Is austerity over? The 2020 Spending Review and the outlook for local government funding

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Sizeable funding boost in 2020-21

Settlement highlights 4.3% real-terms increase in funding

- Additional £1.3 billion from grant and BRR baseline funding
- Additional £1.6 billion from council tax

Much more generous than any settlement in last decade, but

- Ending of most business rates retention pilots
- Assumes tax base growth of 1.9%, which would require further significant falls in cost of Council Tax Support schemes
- Will undo only a small part of the funding cut councils have seen over last decade

Extra funding could undo up to 1/5th of peak-to-trough fall in spending per person

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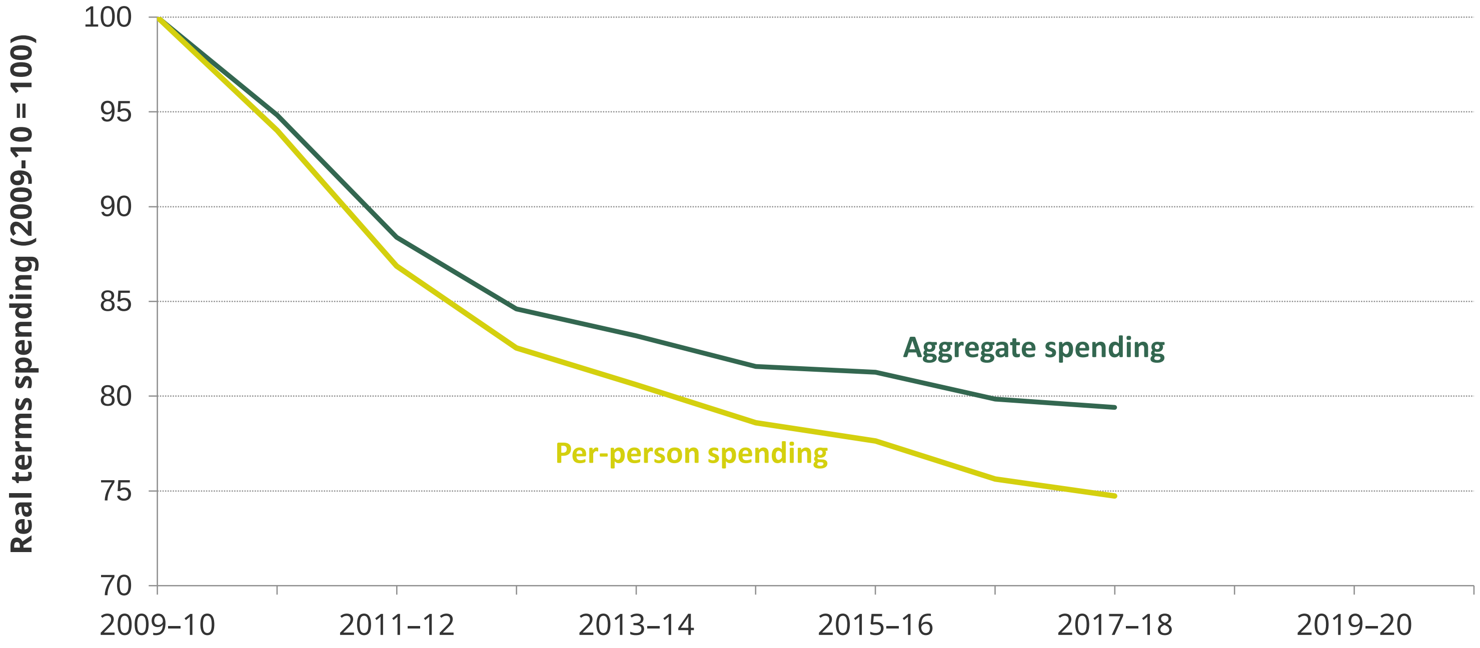

