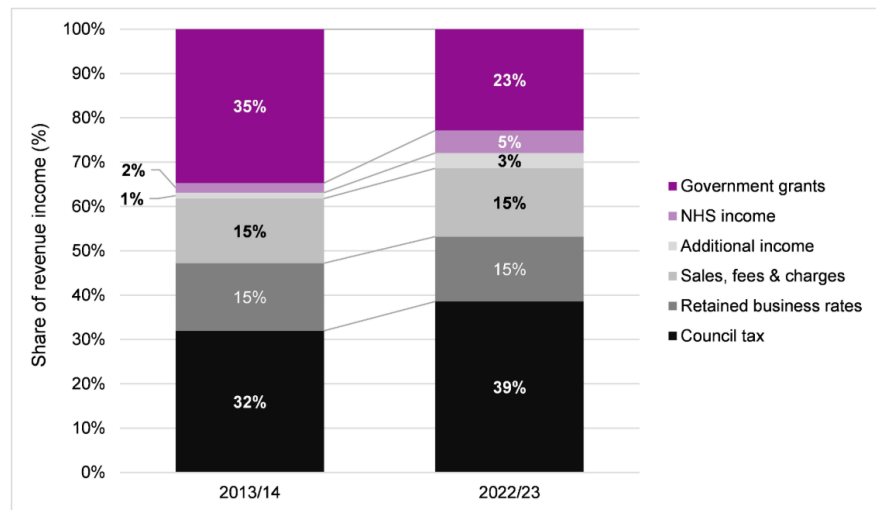
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<sup>5</sup> *The local government finance system in England*, National Audit Office, 2021, Figure 7, p18 and para 16, page 11 <https://www.nao.org.uk/wp-content/uploads/2021/11/The-local-government-finance-system-in-England-overview-and-challenges.pdf>

<sup>6</sup> *Financial distress in local authorities*, HCLG Committee, HC 56, 2023-24, para 27ff, p12 <https://committees.parliament.uk/publications/43165/documents/214689/default/>

<sup>7</sup> *Reforming the local government funding system in England*, LGA, December 2024, Fig 1, <https://www.local.gov.uk/publications/reforming-local-government-funding-system-england#4-new-and-devolved-funding-streams-longer-term-reform>

Figure 1: Council revenue funding sources as a share of total revenue income – 2013/14 and 2022/23



6. **Business rates** are charged on non domestic physical properties in an area at a nationally set rate. All business rate income flows into the department and is redistributed to authorities according to a complex system of tariffs and top ups. Councils retain a proportion of growth in business rates. The main issues with business rates are that need for services and business rates in any local area do not necessarily match and that service demand and ability to generate business rates diverge over time requiring regular resets of top ups and tariffs<sup>8</sup>. The other issue arises from the development of online sales; business rates are charged on bricks and mortar businesses and do not receive any income from business which have no physical presence in an area.
7. Revenue **grants** are given to local authorities by central government to support service provision including adult social care for vulnerable adults, children’s services, special educational needs (SEND), homelessness services, housing, trading standards, transport and other services. Virtually all grants (apart from revenue support grant) come with specific purposes, grant conditions and reporting requirements from a range of central departments, some of which can be onerous. Grants are short term, can be subject to in year cuts and can be withdrawn with little notice leading to instability and a lack of predictability.
8. **Fees and charges** contribute to local authority income but in very different ways and at very different levels across authorities, depending on their individual circumstances. This type of income includes car parking charges, entry fees for theatres and museums and charges for some forms of support for adults who receive social care. There are limits to what can be charged, both economic and political. This type of income is vulnerable to economic downturns and fell away almost completely during the COVID-19 pandemic<sup>9</sup>.
9. Some councils have **commercial income** from capital investments such as rent from properties developed in regeneration schemes, or dividends from investments in local infrastructure such

<sup>8</sup> *Planning for 100% business rate retention*, C&AG’s Report, HC 1058, 2016-17, March 2017, paras 1.7ff <https://www.nao.org.uk/wp-content/uploads/2017/03/Planning-for-100-local-retention-of-local-business-rates.pdf>

<sup>9</sup> *Local government finance in the pandemic*, C&AG’s Report, HC 1240, 2019-21, March 2021, Para 1.20ff <https://www.nao.org.uk/wp-content/uploads/2020/08/Local-government-finance-in-the-pandemic.pdf>

as airports. In recent years some authorities have also made investments in commercial property solely to secure yield. These investments suffered during the COVID-19 pandemic and due to economic conditions, which have caused losses for authorities who may still have to pay for loan interest arising from the investments<sup>10</sup>.

- *Does the local government finance system match funding to the relative needs of local authorities?*

10. **No**, the local government finance system does not match funding to needs. The reasons are set out in paragraphs 11 to 14 below.
11. When central government began reducing funds to local government in 2010-11, they bore down harder on authorities which were more grant dependent as they received a greater proportion of their income from grant. Being more grant dependent means those authorities had more deprived populations. Once set, this pattern continued in later funding settlements<sup>11</sup>. In order to enable local government to cope with reduced central government funding, the department removed the ringfences from grants with specific purposes and rolled them into revenue support grant which could be used for any purpose and then cut that grant.
12. The Department for Communities and Local Government (the department) introduced incentive based funding mechanisms including New Homes Bonus, which awarded extra funding to authorities who built additional homes and 50% business rate retention which was intended to encourage authorities to attract more businesses to their areas. These measures increase differentiation between authorities as not all could build extra homes or had the scope for increasing their business rate income. Also, these changes weakened the link between need and grant income<sup>12</sup>.
13. At the same time as these changes were made, the department stopped updating the assessment of relative spending needs which they used to inform the distribution of revenue support grant<sup>13</sup>.
14. As detailed above in paragraph 6, business rate income does not correlate with need locally. See the chart below<sup>14</sup>.

