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CABINET

STEERING COMMITTEE ON LOCAL GOVERNMENT FINANCE STUDIES

DRAFT GREEN PAPER: CHAPTER 9

Note by the Secretaries

Attached is the draft of Chapter 9 (under the latest numbering) dealing with sales, fees and charges and the budgetary framework. Drafting comments should be sent to Ms J Rutter, Department of the Environment. The text will be discussed at the meeting on Thursday 19 December.

Signed J E ROBERTS
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Cabinet Office

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CHAPTER 9: OTHER FINANCIAL MEASURES

9.1 The taxation and grant reforms proposed in Chapters 2-4 of this Green Paper represent the core of the Government's proposals to improve the financial accountability of local authorities to their electors. The main theme in those chapters has been that, for local accountability to work, electors must be able to see how the price they pay relates to the services they get. This chapter considers two important ancillary issues that are closely related to that theme: the fees and charges levied by local authorities for certain services; and the framework governing the presentation and implementation of local authorities' annual budgets.

Sales, fees and charges

9.2 Chapter 3 described the proposal to introduce a community charge, paid by all adult residents, as a move toward the principle of relating the amount paid in local taxes to the benefit derived from local services, most of which are now provided for people rather than for property. The levying of a charge for a local authority service is of course an even more direct way of ensuring that local people can see what they are getting for what they are paying. Charging has benefits in terms of efficiency as well as accountability. Where consumers have a choice whether to use a service or not, those who provide the service can accurately judge the real level of demand. Realistic charging policies help to improve the efficient use of resources.

9.3 Extensive use is already made of charging for local services. In 1984/85 income to local authorities' general revenue accounts from sales, fees and charges amounted in England to some £2,500 million - equivalent to 60% of the yield of domestic rates. Income to the main local authority trading accounts, for housing and public transport, amounted to £1m and 1% respectively.

9.4 There are reckoned to be more than 600 individual local authority services for which charges are presently made. Some of those charges are far more important as a source of local income than others. And, as figure 1 shows, they tend to be concentrated on particular services

**Figure 1: Income from sales, fees and charges by main services
(England 1984/85)**

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9.5 The provision of public services cannot of course be governed only by market pricing considerations. Some services - like the police - have no individual consumers. They are provided for the community at large, and are appropriately paid for by the community as a whole. Other services are provided for the benefit of those who cannot afford the full cost of a service and must be subsidised if real needs are to be met. Many of the personal social services come into this category. Nevertheless, even in some of the more difficult areas, charges can be, and are, set. Even where the full cost of a service cannot be met by many beneficiaries without additional help, effective charging policies help to make more explicit the extent of the subsidy that is provided by the authority. That in turn can help in focussing attention on options for more cost effective forms of provision.

9.6 The Government's most important contribution to the development of local charging policies is to establish a clear financial climate within which local authorities can properly judge the correct balance between communal and specific user charges. Before 1981 the resources element of the Rate Support Grant positively encouraged local authorities to increase rates and reduce income from charges by giving authorities an increasing share of grant as rate poundages increased. This feature of the resources element was carried over for many authorities into the early years of the block grant arrangements. However, as the pressures to reduce total expenditure were increased as described in paragraphs ■ to ■ of Chapter 1, the advantages of reducing net expenditure by increasing income from fees became more evident. There is some evidence that income from sales, fees and charges has now started to grow in real terms.

9.7 The gradual move to the new financial arrangements described in Chapters 2-4 will reinforce this trend. It will lead to a clearer understanding of the marginal cost to local taxpayers of extra spending funded from the rates or the community charge. Each extra £1 spent will cost local taxpayers £1 more, and each £1 saved will cut the local tax bill by the same amount. The benefits of paying for service improvements by increased charges will be more apparent, since that will clearly put the extra cost on to those who use the services, rather than the generality of local taxpayers.

9.8 A marked feature of current local charging practice is the differences between local authorities in the proportion of their expenditure met from fees and charges. There will inevitably be variations in local circumstances that will affect the scope for charging - for example city centre authorities can obviously raise more from car parking. But even after taking account of this the extent of the range still seems surprisingly wide, as Figure ■ shows.

Figure ■: ■

Improving charging practice

9.9 Because of the real differences in the circumstances of authorities, any overall re-adjustment in the balance between funding services from general revenues or from specific user charges will depend ultimately on the day by day decisions of individual local authorities. It would not be practicable for central Government to attempt to lay down a particular pattern of charges - nor would it be compatible with the emphasis on local accountability which lies at the root of the proposals in this Green Paper. The Government can however affect the environment within which individual local authority decisions are taken.

9.10 The Government has already taken steps to increase the scope for local authority charging. The new fees introduced for planning and building regulation control in the Local Government Planning and Land Act 1980 have been particularly important in generating additional revenue - £11m and £11m respectively in 1984/85. Local education authorities have also been given greater freedom to charge for school transport.

9.11 The Government will continue to look for opportunities for widening the field with which local authorities can make charges. This will be done on a service by service basis. In addition to this search for new opportunities for charging, the Government will re-examine the case for relaxing central control of existing charges. There are over 100 local authority charges which are set directly or indirectly by central Government through regulations or national agreements. Central controls on charges are inefficient. They do not allow for differences between authorities in the cost of providing a service or for local market circumstances. Many of these centrally determined charges relate to local authorities' licensing functions which the Government has undertaken to reconsider in the White Paper "Lifting the Burden" (Cmnd 11), with a view to reducing unnecessary bureaucratic burdens on business. A Ministerial group has therefore been established to review central determination of charges.

