

Financial precarity in English local government

Peter Eckersley

Causes, potential solutions and future challenges

Readers of *Progressive Review*, and particularly those drawn to an issue that sets out the scale of the challenges that face the new Labour government, will be very familiar with the impact that austerity has had on the public realm since 2010. These impacts have been particularly acute at the local level in England, and especially in deprived communities.¹ A spate of local authority ‘bankruptcies’ in major cities such as Birmingham and Nottingham, which involve chief financial officers issuing ‘section 114 notices’ to inform ministers that their expenditure will exceed their revenue over the course of a financial year (something that is illegal under the Local Government Finance Act 1988), have only served to illustrate how widespread the problem has become.²

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Although local government did feature in the government’s first King’s Speech, new legislation is likely to focus on extending devolution ‘deals’ to other parts of England rather than dealing with the financial challenges that councils are facing. Nonetheless, since local authorities will need to play a key role in implementing the government’s broader agenda, ministers will have to address concerns about their long-term financial viability before too long. This requires them to take account of the multiple causes of the problem, as well as consider the potential solutions. Conveniently, some possible solutions have been in development for some time, including a ‘fair funding review’ for English councils and a new system of local public audit.

IDENTIFYING THE PROBLEM: LOWER REVENUES AND HIGHER DEMAND

The scale of austerity cuts to local government in England, particularly in deprived areas, has been well documented.^{3,4} Overall, central funding to councils fell by 46 per cent during the 2010s. Although ad hoc funding schemes to address emergencies such as the Covid-19 pandemic and the sudden energy price rises triggered by Russia’s invasion of Ukraine halted the overall trend, central funding for local authorities will still be 9 per cent lower in real terms (and 18 per cent lower per head of population) in 2024/25 compared with 2010/11.⁵ At the same time, restrictions on

1 Shaw J (2024) ‘Local government: a northern experience’, *Progressive Review*. <https://doi.org/10.1111/newe.12384>.

2 Hoddinott S (2023) ‘Local government section 114 (bankruptcy) notices’, Institute for Government website. <https://www.instituteforgovernment.org.uk/explainer/local-authority-section-114-notices>.

3 Lowndes V and Gardner A (2016) ‘Local governance under the Conservatives: super-austerity, devolution and the “smarter state”’, *Local Government Studies*, 42(3): 357–375.

4 Gray M and Barford A (2018) ‘The depths of the cuts: the uneven geography of local government austerity’, *Cambridge Journal of Regions, Economy and Society*, 11(3): 541–563.

5 Ogden K and Phillips D (2024) *How have English Councils’ Funding and Spending Changed? 2010 to 2024*, Institute for Fiscal Studies. <https://ifs.org.uk/publications/how-have-english-councils-funding-and-spending-changed-2010-2024>.

increasing the rate of council tax,⁶ and on how authorities can spend revenues generated from fees and charges such as parking,⁷ mean that local government in England operates within a much more constrained financial context than in comparable countries. Poorer areas face even bigger challenges, since their revenues from business rates tend to be lower (because they have fewer large firms operating within their areas) and they cannot raise as much income through council tax (because far fewer homes fall into the higher rate bands, and therefore a flat increase of 4 per cent, for example, does not generate as much extra revenue).

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Although some councils have sought to generate revenues in new ways (such as by borrowing to invest in shopping centres, office blocks and other property, and leasing them out to tenants at commercial rates), several of these schemes ended in high-profile failures – and those that are still operating have not necessarily placed their authorities on a more secure financial footing.⁸ Other ad hoc pots of money, such as the Towns and Levelling Up Funds that sought to replace EU funding after Brexit, comprised only a fraction of the amounts available through their predecessor schemes. Crucially, councils also had to bid for this funding through a competitive process that was fraught with political controversy and highly resource intensive.⁹

Ultimately, the system for funding local government in England requires fundamental reform: council tax is still based on property values from 1991 and is inherently regressive, and the formula used to calculate central funding schemes is opaque and not based on a comprehensive analysis of local needs.¹⁰ Additionally, following the abolition of the Audit Commission in 2015, there is very limited oversight of how councils are spending money – which means there is no early warning system to highlight if and when authorities might need to issue section 114 notices in future.