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<sup>10</sup> Ibid, para 1.20ff

<sup>11</sup> *Financial sustainability of local government 2014*, C&AG's Report, HC 783, 2014-15, Fig. 2 and para 1.7 <https://www.nao.org.uk/wp-content/uploads/2014/11/Financial-sustainability-of-local-authorities-20141.pdf>

<sup>12</sup> Ibid, para 2.13

<sup>13</sup> Ibid, para 2.9

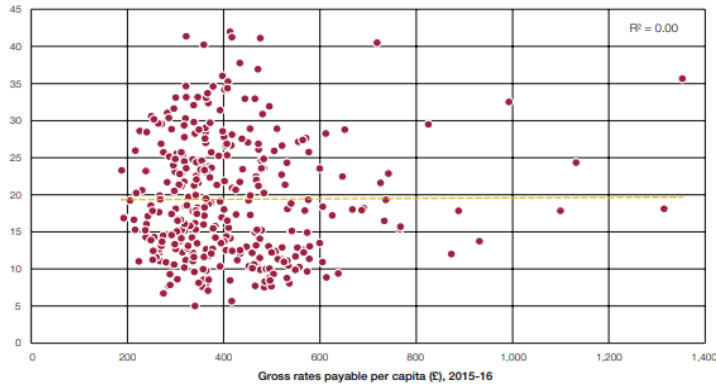
<sup>14</sup> *Planning for 100% business rate retention*, C&AG's Report, HC 1058, 2016-17, March 2017, Fig 2, p14 <https://www.nao.org.uk/wp-content/uploads/2017/03/Planning-for-100-local-retention-of-local-business-rates.pdf>

**Figure 2**

Level of deprivation and gross rates payable per capita by billing authority

The scale of an area's business rates tax base (per capita) does not necessarily match its level of need for local services

Indices of multiple deprivation (average score), 2015



**Notes**

- 1 See separate Methodology document for details of data sources and methodological approach.
- 2 The dotted line is a regression line which shows no correlation between the two variables.

Source: National Audit Office analysis of Department for Communities and Local Government and Office for National Statistics data

15. Council tax has increased as a proportion of local authority income making it more regressive. Council tax support was localised in 2011 which meant that the support offered to residents who had difficulty in paying depended on local decisions on support. Schemes became less generous, increasing bad debts and decreasing income to authorities over time<sup>15</sup>.

- *Does the funding system allow and incentivise local authorities to make sensible long-term choices about their finances and budgets, to better serve their residents?*

16. **No.** The combination of repeated funding reductions, increases in demand for statutory services, one off and short term funding initiatives, multiple changes in the finance system consequent on spending reviews (exemplified in paragraph 17 below), the increase in service overspends in adult and children's social care, repeated single year settlements have all together increased uncertainty for councils and undermined their financial sustainability. Financial uncertainty, both short term and long term, creates risks for value for money as it encourages short-term decision-making and undermines strategic planning<sup>16</sup>.

17. The amount of change in the finance system has been a source of instability and uncertainty for some time. For example, central government funding outside the local government finance settlement changed a number of times post the Spending Review 2015, including: three adult social care grant announcements; the introduction of, and a subsequent change to, the adult social care precept; two changes to rural services delivery grant<sup>17</sup>.

<sup>15</sup> *Council Tax Support*, C&AG's Report, HC882, Session 2013-14, December 2013, para 11, p7 <https://www.nao.org.uk/wp-content/uploads/2013/12/10316-001-Council-Tax-Book.pdf>

<sup>16</sup> *Financial sustainability of local authorities 2018*, C&AG's Report, HC834, Session 2017-19, March 2019, para 20, p10 <https://www.nao.org.uk/wp-content/uploads/2018/03/Financial-sustainability-of-local-authorities-2018.pdf>

<sup>17</sup> *Ibid*, para 4.20. p59

18. This pattern of change continued on during the four-year funding settlement period (2016-17 to 2019-20) continuing the instability and uncertainty, added to by the growth of fragmented funding pots and use of competitive bidding. The latter means that local authorities have no certainty over the amount of funding which could be available to them<sup>18</sup>.

- *How will this be affected by the introduction of multi-year funding settlements?*

19. Multi year settlements would provide some stability for local authorities and would enable them to plan their Medium Term Financial Strategies in a more realistic way. This should help in improving good decision making and improve value for money and strategic planning. However, many grant streams are provided to authorities outside the local government settlement and funding decisions covering more than one year for these would be necessary as well.