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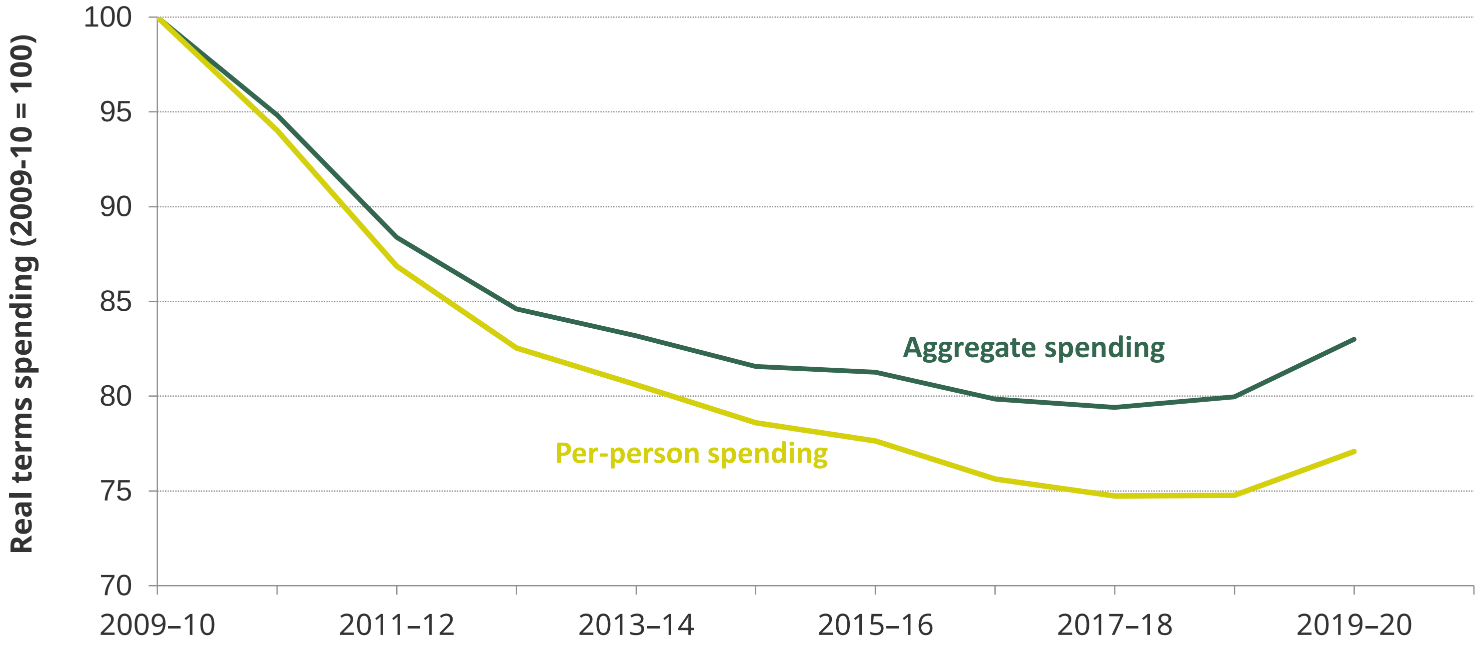

