Confidential

PG/31/75/7

LOCAL GOVERNMENT FINANCE

an interim report

1. The future of rates

We have taken as a basic assumption and background to policy thinking, the October Manifesto pledge to abolish domestic rates recently confirmed by the Shadow Cabinet. We have retained this as central to our policy, whatever Layfield may recommend, but clearly the detailed consideration of alternative local revenue sources would be best left until Layfield has reported.

We take the view that the abolition of all rating must be seriously considered. Without domestic rates, the political sanction of the system will virtually disappear. Industrial and commercial ratepayers would be vulnerable to punitive increases from some councils and would lack any representation to specifically match this taxation.

The advantages of the total abolition of rates would include considerable saving in manpower in the Inland Revenue valuation division, as well as the saving of the costs of administration and payment of the rate rebate scheme. The abolition of rates has implications for water supply charging, but we are maintaining close links with the Water Cycle Policy Group. We wish to consider further the implications of abolishing commercial and industrial rates, because at the present time we need more information about the effect of abolition on the yield of corporation tax.

We have concentrated in our early meetings on the question of controlling the total amount of local government expenditure.

2. The shortcomings of the present system

Quite apart from the disadvantages of the rating system (its inherent unfairness, falling on householders only, its regressive nature, and its lack of buoyancy) there are serious shortcomings in the overall control of local government finance. The Rate Support Grant negotiations establish an agreed sum of 'relevant' expenditure by local authorities which will attract exchequer grants, but this in no way represents the total spending of local authorities. Furthermore there is no statutory way of limiting the rate call of local authorities through the grant mechanism.

The Rate Support Grant order negotiations have their own inflationary momentum, as Colin Jones pointed out in an article in the Financial Times on 7th May, because the negotiations are not based on the result of the RSG negotiations of the previous year, but on the estimated outturn expenditure of that year. There is another inflationary factor in the operation of the Rate Support Grant (increase) order, because local authorities know that they have the safety net of the increase order to contribute retrospectively to their expenditure.

Finally, the cushioning of domestic ratepayers through the domestic element, as well as rate rebates, largely neutralises the deterrent effect of rates on spendthrift councils, which is claimed by enthusiasts for rates. There are, in any case, other more effective methods of making the electorate feel the impact of injudicious budgeting by councils.

3. A Ceiling on local expenditure

The priority is to identify an effective way of controlling or abating growth in local government expenditure. In a time of high inflation, this is even more vital. We take the view that the real freedom of local government is in the decisions taken concerning the provision of services and the spending of money, rather than in the raising of revenues, and that, given a larger element of discretion in the conduct of powers and duties and provision of services, local authorities will accept a more stringent control over the total amount of their expenditure. (We would expect some reduction in staff at DoE, DES and DHSS, if Central Government scrutiny of individual local services was removed.) We propose that the Central Government should, through negotiations between DoE and the local authority associations, determine in advance, the total level of expenditure appropriate in the following financial year. Ninety per cent of this sum would be provided by the Exchequer as a grant or Local Government Allocation (LGA) from centrally-raised revenue. Ten per cent would be raised locally.

4. The Local Government Allocation

The Local Government Allocation would be expressed in terms of cash limits, and there would be no provision for an increase order. The negotiation would be based on the needs and services of the local authorities, but we would hope that the formula used would be simpler than that at present used for RSG.

With the abolition of domestic rates, it will be possible to simplify considerably the calculation of exchequer aid. It will be possible to dispense with the domestic element entirely, and if all rates were abolished, the resources element would also go.

The LGA would be made in separate payments to counties and districts. There would in effect be four different LGAs, paid to Metropolitan Counties, Metropolitan Districts, non-Metropolitan Counties, and non-Metropolitan Districts.

5. Monitoring

To ensure that local authorities generally contain expenditure within the Local Government Allocation, there must be more scrupulous and sophisticated monitoring of manpower and expenditure. This should be operated jointly by the Local Authority Associations, the DoE, and the Consultative Council on Local Government Finance. The latter may need to be reconstituted.