- *What parts of the local government finance system are working well and should be built on further?*

20. If the finance system is taken to include the local government governance system as well, one of its key strengths is the section 151 officer (chief finance officer), a statutory position whose responsibilities include ensuring that the authority stays financially viable and can balance its books each year. A second strength is the statutory framework of legal duties and financial controls overseen by the Ministry of Communities, Housing and Local Government (the department) which governs what authorities can do and how they do it. The section 151 officer is a key part of the framework as is the duty to have a balanced budget; a statutory process (section 114 notice) by which the section 151 officer can cause the council to pause and reconsider spending decisions or budgets; and legal requirements for councils to have a sound system of internal control, proper arrangements for managing their financial affairs and to have their statement of accounts and arrangements for value for money subject to external audit annually<sup>19</sup>.

21. The sector's reserves also constitute a strength in that they enable authorities to plan for more than 1 year, to set aside resources for use in the future and give them a valuable amount of flexibility across the year end. However, not all councils have reserves and some only have a small amount.

22. However, the sector's governance framework has been weakened by decisions by central government, example of which include allowing authorities to use capital receipts to fund service transformation in some circumstances, which risks shrinking an authority's asset base to fund day to day services<sup>20</sup>; making the sale of assets and use of receipts a condition of Exceptional Financial Support to a council in financial difficulty<sup>21</sup>; having a policy of allowing

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<sup>18</sup> *The local government finance system in England: overview and challenges*, C&AG's Report, HC 858, Session 2021-22, November 2021, p32 <https://www.nao.org.uk/wp-content/uploads/2021/11/The-local-government-finance-system-in-England-overview-and-challenges.pdf>

<sup>19</sup> *Local Authority Governance*, C&AG's Report, HC 1865, Session 2017–2019, January 2019

para 3, p5 <https://www.nao.org.uk/wp-content/uploads/2019/01/Local-authority-governance.pdf>

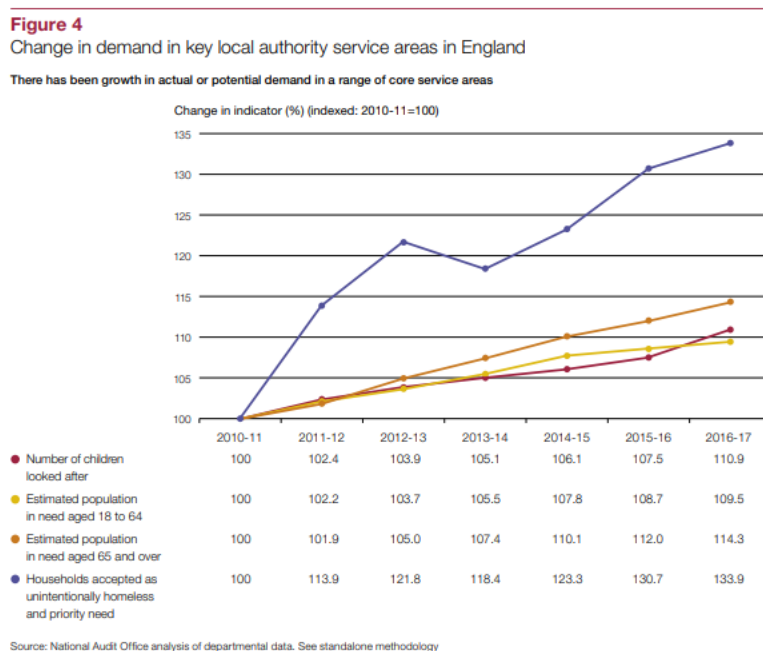
<sup>20</sup> *Financial sustainability of local authorities 2018*, C&AG's Report, HC834, Session 2017-19, March 2019, para 4.16, p59 <https://www.nao.org.uk/wp-content/uploads/2018/03/Financial-sustainability-of-local-authorities-2018.pdf>

<sup>21</sup> *Financial distress in local authorities*, HCLG Committee, HC 56, 2023-24, para 46, p16

authorities who have overspent their budgets for special educational needs to carry these forward as a 'negative reserve' on the balance sheet to be paid off over future years and lastly, overseeing the growth in egregious delays in the audit of local authority accounts leading to a backlog of external audits of several years and seemingly unable to tackle the issue<sup>22</sup>. In 2019, the NAO pointed out the fragmented nature of the governance framework and lack of leadership, urging the department to improve its oversight, transparency and engagement. This is important because as the NAO says, poor governance can make the difference between an authority coping and not coping with financial and service pressures<sup>23</sup>.

- **Where are the most significant funding pressures in local government, and how does the finance system address them?**

23. The most significant funding pressures come from the provision of statutory services to vulnerable people: adult social care, children's social care and homelessness services. These trends have been observable since 2010-11 as the chart from the NAO's report on local government finance in 2019 shows<sup>24</sup>:



24. To take **children's social care first**, local authorities have statutory responsibilities for ensuring and overseeing the effective delivery of services for children, including specific responsibilities to promote and safeguard the welfare of children including those looked after by the local authority. In discharging these responsibilities, local authorities provide some care and accommodation directly and purchase some from independent providers. Numbers in any aspect of children's services are relentlessly upward; for example, the number of children in secure units and children's homes and the number with Education, Health and Care plans