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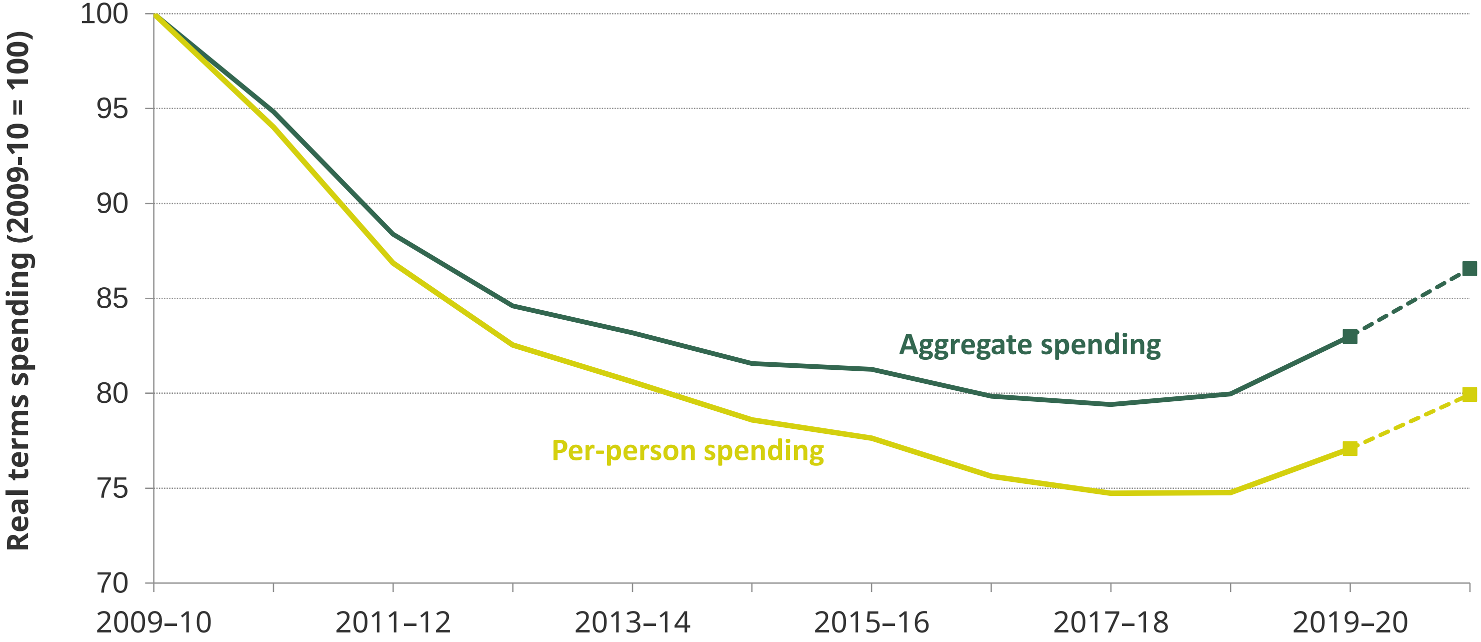


Plans for 2021-22 & beyond (I)

Conservative manifesto pledged little additional funding for councils

- Maintain new £1 billion social care grant for duration of parliament
- Extra £0.5 billion a year for road maintenance (‘potholes’)

Spending Review 2020

- Overall spending envelope set in Spring Budget?
- Departmental allocations (inc. MHCLG) by time of Autumn Budget

Plans for 2021-22 & beyond (II)

