

Briefing Paper

Local Government Finance Settlement 2004/2005

February 2004

Introduction

The Local Government Financial settlement that is announced every winter for the following financial year has always caused excitement amongst local authority chief financial officers who have wanted to analyse the implications for their authority as soon as possible after the announcement is made.

I remember one year when I was Director of Finance at Copeland Borough Council in West Cumbria, sending a member of staff down to the Government Office Northwest in Manchester on a motorcycle to collect the local government financial settlement. They then had to find a public telephone box from which to call the accountancy section with the news. One of the accountants then rushed into a meeting of the Policy & Resources Committee to give me the details so that I could announce the implications for the authority to the committee and to the newshounds from the 'Whitehaven News'. This was only about ten years ago!

The technology is now much better but the process remains much the same.

However, the settlement for 2003/2004 has made the process one that attracts greater public interest. Large increases in council tax that council tax payers found hard to understand led to the local government finance settlement moving up the political agenda and to it achieving a higher public profile. The 2004/2005 settlement therefore attracted more attention than usual. But why were there the problems in 2003/2004 and were the right answers found in 2004/2005?

The Background - Local Government Finance Settlement 2003/2004

In April 2003 the average increase in council tax in England was 13% but many authorities increased council tax by more than this with the largest increase of 45% being made by Wandsworth Borough Council.

The settlement was affected by:

- Mistakes in the population count
- Increases in education budgets were less than the amounts that had to be 'passported' to schools

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- Ceilings on grant increases dampened increases in the formula share for many authorities
- Specific grants increased to an eighth of the total budget

The turbulence caused by the move from 'standard spending assessments' to 'formula funding shares' was sufficient for ministers to decide to use 'floors and ceilings' to restart the scale of redistribution.

Such measures might just have been enough to stop a major shift in local tax bills and / or spending - but for the Department for Education and Skills insistence on the full 'passporting' of particular amounts of funding to schools.

"Essex County Council was one that was required to increase their schools spending by an amount greater than the overall increase in formula grant for all services. To make matters worse the removal of a proportion of Standards Grant Allocations left many individual schools in significant trouble". From 1998/99 to 2003/04 central government current expenditure increased by 32% while tax revenues increased by 26%. From 1997/98 to 2002/2003 local government current expenditure increased by 33%, but council tax rose by 51%.

Government expenditure plans and forecasts of local government expenditure imply similar real term increases in Council tax in 2004. Furthermore the Department for Education & Skills is requiring that every school should receive a guaranteed level of funding. As a result continued education 'passporting' is likely to oblige many authorities to make significant real increases in council tax and/or reductions in services outside education. Should childrens' social services be merged with education services in new trusts they would also be likely to be similarly protected. Should capping be introduced the solution would inevitably be major reductions in expenditure on services other than education.

However, referring to 2004 council tax levels, Nick Raynsford, Minister of local government said:

"We don't want to do it, but we cannot stand aside if there are repeated irrecoverable increase in council tax".

"There is a quite serious problem building up because of public resistance to incredibly large council tax increases"

Currently 26% of local government expenditure is funded by Council Tax and 74% is supported by central government. This produces the 'grants' mechanism reveals a 4% increase in Council Tax is needed to fund a 1% increase in local government spending or a 3% increase in Council Tax is needed to make up a 1% reduction in revenue support grant.

The government has reserved powers to improve either a borrowing limit on an individual council if it believes it is not being prudent, or a natural ceiling in times of macroeconomic crisis.

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The Pre-Budget Report – December 2003

In December 2003 the pre-budget report earmarked a £406million increase in central government support for local government budgets. Of this, £340million will be allocated to England in addition to the £420million that was announced in November 2003. According to the Chancellor this brings the total available to English councils to £3.6billion more than in 2003/2004 which provides English authorities with most of the £800million that they had requested and should allow them to levy increases in council tax of under 10%.

Gordon Brown, Chancellor of the Exchequer, said:

“The government will, to ensure next year reasonable levels of council tax, be prepared to use capping powers where appropriate and necessary.”

John Prescott, Deputy Prime Minister, said:

“The government and council tax payers now expect councils to deliver. Given this significant investment in local services and the scope for efficiency improvements, it is my view that next year local authorities can and should deliver council tax increases in low single figures.

“When considering whether to cap authorities I would have to look at the excessiveness of the budget. I would also expect to look at the size of the council tax increase.

“But it may well be appropriate to consider other matters such as how acceptable the rise in council tax is locally. Council tax payers do not want another round of high increases. If their councils think they do, why don't they allow local people to have their say in a local poll?”