<https://committees.parliament.uk/publications/43165/documents/214689/default/>

<sup>22</sup> Progress update: Timeliness of local auditor reporting on local government in England, C&AG's Report, HC 1026, Session 2022-23, para 2.9ff, p22 <https://www.nao.org.uk/wp-content/uploads/2023/01/progress-update-timeliness-of-local-auditor-reporting.pdf>

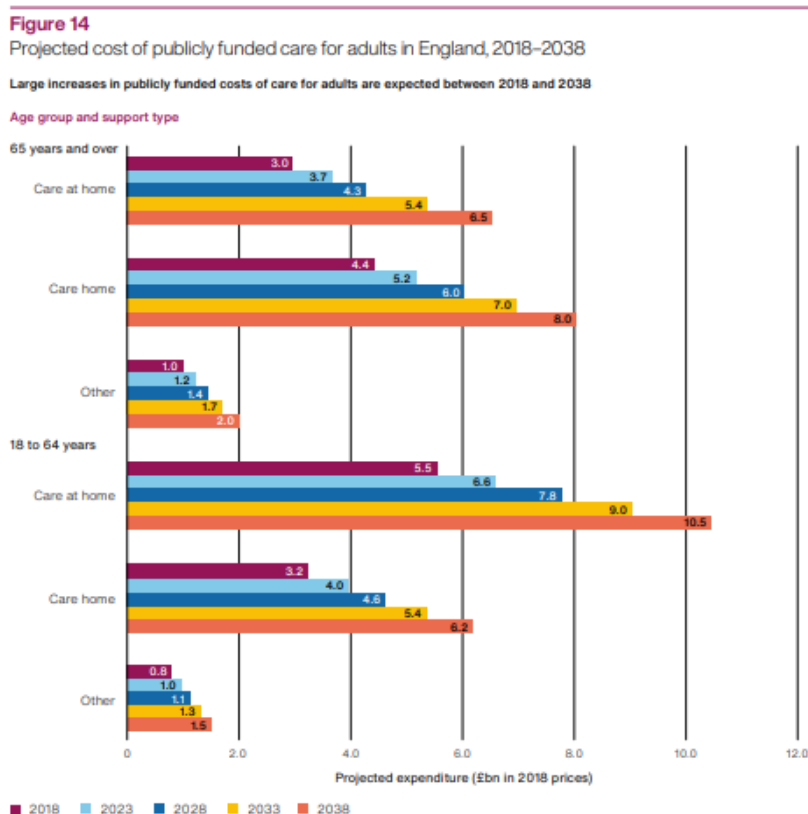
<sup>23</sup> Local Authority Governance, C&AG's Report, HC 1865, Session 2017-2019, January 2019 para 22, p12 <https://www.nao.org.uk/wp-content/uploads/2019/01/Local-authority-governance.pdf>

<sup>24</sup> Financial sustainability of local authorities 2018, C&AG's Report, HC834, Session 2017-19, March 2019, Fig 4 <https://www.nao.org.uk/wp-content/uploads/2018/03/Financial-sustainability-of-local-authorities-2018.pdf>



(EHCPs) both increased by over 30% between early 2020 and early 2023. Costs have reflected this same pattern: the cost per placement in children’s homes increased by 20% between 2019–20 and 2022–23, while the cost of care home placements for adults aged 65 or over increased by 35% between 2019–20 and 2023–24<sup>25</sup>. The Competitions and Markets Authority has commented adversely on the working of the market in residential care, particularly on the profit levels earned by some providers<sup>26</sup>.

25. As for **adult social care**, the costs are again relentlessly upwards, despite there being also a record number of people waiting for care, particularly domiciliary care. This chart from the NAO’s report on the adult social care market shows the forecast costs by type of client to 2038<sup>27</sup>:



26. The number of new requests for adult social care support increased from 1.98 million in 2021-22 to 2.0 million in 2022-23. This reflects both an increasingly aging population and increasing disability among working-age adults. There were also continued delays in responding to requests for support. A survey by the Association of Directors of Adult Social Services in autumn 2023 reported that nearly 250,000 people were still waiting for adult social care assessments at the end of August 2023<sup>28</sup>. Delays mean that people become more ill and therefore more dependent when they do finally receive care, meaning their needs are greater.

<sup>25</sup> <https://ifs.org.uk/publications/how-have-english-councils-funding-and-spending-changed-2010-2024>

<sup>26</sup> *Financial distress in local authorities*, HCLG Committee, HC 56, 2023-24, para 68, p22  
<https://committees.parliament.uk/publications/43165/documents/214689/default/>

<sup>27</sup> The adult social care market in England, C&AG’s Report, HC 1244, Session 2019-21, Fig 14  
<https://www.nao.org.uk/wp-content/uploads/2021/03/The-adult-social-care-market-in-England.pdf>

<sup>28</sup> Kings Fund, *Social care 360*, access, March 2024 <https://www.kingsfund.org.uk/insight-and-analysis/long-reads/social-care-360-access#1.-requests-for-support>



