Northumbria University NEWCASTLE

Feb 02, 2024 09:35 GMT

EXPERT COMMENT: Four reforms to stop English councils from going bankrupt

In this article originally written for The Conversation*, Kevin Muldoon-Smith, Associate Professor in Strategic Public Sector Finance and Urban Adaptation at Northumbria University, and Mark Sandford, Honorary Professor of Local Government at the University of Bristol, discuss four reforms to stop English councils from going bankrupt.

England's councils are in serious financial trouble. Six including Birmingham, Nottingham and Croydon have effectively announced their bankruptcy, in the form of "section 114 notices", since 2020. Various others, including Somerset and Bradford, have warned in recent months that they might have to do the same. And now a cross-political party committee in parliament is indicating that the government must plug a £4 billion funding gap across the board.

This comes after years of council grant settlements not keeping pace with inflation, amid rising demand for services and increasing divergence between core funding and needs. While the government has just announced an additional £600 million to help address pressure on social care, amounting to a 7.5% increase in total funding, council grants saw an overall 40% cut in real terms from 2010-20 – including a 25% cut in non-social care funding.

With a general election coming up in the next year, there's an opportunity to think again. We recently carried out an international study of local government finance in Germany, Italy and Japan, in partnership with the Local Government Information Unit, a thinktank for council policy. We have four proposals for improving councils' financial resilience. Money is likely to be in short supply, so we mostly focus on alternative ways of using existing funds.

Proposal 1: rework needs assessment

In England, councils' financial requirements used to be assessed based on their relative needs. This was suspended in 2013 when a new policy meant half of all business rates were retained by local government. This has meant that councils' funding allocations have gradually diverged from the 2013 needs assessment.

The system was to have been reset in line with a future needs assessment via the government's "fair funding review" in 2016, but this is not now expected until 2025 at the earliest.

This situation makes England a significant outlier. In contrast, Germany, Italy and Japan all have mature and detailed needs assessment for local government, with reviews every couple of years. In each case, rates of local government insolvency have reduced following reforms in recent years.

England's fair funding review should be reopened and delivered, paving the way for yearly needs assessment. Whereas the 2016 version was to be restricted to only some council grants, it could be extended across the board. This would give councils greater latitude to allocate funding between their vast range of tasks, since they would not be restricted by ring-fencing or narrow grant objectives.

Proposal 2: equitable funding

Germany, Italy and Japan all redistribute taxes not only from the centre to municipalities but also between municipalities. This is known as territorial equalisation, and England is an outlier in lacking such a system.

Introducing this based on needs assessment would help remove the risk of section 114 notices. It would also help councils to plan for the future.

Proposal 3: a standing commission

Discussions between councils and the government about finances are ad hoc and haphazard. Neither side has an incentive to pursue a closer relationship: councils have few cards to play, and know that any gains would probably come at the cost of extra requirements. Witness the recent government announcement that, along with the £600 million funding for social care, councils are expected to follow new "productivity plans".

We propose a one-stop statutory body for handling financial negotiations between the government and local authorities. This would go hand-in-hand with needs assessment, since once there is a basis for understanding councils' requirements, there is more of a basis for negotiation.

This standing commission would also be a general discussion forum for consulting on government proposals, raising emerging issues, and mediating conflict. Indeed, the Institute for Government thinktank is proposing a similar body for metro mayors and their combined authorities, but we think all councils would benefit from such a forum.

It would help build trust and reduce the constant worry, noted by the Institute for Government in 2014, that local authorities will "do something barmy". Moving away from the current top-down relationship would be unfamiliar, but this was true in Italy and Japan 20 years ago, and both have pulled off a similar transition. Germany, Italy and Japan all have comparable standing commissions.

Proposal 4: assign national taxes

Councils in Germany, Italy and Japan all receive revenues from a range of national taxes. Most come from "assigned revenues" rather than local rights to set tax rates. In Germany, for example, 25% of national VAT revenues go to councils, distributed according to a needs-assessment.

English councils could receive a fixed percentage of revenues from one or more national taxes, such as income tax, VAT, employers' national insurance, corporation tax or stamp duty. Again, this could be distributed by needs assessment.

It's sometimes proposed that councils should raise more of their own taxes – but this could lead to richer areas raising more money per head. Our proposal avoids this and improves on councils' heavy reliance on council tax and business rates. It would also symbolise that central and local government are partners in public service delivery.

Implementation

Our first three proposals could be introduced fairly quickly and lay the foundations for a more stable system. The standing commission could then optimise territorial equalisation through negotiation, and explore how to assign national tax revenues. This would emulate the Trinity Reform in Japan during the early 2000s, which created a legislative framework that made it possible to rework local-government finance.

Of course, councils only occupy a small corner in public consciousness. They have only a walk-on role in health, immigration and crime. It might be tempting for a new reforming government to regard their financial failures as a minor inconvenience that can be tolerated when there are bigger fish to fry.

Yet we all rely on councils for core public services, including social care, roads, waste and planning. They play a vital role in planning and regeneration, community safety, decarbonisation and energy efficiency. In short, they are critical delivery partners for any UK government. If financial difficulties hobble them, the government loses time and capacity too.

*This article was originally published by The Conversation. Please see here for republishing guidelines.

Contacts

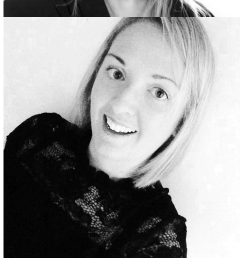
Rik Kendall
Press Contact
PR and Media Manager
Business and Law / Arts, Design & Social Sciences
rik.kendall@northumbria.ac.uk
07923 382339

Andrea Slowey
Press Contact
PR and Media Manager
Engineering and Environment / Health and Life Sciences
andrea.slowey@northumbria.ac.uk
07708 509436

Rachael Barwick
Press Contact
PR and Media Manager
rachael.barwick@northumbria.ac.uk
07377422415

James Fox
Press Contact
Student Communications Manager
james2.fox@northumbria.ac.uk

Kelly Elliott
Press Contact
PR and Media Officer
kelly2.elliott@northumbria.ac.uk



Gemma Brown
Press Contact
PR and Media Officer
gemma6.brown@northumbria.ac.uk