Business Rates Retention

- Consultation on detailed proposals later this year, implementing next

Fair Funding

- Consultation on detailed proposals later this year, implementing next

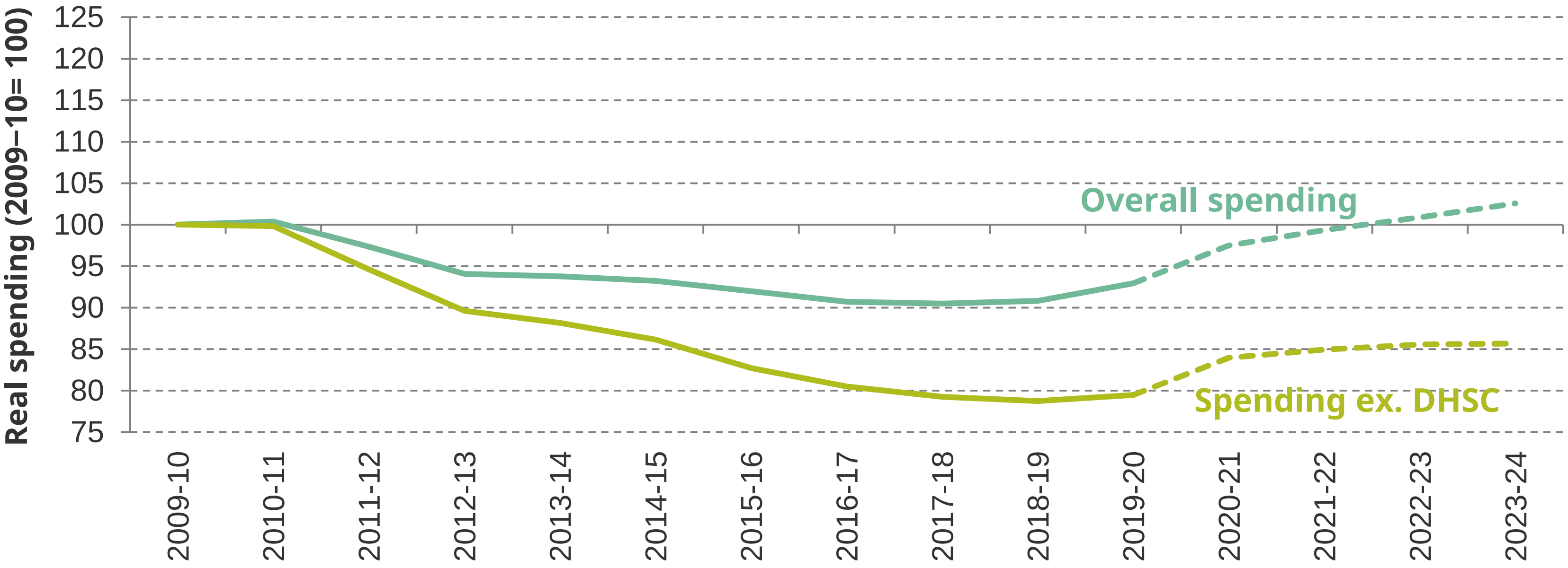
New Homes Bonus to be phased out

English devolution White Paper later this year

Social Care plans – "build a cross party consensus"

- Exemption of main residence from means test is big unfunded pledge

Overall day-to-day spending set to exceed 2010 levels by 2022-23, but outside health still down 15%



Note: All figures denote public sector current expenditure in resource DEL (PSCE in RDEL). Government spending plans do not exist beyond 2020–21: we assume that in the absence of the election, the government would have frozen all spending outside of the NHS and schools in England in real terms between 2020–21 and 2023–24; this is consistent with the Conservative manifesto.

Capital spending – potential for big increases

Conservative manifesto pledged to borrow £100 billion more than previously planned over this parliament to boost capital spending

- Includes money for potholes, flood defence, social housing energy efficiency, 'intra-city' transport etc.

But most of the extra capital spend is still to be allocated

- Strong hints that impact on geographical inequalities will be a more important determinant of funding allocation in future
- How much will come to (northern, midlands, coastal) councils as part of devolution plans?

How could these plans change?

Over the last four years, government has consistently topped up spending

- Seems unlikely will actually want to freeze spending outside health, schools
- But little leeway in new (looser) fiscal rules, so will it bust them or put up taxes (where it has also hedged itself in)?

The B word

- Still a risk of no-deal Brexit
- If this takes place likely short-term spending boost to support economy, but in long-run probably mean more spending cuts / tax rises

Positive or negative shocks to economic outlook

- Recently spent windfalls but borrowed to cover shortfalls – risky?

What about local government in particular?

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75% rates retention due in 2021-22

- Stronger local financial incentives for property development/growth
- A more financially self-sufficient local government sector?