27. There is not enough money in the adult social care system (see for example the record number of vacancies in the workforce partly because hourly rates are not competitive). The committee's predecessor recommended in their July 2022 report: *Long-term Funding of Adult Social Care* that "the Government urgently needs to allocate more funding to adult social care in the order of several billions each year, at least £7 billion..."<sup>29</sup>
28. The third major pressure on local authority finances is due to **homelessness**. Cases of homelessness are rising, meaning more people are in search of advice, support and temporary accommodation. The latest data show that 123,000 households in England were being housed in temporary accommodation as at June 2024. In 2023–24, local authorities spent over £3.1 billion on delivering homelessness services, of which over £2.1 billion was used to provide temporary accommodation<sup>30</sup>. Local authorities have a statutory duty to provide temporary accommodation to all households in priority need, so increasing need has forced local authorities to spend more on temporary accommodation. The situation was sufficiently serious that a number of local authorities, such as Eastbourne Borough Council, have been forced to approach MHCLG for exceptional financial support<sup>31</sup>.
- ***Does the current statutory regime for identifying and responding to financial distress in local authorities support local authorities to get out of financial distress?***
29. The department offers Exceptional Financial Support to authorities which are experiencing significant financial difficulties that cannot be managed within their own resources<sup>32</sup>. The EFS framework scheme is not statutory though interventions in authorities who have been granted EFS are. Most commonly, EFS involves a capitalisation direction which allows authorities to either borrow or use capital receipts to support revenue spending. Officials establish the underlying causes of the need for exceptional support to give ministers assurance that exceptional support would enable an authority to set a balanced budget and sustain its financial position<sup>33</sup>.
- *Have Government interventions in response to local authorities being in financial distress helped those local authorities to stabilise their finances and avoid further financial distress?*
30. It is not possible to say whether the department's EFS framework has restored authorities to avoid financial distress. Six authorities have issued section 114 reports meaning that the authority is at risk of failing to balance its budget and 3 have had to issue a second section 114 report, indicating that financial problems persist. Some authorities have a capitalisation direction in place without issuing a section 114 report: 19 for 2024-25 of which 5 have issued section 114 reports<sup>34</sup>.
31. However, to assess whether the department is succeeding in supporting authorities in financial trouble successfully, one would need to know how many authorities approach the department

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<sup>29</sup> *Financial distress in local authorities*, HCLG Committee, HC 56, 2023-24, para 91

<https://committees.parliament.uk/publications/43165/documents/214689/default/>

<sup>30</sup> *Tackling homelessness*, Committee of Public Accounts, Fourth Report of Session 2024–25 HC 352, para 3, p9

<https://committees.parliament.uk/publications/46302/documents/233214/default/>

<sup>31</sup> *Ibid*, para 7, p11

<sup>32</sup> <https://www.gov.uk/guidance/exceptional-financial-support-for-local-authorities-for-2024-25>

<sup>33</sup> *Local government finance in the pandemic*, C&AG's Report, HC 1240, 2019-21, March 2021, para 2.44

<https://www.nao.org.uk/wp-content/uploads/2020/08/Local-government-finance-in-the-pandemic.pdf>

<sup>34</sup> <https://www.gov.uk/guidance/exceptional-financial-support-for-local-authorities-for-2024-25>

to discuss their finances and track what happened afterwards, including those authorities who withdrew from discussions. However, when the NAO attempted to assess the department's effectiveness in this area in 2021, the department would not share the number of authorities that had enquired about exceptional support or those where the department was concerned about the financial health of the authority. The department told the NAO that its conversations about exceptional support and its risk analysis were confidential. It is not possible to understand the full picture of financial stress in the sector or to evaluate the department's effectiveness in addressing it without knowing the level of demand for exceptional support or the department's views on financial risk in the sector more generally. The NAO concluded that the department had not found a way of being more transparent about the level of financial stress in the sector while nonetheless maintaining a safe space to engage with individual authorities. Nor could the NAO assess the effectiveness of either the EFS framework or the department's efforts more generally to relieve financial stress in the sector<sup>35</sup>. This area needs further research, assessment by the NAO and transparency on the part of the department.

- *What should a broader support system for local authorities in financial distress look like?*

32. A broader support system should encompass an in depth review of the authority's service demands coupled with the normally carried out review of its financial position; a better support system would have more solutions at its disposal than only a capitalisation direction (short term grant funding for example); it would ensure that asset sales are carried out in ways that are not to the detriment of the future of the authority and lastly, support should involve other government departments which have policy responsibility for major service areas.

- *Are there any specific circumstances that have led some councils into financial distress and others to avoid financial distress so far?*

33. Authorities vary in many ways including their level of reserves, the level of deprivation of their populations and whether they are able to generate additional income from say, business rates, to name only three aspects. Other factors like their geography and history also exert an influence. Then the depth and quality of financial management, governance and decision making is critical: Northamptonshire County Council was condemned by the government's chief commissioner for poor management, a lack of budgetary control and a culture which discouraged challenge<sup>36</sup>. The London Borough of Croydon was found by its auditors to have deteriorating financial resilience, increasing service overspends, increasing levels of borrowing and wholly owned companies which were not producing any returns<sup>37</sup>. Thurrock<sup>38</sup> and Nottingham's<sup>39</sup> problems arose from investment in energy related transactions to a level which risked the authorities' very financial survival.