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At the same time, demand for local services has risen substantially over this period. Local government is responsible for social care, and there are now far more older people in England who require this assistance than in 2010. Indeed, adult social care accounted for 43 per cent of all local authority spending in 2019/20, up from 35 per cent in 2010/11.¹¹ Alongside higher energy prices, and increasing demand for homelessness, children’s and welfare services, councils are now faced with much larger bills than was previously the case. Moreover, the vast majority of frontline local services are delivered based on need. As with the constraints on the revenue side, therefore, councils have almost no control over demand. Given that they are required by law to deliver balanced annual

6 If a local authority wishes to increase council tax by a rate higher than that set out by ministers, it has to gain approval for the increase through a local referendum. As of summer 2024, only one council – Bedfordshire in 2015 – has ever held such a referendum and local people voted against the idea; see Stacey K (2024) ‘Rishi Sunak criticises local authorities for requesting steep council tax rises’, *The Guardian*, 9 February 2024. <https://www.theguardian.com/money/2024/feb/09/rishi-sunak-criticises-local-authorities-council-tax-rises>.

7 By law, English councils must spend any revenues generated from parking charges and fines on running parking services or on local transport projects.

8 Pike A (2023) *Financialization and Local Statecraft*, Oxford University Press.

9 Pope T (2023) ‘The Levelling Up Fund will not deliver on the government’s flagship agenda’, Institute for Government website. <https://www.instituteforgovernment.org.uk/comment/levelling-up-fund>.

10 Sandford M (2024) *Local Authority Financial Resilience*, House of Commons Library. <https://commonslibrary.parliament.uk/research-briefings/cbp-8520>.

11 Ogden K and Phillips D (2024) *How have English Councils’ Funding and Spending Changed? 2010 to 2024*, Institute for Fiscal Studies. <https://ifs.org.uk/publications/how-have-english-councils-funding-and-spending-changed-2010-2024>.

budgets, we should not be surprised that they have focussed on reducing the scale and scope of frontline service provision,¹² as well as back-office corporate and strategic policymaking functions,¹³ in order to prevent overspends. As we have seen with the spate of section 114 notices since 2021, however, even the most drastic cuts to spending in places like Birmingham have not prevented some councils from acknowledging that they cannot balance the books.

POTENTIAL SOLUTIONS: OFF-THE-SHELF IDEAS AND NEW THINKING

Academics, think tanks and policymakers have been discussing the problems outlined above for many years, and have suggested multiple ways to try to address them. These include reforming council tax (including by revaluing properties and/or introducing new payment bands), or replacing it altogether with a local income, sales or land tax. However, although the current system is hugely outdated and inequitable, some of these alternatives would not remove the risk that deprived areas fall further behind. Not only do residents in poorer places earn less and spend less, but land values are also lower. Particularly given the fact that demand for local public services in these areas tends to be higher, we can see that poorer councils would not be able to generate sufficient revenue to cover their necessary spending – unless a comprehensive national funding transfer system operates in parallel with local taxation.

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In addition, most Western democracies levy some kind of property tax, and often at the municipal level, because it is difficult to avoid payment, is clearly linked to the locality and acts as a reasonable proxy for wealth. Although land taxes are similarly difficult to avoid and clearly connected to place, land values vary hugely across the country and therefore this option would not remove the need for frequent revaluations. For their part, sales taxes tend to be regressive (because poorer people spend a larger share of their income than wealthy people), and richer people tend to be more mobile and therefore find it easier to avoid paying income tax. As a result, any replacement for council tax would need to be accompanied by a national redistributive mechanism of some kind, and may not necessarily be better than a local property-based system.

The current system for revenue redistribution is also inadequate and outdated. In response to various select committee reports about local government finance prior to the 2024 general election, the previous UK government promised to revisit the needs assessment upon which it bases council funding allocations. However, despite being launched in 2016, and being subjected to a long consultation period, this long-awaited ‘fair funding review’ is still to be published. It may well be, though, that civil servants can pull any preliminary work out of a metaphorical filing cabinet in Whitehall and update it for the new government accordingly. Key elements should include a clearer needs-based formula for central funding of local authorities (which is kept under review and authorised by parliament) and a comprehensive, independent review of how councils could and should raise money locally.