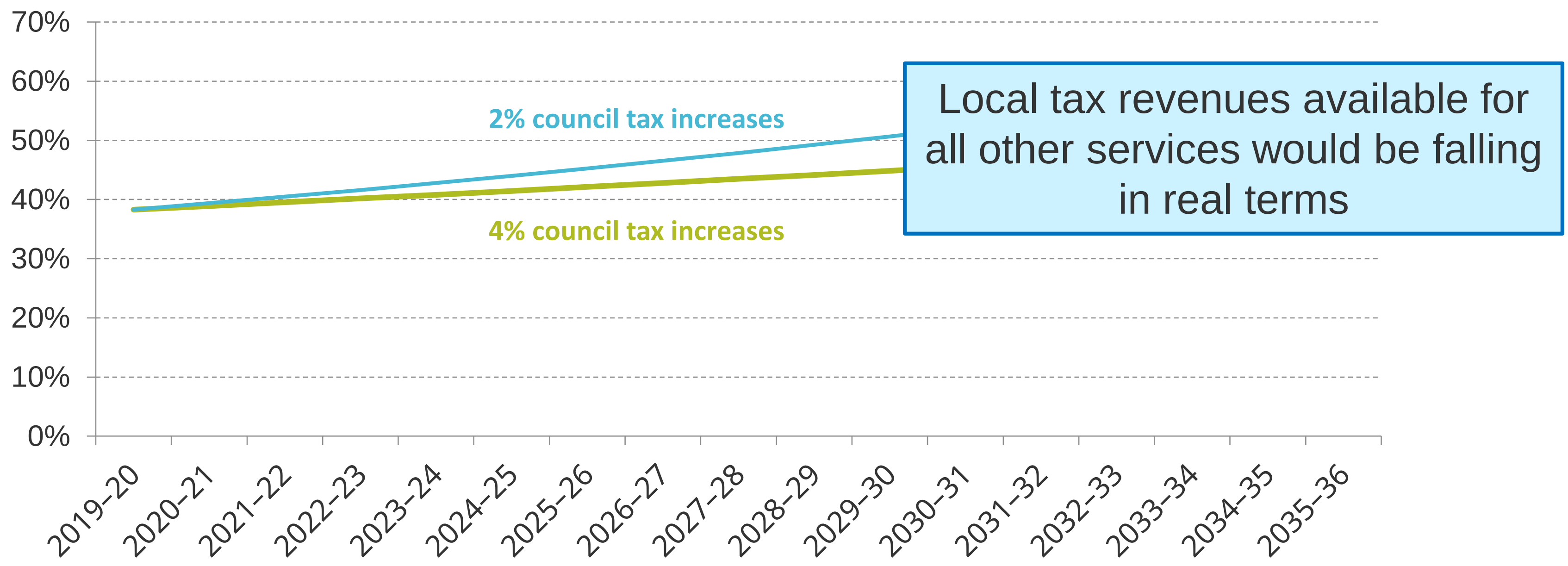
Govt will still have levers to give to / take from councils though

- Choice of retention rate and grants/responsibilities to be rolled in
- Net tariff or top-up to system to remove/add funding
- Level of any remaining grants, and whether other revenues devolved