6. Problems arising from cash limits

While we favour the imposition of cash limits for local authority expenditure, we recognise that there may be a number of contingencies which lead to overspending or local authorities running out of money before the financial year ends. These are:

a) unexpected levels of inflation. To contemplate an increase order to keep pace with inflation would run counter to the cash limits principle. In this circumstance, the authority must make economies by cutting capital expenditure schemes first, and then reducing services or standards or running down staff.

b) additional duties or commitments given to local authorities by Central Government. In the introduction of legislation or nationally-agreed pay settlements, Parliament or Central Government add to the outgoings of the local council. In these circumstances, a specific grant should be made in respect of the cost of the additional commitments during the financial year.

We suggest that wherever appropriate, new legislation should be accompanied by an appraisal, agreed with the Local Authority Associations, of the revenue and manpower implications for local authorities. The same should apply to loan sanction for capital projects. The revenue implications of loan sanction for, say, new nursery school buildings must be recognised. We feel that the spending departments of Whitehall must adopt a corporate approach within the Government in their relationship with local government.

c) local extravagance or slack budgeting. Where the local authority is directly responsible for overspending, they should not be rescued by Central Government, but should have the option of either cutting their capital programmes, reducing their services, or levying a charge, with the approval of the Secretary of State, on all their electors in that financial year. This would have the merit of identifying the extravagance of the local council with the hardship experienced by the electorate. The charge will not be operated as a regular source of local revenue but only as a sanction against profligate spending.

d) unexpected contingencies, for example, natural disasters, oil pollution or the influx of large numbers of immigrants, will obviously place extraordinary pressures on local authorities and special arrangements would have to be made in these cases.

7. Budgetary programmes

We believe that there is scope for more flexibility in the budgeting of local authorities and in particular that it should be possible to transfer money from capital to revenue accounts and vice versa, to alter priorities and bring in new options as circumstances change.

We are considering the merits of rolling quinquennial budgetary cycles of both capital and revenue expenditure.

These would provide the flexibility needed, but would have serious implications for the operation of key sector approval for loan sanction. We wish to study the question of finance for capital expenditure in more detail.

8. The county precept

We recognise that, particularly in Metropolitan areas, there is considerable dissatisfaction with the levying of county precepts. District councils resent having to collect money for a County Council, which might be controlled by a different Party, or ILEA, or the Water Authority. It also provides an alibi for the council which attempts to conceal its own financial weaknesses. With the abolition of domestic rating, we think the time is opportune for abolishing precepts, and giving each authority its own revenue.

We expect Regional Water Authorities to move to direct billing over the next few years, and this is also the view of the Water Cycle Policy Group. The special arrangement for the Police Authority to bill County Councils should be retained. The LGA would be paid separately to counties and districts, within and outside metropolitan areas, and such additional locally-raised revenue as may be approved would also be collected by each authority.

9. Locally-Raised Revenues

Returning to the question of rating, we accept that, in spite of its advantages, this tax is not suited to the scope of services provided by local government today. We agree that about ten per cent of local authority revenue should be raised locally through buoyant and progressive taxes. We shall look at this in more detail at a later stage in our discussions, taking account of the findings of the Layfield Report.

10. Local Authority Services

It is not the policy of the Party to reorganise local government, and certainly not to leave half open doors for the advocates of regional government. We recognise, however, that the 1972 reorganisation has created a number of problems, particularly in the duplication of services at county and district level and at Whitehall, continual bickering over agencies, and increases in staff. At a later stage we intend to review services, function by function, to remove duplication, and to see if they are properly in the public sector.

11. Manpower

The Government estimates that 55 per cent of the cost of local government is taken up by salaries and wages. Local Government is a labour intensive service, and is, thus, particularly susceptible to wage inflation. The Government has recognised this in its Remuneration Charges and Grants Bill by taking powers to withhold RSG from Authorities which disregard pay limits.

Reorganisation undoubtedly generated increases in both staffing and salary levels. It is estimated that the planning requirements of the new authorities represent a seventy per cent increase over pre-1972 staff numbers. Increases in population of the new district councils also led to a unique spiral of pay inflation, largely for senior officers' salaries.

We believe that the manpower requirements of all local authorities should be strictly monitored.

We know that nationally-agreed pay settlements for the police and teachers are subject of the direct approval of the Home Secretary and Education Secretary respectively. We believe that pay agreements negotiated through the National Joint Council for other local authority employees should be subject to the approval of the Secretary of State for the Environment.

Conservative Research Department,
24 Old Queen Street,
London SWI

AJMHJCG
23rd July 1975