Sir Jeremy Beecham, Chair of the Local Government Association, said:

“The money is more than just a sticking plaster measure... It points the way to a more fundamental change in local government finance to a fairer, more transparent and accountable system which will allow people to better understand the relationship between council spending decisions and the local tax they have to pay.

“This money may not be enough to prevent above inflation council tax rises in many areas, but it will certainly help.

“Councils will do their level best to keep council tax rises as low as possible.

“Councils should also receive additional rate income if they are successful in promoting small business creation. This could be £150million in 2005, £300million in 2006 and £450million a year thereafter.”

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Revenue Support Grant Settlement 2004/2005

The revenue support grant settlement for 2004/2005 shows increases for English, Scottish and Welsh authorities of 4.7%, 4.8% and 5.0% respectively. This compares with an increase for England of 5.9% in 2003/2004. However, district councils, that do not provide education services have received the lowest increases, many as low as 2.2%.

Nick Raynsford, Minister for Local Government, referring to the £120million increase in transitional funding for education, said:

"We have considered the point put to us by local government that, while they share our ambitions for schools, it might be difficult to fund these fully because of spending pressures elsewhere.

"This settlement will enable councils to deliver improved services at reasonable council tax levels.

"I have said many times the current trend in council tax rises is unsustainable. We do have targeted capping powers and we are prepared to use them.

"But with this settlement, there really should be no need for excessive increases."

The proportion of funding that is ring fenced will be reduced from 13.3% in 2003/2004 to 11.1% in 2004/2005 and below 10% in 2005/2006.

Bob Linnard, Local Government Finance Director at the Office of the Deputy Prime Minister, said:

"There has been a quite marked trend since 1997 of increasing ring fencing which has now been reversed.

"There are two agendas – giving more flexibility and power to local government (versus) delivering national priorities – and the government is trying to balance these."

The only reduction in ceilings has been for education authorities from 8% to 5.8%.

School budgets should be protected and £300million additional funding made available to childrens', environmental, protective and cultural services.

However, the Chartered Institute of Public Finance and Accountancy has warned that many types of council will be unable to balance budgets without increasing council tax. They calculate that for increases in council tax to be below 10%, increases in expenditure will need to be limited to 5.7%, much less than the forecast double-figure increase.

It is expected that most council will opt to reduce services rather than to make significant increases in council tax. However, as grant is 'passported' to schools this means that any savings will be made in other service areas.

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Jeremy Beecham, Chair of the Local Government Association, said:

“Government’s centralising solution for schools will leave many councils, including practically all districts, with a dilemma.”

Kit Malthouse, Conservative Deputy Leader of Westminster City Council, said:

“The government has ordered us to pay virtually all (the increase in grant) to schools. The burden of funding other services will now inevitably fall on council tax payers. The lack of discretion undermines our efforts and puts national demands ahead of local needs.”

Mark McLaughlin, Director of Resources at Enfield Borough Council has identified a funding gap in social services:

“Our needs, as per the formula spending share, have grown 6.8% but the grant goes up by only 5.8%.

“At the same time we are facing massive increases in residential care costs, huge growth in demand on both childrens’ and adults’ services and unknown cost increases because of the asylum seekers’ amnesty.”

Mark Hunter, Liberal-Democrat Leader of Stockport Borough Council, said in November 2003:

“Local Government has been dealt a body blow with the announcement of the annual financial settlement.

“Local Government minister, Nick Raynsford, should explain why a borough like Stockport Borough Council has received an increase of just 3.5% when the national average for councils with education and social services responsibilities is 5.1%.

“It is all well and good ministers claiming there is no need for large council tax increases, and threatening to ‘cap’, but what do they expect us to do if they are not giving us enough money in the first place?

“Mr. Raynsford, as the minister responsible, has a nerve to lecture us about ‘unreasonable increases’ in council tax when he has clearly failed to persuade his cabinet colleagues to provide us with the necessary resources to do the job properly.”

Preston City Council appears to have lost £1million in funding (4%) which could lead to a 13% increase in council tax. Bernard Hayes, Director of Finance, said:

“Once again, districts have lost out to upper tier authorities.

“Our members wont countenance a 13% increase in council tax, so we will be looking at service cuts across the board.”

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David Cook, Chief Executive of Kettering Borough Council, said:

"It seems clear that ministers felt under so much pressure on the education and social services front there wasn't much left in the cupboard for the districts."

David Rawsthorn Director of Finance Eden District Council said:

"You have reported that districts received a poor settlement of 2.2% to 2.9%. The reality appears much worse. Taking rent allowance and council tax benefit subsidy out of the RSG and paying it through the subsidy claim has big implications. It appears that the rent allowance changes will reduce the cash increase for many councils. If a council pays below average CTB as a percentage of total council tax, it will lose out here as well."