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<sup>35</sup> *Local government finance in the pandemic*, C&AG's Report, HC 1240, 2019-21, March 2021, para 19  
<https://www.nao.org.uk/wp-content/uploads/2020/08/Local-government-finance-in-the-pandemic.pdf>

<sup>36</sup> Para 1.1 ff

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<sup>37</sup> <https://www.croydon.gov.uk/sites/default/files/2021-03/Report%20in%20the%20Public%20Interest%20-%20London%20Borough%20of%20Croydon.pdf>

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[https://assets.publishing.service.gov.uk/media/6489dc31b32b9e0012a967e7/Thurrock\\_Best\\_Value\\_Inspection\\_report\\_19\\_May\\_2023.pdf](https://assets.publishing.service.gov.uk/media/6489dc31b32b9e0012a967e7/Thurrock_Best_Value_Inspection_report_19_May_2023.pdf)

<sup>39</sup> [https://assets.publishing.service.gov.uk/media/5fd39b45e90e076636a8a65a/201127\\_NCCreport.pdf](https://assets.publishing.service.gov.uk/media/5fd39b45e90e076636a8a65a/201127_NCCreport.pdf)

34. So, up to recently, authorities who got into the worst difficulties had management and governance failures which magnified the deleterious effects of funding reductions and increasing demand. However, things may be changing: despite additional funding to local government in recent years, services continue to be a major driver of spending, with user numbers growing and costs outpacing general inflation<sup>40</sup>. We may see councils which are well managed succumbing to financial failure as their resources do not keep pace with demand<sup>41</sup>.

- ***How much control do local authorities have over the levels of funding they receive, including from local taxation, business rates, central Government grants, and returns on commercial investments?***

35. As detailed in the paragraphs 4 and 5 above, local authorities have little control over council tax rates and the council tax base takes years to increase, dependent as it is on house building. As for business rates, this too is not under the control of authorities as the rate is set centrally and few authorities have ways of expanding their business rate base easily. And revaluations relating to both taxes are decided upon by central government. Central government grants are decided upon at spending reviews by HM Treasury ultimately, and reflect the overall priorities of central government which may not favour local services, despite the case made by local government and relevant sponsoring departments. Lastly, return on commercial investments are affected by the business cycle and the overall economic position of the UK and were badly affected by the COVID-19 pandemic. The large increase in borrowing for investment by some authorities in the period before 2020 increased the financial exposure of those authorities and their risk levels; this development was highlighted and warned against by both NAO and the Committee of Public Accounts<sup>42</sup>.

- *How does this differ between different types of local authorities and between authorities with different devolution agreements?*

36. The authorities most at risk are those that provide adult and children services as these areas are both key cost drivers. Authorities in the most deprived areas have had bigger funding reductions and have less scope to increase their income. Authorities created under various devolution agreements (combined authorities) tend to be focused on regeneration and transport and have limited access to council tax and business rate growth but do not have the service demands.

- *What are the impacts of statutory restrictions preventing the use of capital returns (e.g. from asset sales) as revenue funding, and are those restrictions beneficial for local authorities?*

37. Preventing capital receipts being used to support revenue spend (apart from in specific circumstances) is to prevent an authority dissipating its assets to the detriment of future generations. Authorities are the stewards of the public assets they hold. Shrinking their asset base may solve an immediate crisis but may not be the right choice longer term.

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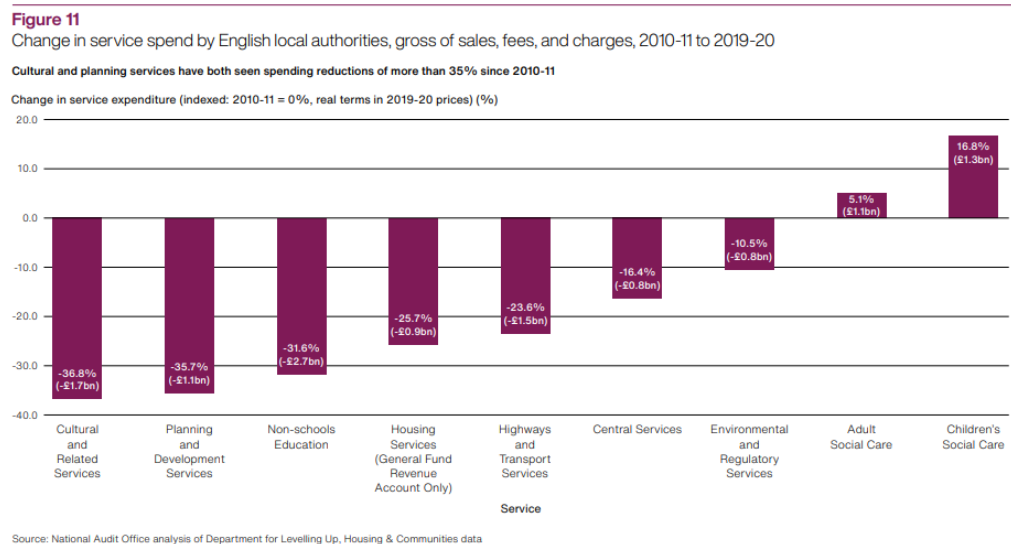
<sup>40</sup> *How have English councils' funding and spending changed? 2010 to 2024*, IFS. June 2024, para 5 <https://ifs.org.uk/publications/how-have-english-councils-funding-and-spending-changed-2010-2024#:~:text=Download%20the%20data-,Key%20findings,the%20start%20of%20the%202010s.>