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12 Webb JR and Bywaters P (2018) ‘Austerity, rationing and inequity: trends in children’s and young people’s services expenditure in England between 2010 and 2015’, *Local Government Studies*, 44(3): 391–415.

13 Eckersley P and Tobin P (2019) ‘The impact of austerity on policy capacity in local government’, *Policy & Politics*, 47(3): 455–472.

To balance out regional inequalities, other countries adopt very different approaches to local government finance, including ‘shared’ taxes (whereby different tiers of government receive an agreed percentage of revenue from different taxes levied at the national level) and constitutionally embedded systems of territorial redistribution.¹⁴ Should the new government establish an independent commission to review the local government finance system, this body should consider such mechanisms. If the new government decides to retain council tax, it should propose legislation to ensure that properties are revalued at regular intervals to update the tax base. It should also consider raising or abolishing the level at which an increase requires an authority to hold a referendum to endorse its decision. Crucially, Keir Starmer did not rule out a change to the council tax system when questioned about it during the election campaign (whereas he did promise not to increase the rates of income tax, national insurance or VAT). This provides the new government with some room for manoeuvre, as and when the financial crisis facing local government becomes even more apparent.

Additionally, the system of local public audit needs fundamental reform. Since this function was essentially privatised in 2014, and local authorities were allowed to appoint their own auditors, ministers, civil servants and councillors have had much less oversight of local government finance, and audit reports into nearly every English council have been delayed.¹⁵ The previous government belatedly recognised that this was a problem, and launched an independent review, led by Sir Tony Redmond, which made a series of recommendations that incoming ministers should seek to adopt.¹⁶ These included improving training for auditors, revising the fee structure, requiring auditors to submit their annual reports to full council meetings, ensuring that auditors and inspectorates share any concerns they may have with each other and – crucially – setting up a new public body to lead, regulate and manage public audit. Such changes would help to provide politicians and officials at both central and local levels with a better understanding of potential vulnerabilities, and deal with financial problems in councils as they arise.

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CONCLUDING THOUGHTS

Ultimately, questions about local government finance touch on the issue of local government itself: what it is – or should be – *for*, and how it should relate to the centre of government. To what extent should councils be free to levy taxes, spend money and shape places as they wish? Should they exist primarily as delivery arms for central policies, or do they also have a key role to play in shaping local communities? Ultimately, whom do they exist to represent?

Local authorities in the UK are very unlike their counterparts elsewhere, in that they tend to cover large geographical areas and very large populations that do not always correspond to local identities. This is the result of a longstanding belief in the administrative superiority of larger governmental units, rather than any wish to ensure that local government represents identifiable local places.¹⁷

14 Muldoon-Smith K, Walker A and Stride G (2024) *Learning from Local Government Finance across the World: Proposals for improving the financial resilience of local government in England*, Local Government Information Unit. <https://lgiu.org/publication/learning-from-local-government-finance-across-the-world>.

15 Only 1 per cent of local authority accounts for 2022/23 had their audits published by the 30 September deadline; see National Audit Office (2023) *Progress Update: Timeliness of local auditor reporting on local government in England*, National Audit Office. <https://www.nao.org.uk/reports/progress-update-timeliness-of-local-auditor-reporting-on-local-government-in-england>.

16 Murphy P, Lakoma K, Eckersley P, Dom BK and Jones M (2023) ‘Public goods, public value and public audit: the Redmond Review and English local government’, *Public Money & Management*, 43(3): 242–250.

17 Copus C and Leach S (2023) *The Strange Demise of the Local in Local Government: Bigger is not better*, Palgrave Macmillan.

Indeed, the previous government's direction of travel continued in this direction, by emphasising the role of large, subregional metro mayors and combined authorities. Starmer and his team appear to have bought into this idea, and have been less forthcoming in setting out their vision for what we might call 'traditional' local government. Nonetheless, working on the basis that Starmer's team recognise the key role that councils need to play in addressing challenges such as lacklustre economic growth, climate change and endemic poverty, we could see a revitalisation of subnational government in England in the coming years. The challenge of rebuilding capacity within local authorities – as well as in other public bodies – will be difficult, but is necessary to ensure that the state can deliver on all parts of the government's agenda.

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