Councils will face a range of spending pressures

- Ageing population and increasing needs; rising labour and other costs

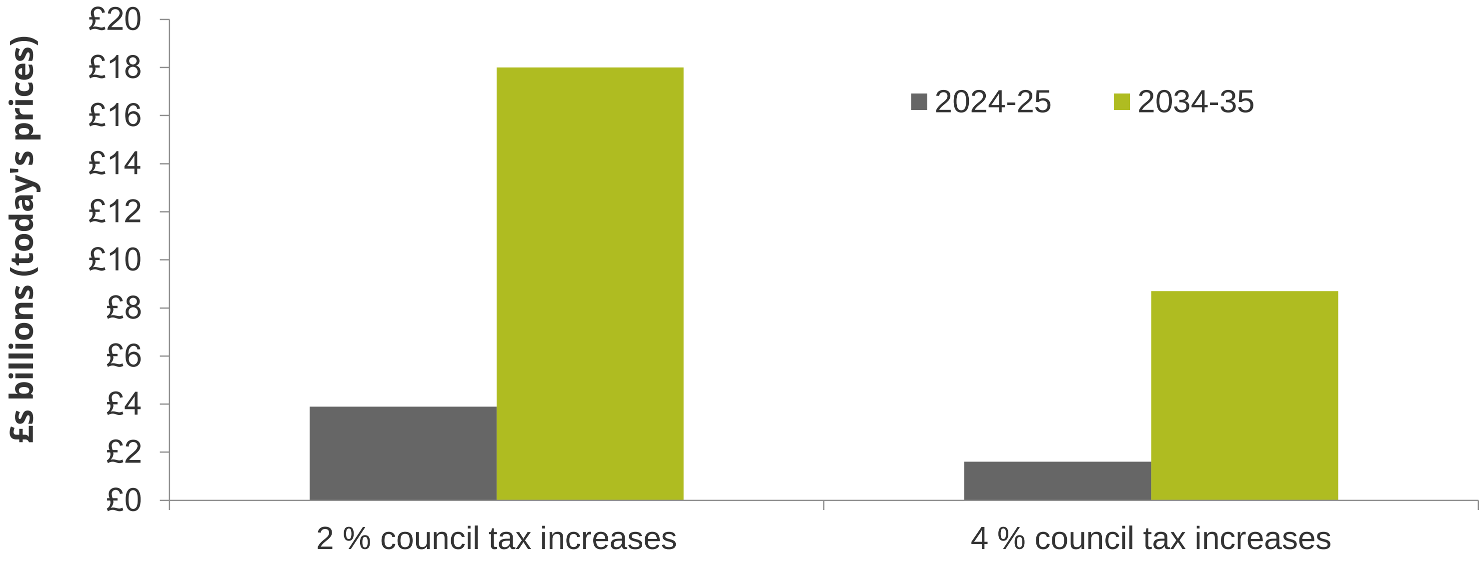
Under OBR central projection, adult social care will take up growing share of local taxes…



Note: Assumes adult social care costs increase by 3.4% a year in real terms – in line with OBR central projection

Billions in additional grants likely needed to top up existing local taxes

In order to stop spending on other services falling as % national income:



Note: Assumes adult social care costs increase by 3.4% a year in real terms – in line with OBR central projection

So what to do?


Improve productivity performance significantly or accept councils can do (even) less
Raise more revenues either nationally or locally
Raise nationally if prioritise redistribution and consistency
Raise locally if prioritise incentives and discretion

Tax devolution options

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100% business rates retention would transfer £6 billion to councils

Administratively straightforward

But narrow and unbuoyant tax base

1p flat-rate local income tax would raise about £6 billion for councils

Administratively more complex – though less so than VAT, Corporation Tax

But a range of desirable properties – buoyancy, accountability, incentives

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IFSBriefing

Taking control: which taxes could be devolved to English local government?

In recent years, there has been renewed interest in the question of tax devolution to local government:

- The past decade has seen a number of changes to how local government is funded, including the introduction of business rates retention. Broadly, these changes have focused on giving councils more control over their funding and providing stronger financial incentives to councils to drive local growth and development. Devolution of additional tax revenues and powers could be seen as a natural extension of this agenda.
- After years of cuts, councils in England face serious short-term funding pressures. In the longer term the costs of funding social care are likely to increase faster than the revenues councils receive from council tax and business rates. While these issues could be addressed by using national taxation to increase the grant-funding given to councils, devolution of additional tax revenues and powers could also play a role.

This note summarises a new IFS report on the scope for tax devolution to English local government. It sets out criteria which can be used to assess

Summary

Plans imply real-terms freeze for spending outside health & schools

- Recent history suggests government likely to top these up
- But sustainability depends on willingness to put up taxes and economic performance – and still a risk of no-deal Brexit at end of the year

Continued above-inflation increases in council tax would mean councils budgets continuing to increase in 2021-22 and beyond

- But unlikely by enough to meet rising costs/demands of services
- Reduce services? Keep & increase grant funding or devolve additional taxes?

Plans for devolution and social care reform must be consistent with funding levels and system – opportunity for coherent package rather than piecemeal policymaking

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