<sup>41</sup> *Financial distress in local authorities*, HCLG Committee, HC 56, 2023-24, para 6, p6 <https://committees.parliament.uk/publications/43165/documents/214689/default/>

<sup>42</sup> *Local authority investment in commercial property*, PAC, Eleventh Report of Session 2019–21, HC312 July 2020, p10 <https://committees.parliament.uk/publications/1845/documents/19224/default/>

- **How much control do local authorities have over their costs, including on mandatory services (which they are required to deliver by statute) and demand-led services (for which the level of cost is determined by the needs of residents)?**

38. Local authorities provide statutory services ('mandatory' as described in the term of reference above) which are set out in statute: adults and children's services and homelessness services are the main ones, which are demand led. Local authorities have many statutory duties, estimated at over 1000. Authorities can choose to provide discretionary services which are beneficial to their areas and citizens and often these support the aims of councils more generally, but are not statutory. The pattern of spending in the first part of austerity up to 2018-19 showed a narrowing of spend across the sector onto social care with an increasing proportion of spend being taken up by social care, according to the NAO. This pattern has continued. Concomitant with that has been a fall in discretionary spending: the NAO said that cultural spend had fallen by 36% and planning and economic development also by 36% from 2010-11 to 2019-20<sup>43</sup>. See the chart below.



39. Local authorities commission for or contract for adult social care from the providers in their areas. These are private sector or third sector entities and vary from the very large national providers to individual, possibly niche providers. As for domiciliary care, individuals can purchase their own care or have the local authority do it for them. As commissioners, authorities would seem to be in the dominant position for how much they will pay but they are heavily constrained by what provision is available locally, the level of competition, the assessed needs of service users and cost pressures including employers' national insurance, inflation and increases in the minimum wage, plus of course the number of people needing care and their own budgets. The proportion of self funders (people paying for their own care) also has an influence as they cross subsidise those whom local authorities pay.

40. As regards children's social care, recent reviews have pinpointed market failure in the market for children's residential care. The Competitions and Market Authority (CMA) found evidence

<sup>43</sup> *The local government finance system in England: overview and challenges*, C&AG's Report, HC 858, Session 2021-22, November 2021, Fig 11 <https://www.nao.org.uk/wp-content/uploads/2021/11/The-local-government-finance-system-in-England-overview-and-challenges.pdf>

indicating that a significant number of children were not gaining access to appropriate placements due to a lack of supply; that some authorities were forced to place children in unregulated accommodation because of a lack of suitable placements and the largest private providers of placements were making materially higher profits, and charging materially higher prices, than the CMA would expect if this market were functioning effectively<sup>44</sup>. Thus authorities have little control over the costs they pay for their two major service areas. Likewise, the same factors of constrained local supply and limits to councils' budgets hold true for homelessness services like temporary accommodation which is causing strain on budgets (see paragraph 28 above).

41. Discretionary services as their name suggests are limited by how much authorities can budget for these.

*How does this differ between different types of local authorities and between authorities with different devolution agreements?*

42. The same pattern of spending as described in the paragraphs above holds true for all authorities<sup>45</sup>

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- *What flexibility do local authorities have in the delivery of their mandatory services, and to what extent do they have the ability to deliver non-mandatory services?*

43. Statutes which impose duties on local authorities tend not to be specific about what exactly constitutes an acceptable service level, so local authorities have some leeway in how a service is provided. For example, libraries constitute a statutory service but that could mean centralising library services in an area or cutting hours across the board or indeed outlets. The only way to test service levels is to apply for judicial review.

44. For some services, there are independent inspectorates (CQC and Ofsted) which inspect services for quality. An adverse report will mean that an authority will have to implement recommendations where a service or provider is deemed inadequate. The existence of inspectorates tends to reduce leeway for authorities, but where services are in high demand like adult social care, waiting lists can help manage demand or adjusting thresholds for services or insisting on a solution for individuals which cuts costs for the authority.

45. As regards discretionary services, what an authority can provide is dictated by its priorities and available budget, within its overall duty to balance its books every year.

46. However, there is a growing dissonance between the fact that local government does not really control its resources in any real sense yet increasingly provides statutory services. This raises the accountability dilemma: as a citizen and council tax payer, what am I really holding my local authority to account for at the ballot box<sup>46</sup>?

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<sup>44</sup> <https://www.gov.uk/government/publications/childrens-social-care-market-study-final-report/final-report#outcomes-from-the-placements-market>

<sup>45</sup> *Financial sustainability of local authorities 2018*, C&AG's Report, HC834, Session 2017-19, March 2019, Fig 9 <https://www.nao.org.uk/wp-content/uploads/2018/03/Financial-sustainability-of-local-authorities-2018.pdf>

<sup>46</sup> *Auditing governable space—A study of place-based accountability in England*, Laurence Ferry, Henry Midgley, Aileen Murphie, Mark Sandford, Financial Accountability and Management March 2022 <https://onlinelibrary.wiley.com/doi/full/10.1111/faam.12321>