"Eden's cash increase of 2.9% amounted to £102,000, giving a net cash decrease: the impact on council tax is a 4% rise. Can anyone help me in explaining this to the district's council tax payers?"

Education Funding

Plans for education funding for 2004/2005 were announced in November 2003. They included a real terms teachers' pay freeze to help to guarantee schools' minimum cash increases, and more devolution of cash from councils to head teachers.

In 2003/2004 school spending increased by 11.6% but increases were spread unevenly. Many southeast councils found funding inadequate for increased teachers' pay, national insurance, superannuation and the loss of targeted funding.

Average pupil spending will rise by 5.5% in 2004/2005. Authorities will get a per pupil increase between 5% and 6.5%. Schools will get at least 4% more per pupil – or 3.4% where rolls are rising.

The Standards Fund which pays for school improvement will be increased and there will be transitional funding for authorities that were badly affected in 2003/2004.

Sir Jeremy Beecham, Chair of the Local Government Association, said:

"The sensible planning of local education can only be done in conjunction with spending decisions that take account of local needs and are integrated with other local services such as social services."

Doug McAvoy, General Secretary of the National Union of Teachers, said:

"The government intends that progress on the upper pay scale will be rationed and that all teachers will suffer a pay freeze until September 2006... There is insufficient money to employ the additional teachers necessary to implement the workload agreement."

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The government expects councils to passport, in full, the 4% per pupil increase even if that increase takes up the council's total grant increase. This is likely to reduce the ability of councils to use discretion to channel money according to need through local fair funding arrangements.

Sir Jeremy Beecham, Chair of the Local Government Association, said:

"The reduction of local discretion would allow councils little scope to direct funding where it is needed and some schools will be left short next year.

"We have won an assurance from Mr. Clarke that the education element of council grant will fund the 4% pupil guarantee. But the education element does not account for the majority of council spending.

"One of the flaws... is that it freezes the existing distribution and then tops it up in a way that doesn't reflect need.

"Most schools and many parents want increased provision for special educational needs, not less... The fact this is defined as central expenditure because it is spent by the council rather than the school is very misleading."

Steve Lord, Director of Local Government Finance at the Association of London Government, said:

"In the past, councils would have been able to assume efficiency savings across the whole authority – now they have been restricted to making savings in half their budgets."

Keith Mitchell, Leader of Oxfordshire County Council, said:

"We can manage for the next two years – our continual worry is that schools' balances are down to almost zero but schools will continue to have no real balances so there is no flexibility for the rainy day that will eventually come.

"It is excellent news for schools – but we must guard that this is not at the expense of services we provide to pensioners and other council tax payers."

Council Tax Capping

Nick Raynsford, Minister of State for Local Government, told the Local Government Association's finance conference that it was essential for local authorities to focus on greater value for money, delivering quality public services without raising council tax to unreasonable levels, and that re-introducing capping was a realistic possibility.

"We must all be clear that year on year increases in council tax at the scale (seen in 2003) are not acceptable to voters or to the government.

"We would prefer councils to be answerable to the electorate, but cannot stand aside if there is a continuation of unreasonable increases."

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Edward Davey MP, Liberal-Democrat spokesman on local government, said:

“However prudent and penny-pinching councils are, it is crystal clear the average increase in council tax will be over three times the rate of inflation – at least 8%.”

Cllr Ken Thornber, Conservative Leader of Hampshire County Council said;

“Top Councils were promised revenue freedoms and yet within months of becoming ‘excellent’ we in Hampshire now have the threat of capping hanging over us. The reason why we run the risk of capping is that the Government fails to fund us properly..... The Government must intervene and use its powers to reduce the burden of council tax increases”.

Tony Travers, Director of the Greater London Group at the London School of Economics said;

“How on earth could a Government committed to ‘new location’ end up threatening councils with a return to capping? Even authorities deemed ‘excellent’ and ‘good’ under the comprehensive performance assessment now face the possibility that the deputy prime minister will pursue them with a spending cap. So much for earned autonomy”

Gordon Keymer Conservative Leader of Tandridge DC said:

“It is fascinating to watch as ministers stick doggedly to their script on council tax increases in the face of contrary figures from the Treasury and a report from the Audit Commission. Deputy Prime Minister John Prescott talks about expecting next year’s council tax increases to be “in low single figures” while treasury expectations are for increases averaging 7% - far from a low single figure.