- *Has the level of demand for local authorities' services changed recently? If so, in which specific areas and why?*
47. Rises in demand in services for the vulnerable are covered in the paragraphs (23ff) above.
- *Where local authorities cut costs by reducing the services they pay for or provide, what services are most affected and what is the impact on residents?*
48. Two obvious examples are the numbers waiting for social care cited in paragraphs 25 and 26 above; if authorities were able to pay higher hourly rates or commission more care or both, then fewer people would be waiting. Delayed discharges from acute hospital settings are partly caused by a lack of suitable social care provision, especially domiciliary care<sup>47</sup>. A second example can be found in planning departments: delays in granting planning consent, partly due to fewer planning officers<sup>48</sup>.
- ***How well does the Government understand the consequences of funding and mandatory service decisions?***
49. This question has been reported on by the NAO from 2014 onwards. The department was criticised by the NAO for not understanding the effect that funding reductions were having on local authorities, their services and on citizens masterfully summed up by the C&AG commenting that, 'If you're going to do radical surgery it would be nice if you knew where the heart was; you're slightly more likely not to stick a knife in it by mistake.'<sup>49</sup>
50. By 2018, the department was praised by the NAO for having improved its understanding and having an improved evidence base on which to advise ministers at Spending Reviews and at other points<sup>50</sup>. However, information from other departments was highly variable in quality. Their analysis also tended to be high level, with little evidence that the departments had analysed distributional issues and understood how pressures differed across authorities with the same duties, for example geographically or by type. This matters for local government a great deal: budgets for services and functions need to be based on up to date accurate information about need and demand plus accurate information about councils' performance. The decision by the coalition government in 2010-11 to abolish the performance management regime for local government together with the Audit Commission means that there is a lack of information and hence understanding about the outputs and outcomes deriving from current levels of funding. The NAO pointed out in 2018 that there are many services areas where there is no activity data for their component activities, meaning it is not possible to discern the effect of funding reductions<sup>51</sup>.

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<sup>47</sup> [https://www.health.org.uk/reports-and-analysis/analysis/why-are-delayed-discharges-from-hospital-increasing-seeing-the-bigger?gad\\_source=1&gclid=CjwKCAiAkc28BhB0EiwAM001TUK9uQerV0DsrJqRE4KR4A6ouFR4mCMkIACEsgtTqhTfm8-PH8SsNB0CHm0QAvD\\_BwE](https://www.health.org.uk/reports-and-analysis/analysis/why-are-delayed-discharges-from-hospital-increasing-seeing-the-bigger?gad_source=1&gclid=CjwKCAiAkc28BhB0EiwAM001TUK9uQerV0DsrJqRE4KR4A6ouFR4mCMkIACEsgtTqhTfm8-PH8SsNB0CHm0QAvD_BwE)

<sup>48</sup> <https://www.gov.uk/government/statistics/planning-applications-in-england-july-to-september-2024/planning-applications-in-england-july-to-september-2024-statistical-release>

<sup>49</sup> <https://www.theguardian.com/politics/2015/mar/16/whitehall-oblivious-to-effects-of-cuts-says-spending-watchdog-chief>

<sup>50</sup> *Financial sustainability of local authorities 2018*, C&AG's Report, HC834, Session 2017-19, March 2019, paras 18 & 19 <https://www.nao.org.uk/wp-content/uploads/2018/03/Financial-sustainability-of-local-authorities-2018.pdf>

<sup>51</sup> *Financial sustainability of local authorities 2018*, C&AG's Report, HC834, Session 2017-19, March 2019, Fig 15 [Financial sustainability of local authorities 2018](#)

51. By 2021, the department had improved its financial oversight and understanding of the sector which deepened particularly during the COVID 19 pandemic. The sector welcomed the deeper engagement and also the department's ability to represent local government's issues within central government<sup>52</sup>. However, other government departments still lacked the department's understanding of local government finance and practical details of delivering specific schemes. This reflects findings from the NAO's previous work on local authority financial sustainability and needs addressing. The sector is not a fixed entity and understanding and oversight has to shift to keep up especially when considered alongside the lack of information about the outputs and outcomes about what local government is delivering<sup>53</sup>.
52. Lastly, there is no single point of understanding of local government in central government. Each department pursues its own policy and delivery without knowledge of other pressures which local government is subject to. Central government needs to develop an integrated understanding of local government and its pressures as a whole.
53. The sector needs a long term plan for financial sustainability and definition of what local government is there to do, which should underpin how local government is to be funded and from what sources, rather than the continued patching up and tweaking of the current unsustainable system. Any source of income to be considered should conform to certain principles: they need to be buoyant; progressive; fair; efficient and predictable. There is a growing dissonance between the fact that local government does not really control its resources in any real sense yet increasingly provides statutory services. This raises the accountability dilemma: as a citizen and council tax payer, what am I really holding my local authority to account for at the ballot box?

January 2025

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<sup>52</sup> *The local government finance system in England: overview and challenges*, C&AG's Report, HC 858, Session 2021-22, November 2021, p17 <https://www.nao.org.uk/wp-content/uploads/2021/11/The-local-government-finance-system-in-England-overview-and-challenges.pdf>

<sup>53</sup> *Local government finance in the pandemic*, C&AG's Report, HC 1240, 2019-21, March 2021, para 17 <https://www.nao.org.uk/wp-content/uploads/2020/08/Local-government-finance-in-the-pandemic.pdf>