As far as shire districts are concerned, while the removal of the ceilings may have helped some, those on the floor have seen hardly any benefit from the additional £340m grant. My own council has received just £38, 000 more.

I have been critical of the Audit Commission in the past, but I have to thank them for being the catalyst for the extra £340m. The commission’s report on the reasons for the council tax increases last year is a good example of how it can best help local government and the public and where it should be concentrating its efforts.”

Nicholas True Conservative Deputy Leader of Richmond upon Thames BC said:

“The chancellor announced in his pre-Budget report an extra £340m for councils to help keep council tax rises down. But Richmond upon Thames LBC’s share of the payout is £3,300. This defies belief.

“Last month Richmond was told it was receiving the lowest Government grant settlement of any London borough and the second lowest for a unitary in England.

“The chancellor trumpeted this payout for councils as some sort of lifeline, but the amount Richmond will receive is less than derisory – 4p per household.

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“We will now be contacting deputy Prime Minister John Prescott’s office urgently to find out why such an insulting sum has been awarded to the people of Richmond. The borough desperately requires a fair deal to ensure services are properly funded and to keep tax rises to a minimum.

“Is £3,300 all the chancellor thinks our borough is worth? It is a huge insult”.

Consultation with Council Tax Payers

Some authorities have taken the advice of the Deputy Prime Minister and have consulted council tax payers.

A consultation exercise on how people in Cumbria would like their council tax to be spent has revealed a preference for focusing on vulnerable people.

Consultees were asked to make “trade offs” between different services in order to spend their limited budget, reflecting the way in which the council itself has to work.

Over a seven-week fieldwork period, 601 Cumbrian residents gave up an hour of their time to be interviewed.

The themes, which have emerged, are that services which provide support to vulnerable people (e.g. disabled adults, the elderly, special needs children and children at risk) are considered of greater importance than other types. People feel more should be spent on these services even if it has a negative impact on funding for others.

It also emerged that people are prepared to pay slightly more council tax so long as the services they consider a priority see the benefit. Despite calls for council tax cuts, there is very little support for making the reductions in service provision that would be necessary to achieve them. Fewer than 10 percent of respondents chose lower services levels for lower council tax.

Respondents also wanted an increase in service levels to ensure every child at risk has a social worker allocated to them; ensure no disabled children are awaiting a service; increase support to older people to reduce the level of unmet, non urgent need; allocate specific funding to tackle the problem of doorstep crime; increase educational spending for children with special needs; ensure no disabled adults are awaiting specialist equipment; increase funding to home care for the elderly; increase the number of young people offered apprenticeships with the county council; and increase the percentage of the road network covered by priority winter maintenance.

To help pay for these changes people said they were willing to see cuts through stopping production of the county council residents magazine, removing support from e-business club, downgrading maintenance of public rights of way, reducing the number of traffic calming schemes, reducing spending on animal welfare to minimum national standards, closing some small static libraries, reducing coverage of fire prevention schemes to urban areas only, reducing support for business growth in Cumbria, reducing support for subsidised bus routes, reducing the level of grants to the voluntary sector, and reducing spending on waste and recycling.

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The council is considering the findings in light of its statutory obligations and its existing spending commitments.

It is expected that the County Council will increase its council tax by 4.3%, but that a 27% increase in the police precept will mean that increases in council tax faced by council tax payers in the county will approach 10%.

Future Prospects

The government's efficiency review is understood to have been set a target of reducing local government spending by 7% by 2007/2008. It is understood to be believed that the greatest scope for savings is in:

- Procurement (shared services and collective procurement)
- Central Support services
- Frontline transactions

The swifter transfer of best practice and increased use of information and communications technology are seen as a way of achieving the desired savings.

Conclusions

Central government funds 74% of local government expenditure, and also wishes to influence levels of expenditure and council tax. Consequently the annual local government financial settlement continues to be the main determinant of the level of expenditure that a council can afford to incur and the level of council tax that it has to levy.

In 2003/2004 changes to the methods of distribution, education 'passporting' and local circumstances combined to produce very high increases in council tax in some areas. Politicians at national and local level, mindful of their prospects for re-election are obviously concerned that they should not be held responsible by the electorate for increases in council tax that are seen as excessive.

The government has therefore had to perform a delicate balancing act for 2004/2005. It has attempted to avoid high council tax increases by putting more money into the system and by threatening councils with council tax capping. At the same time it has continued to give a high priority to education spending, perhaps to the detriment of other services.

The Balance of Funding Review may make recommendations to change the regime for 2005/2006. However, it will need to make radical changes for the stresses that are currently evident in local government finance to be relieved.

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February 2004.

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