9.12 The review will have two main stages. First, the need for any continuing regulation will be considered. Second, where it is decided that continuing regulation is justified, the case for retaining central controls or national agreements over pricing policy will be reviewed. In the first stage the presumption will be that licensing functions should be abolished unless there is a good case for their retention. In the second stage the presumption will be that local authorities should have discretion to make charges which are reasonable in relation to their costs in performing the function unless there are powerful arguments in favour of national standards.

9.13 The wide variation in the proportion of local authorities' expenditure met from charging supports the conclusion reached in many studies of local charging practices that local authorities have widely different levels of performance in relation to charging strategies or procedures for determining charging levels. Local government is itself trying hard, particularly through its professional institutions, to increase knowledge of the best practices in charging. It has been argued, however, that the efforts of the professional organisations might be more successful if they were backed by a requirement for local authorities

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to have regard to a statutory code of conduct in reviewing and determining user charges. The Government will consider the arguments for and against such a code as part of the Ministerial review announced above.

The budgetary framework

9.14 The proposals for reforming the taxation and grant systems will go a long way towards helping local taxpayers understand the relationship between what they pay and what they get. They will remove the distorting effects of the present grant and non-domestic rating arrangements on the relationship between expenditure and taxes at the margin and they will shift the currency of local domestic taxation from rate poundages, varying in their effect on rate bills according to the rateable value of property, towards a flat-rate £ amount levied on all resident adults of an authority.

9.15 However, the relationship between marginal changes in an authority's expenditure and the level of its tax is also affected by the way in which the authority organises its own finances. For example, an authority can reduce the effect of an increase in expenditure on tax levels by drawing on its reserves. Conversely, if it wishes to raise revenue to replenish its reserves, it will need to increase tax levels more than is necessary simply to finance an increase in expenditure on goods and services. Other internal financing arrangements can have similar effects.

9.16 In recent years, there has been considerable distortion in the relationship between changes in authorities' expenditure and rate levels at the margin. This has been due in part to financing adjustments which authorities have considered necessary to cope with the instability and uncertainty of the present grant system described in paragraphs 4.16 to 4.18 above, and to minimise grant losses under the system of penalties which operated from 1981/82 to 1985/86. The proposals for a new grant system which is stable and which involves grant allocations to authorities which are fixed at the start of the year should significantly reduce the need for such financing adjustments, although the Government recognises that local authorities will need to retain some flexibility in deploying their resources in the interests of prudent financial management.

9.17 However, the experience of the last two or three years has indicated that, in a few cases, there may be a more serious cause of distortion in the relationship between marginal increases in expenditure and rates. This arises where authorities prepare budgets which conceal or distort their true financial position in order to avoid difficult decisions about expenditure priorities or higher rate increases. This can involve levying a rate which is inadequate to meet planned expenditure, or specifying a planned level of expenditure which is unrealistically low which in turn means that the associated rate is also too low. Such devices may not lead to an immediate crisis in the authority's finances, because various stop-gap measures may be adopted to keep the authority's books balanced in the short term. They may be storing up serious long-term problems. They mislead local electors about the true costs of the services provided for them. This is an undesirable development which is not in the interest of responsible local government, hard-pressed local taxpayers or healthy local democracy.

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9.18 The District Auditor has, of course, an important part of play in ensuring financial propriety. But the main focus of his powers is the authority's audited accounts, after the end of the financial year. He can act once financial impropriety can be clearly established. But his ability to intervene to forestall improper or imprudent financial actions before or during the financial year is very limited.

9.19 One way of tackling this problem might be to set up a process whereby authorities' budgets were subject to some sort of checking or scrutiny by the auditor before they were approved by the authority to ensure that they were soundly based. But it would not be practical or necessary to submit all authorities to such a procedure. The problem of unbalanced budgets is not widespread, and a measure such as this would be understandably resented by local government. The Government would therefore much prefer a "self-policing" solution which drew upon the professional probity of local government financial management to ensure that sound budgetary practice is maintained in all authorities, and that, where departures from such practice occur, they are drawn to the attention of the authority and of its electors.

9.20 This could be achieved by establishing a specific statutory role for the treasurer or chief finance officer in relation to the legality and propriety of the expenditure by his local authority. This would bear in particular on the preparation of the budget and rate demand (or community charge demand, as it would be under the new arrangements) and the monitoring of expenditure and income during the financial year. A possible approach to this might be to establish a statutorily recognised role for the chief financial officer in the drawing up and execution of budgetary decisions. It would be possible for example to provide that:

- no rating resolution of the council would be valid without a certificate from the treasurer that the authority's proposed tax demand for the coming year was adequate to meet its estimated expenditure;
- the treasurer would have a legal duty to satisfy himself, in deciding whether to make such certification, that the authority's estimated expenditure for the year represented a fair and reasonable statement of the council's expenditure policies;
- the treasurer would have a legal duty to make a formal public report to the full Council and to the District Auditor if he considered at any time that a proposed item of expenditure or financing mechanism were either illegal or improper;
- the treasurer would also be obliged to make a formal report to the full Council if on the basis of his professional judgment he considered at any time during the year that the authority's resources were likely to be inadequate to finance its expenditure, either on the basis of existing expenditure plans or proposed new commitments.

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9.21 If the treasurer felt unable to certify the Council's proposed local tax demand, then it would not be payable. If the Council were to persist in incurring expenditure which they had been warned was unlawful or improper, councillors would weaken their position in any action which might subsequently be taken against them by the Auditor or in the Courts. And any warning that resources were likely to be inadequate to meet expenditure, together with the Council's response to it, would be on the record when the authority's accounts came to be audited at the end of the financial year.

9.22 In practice, the Government envisages that treasurers would rarely have to resort to these powers, or to issue formal reports. An informal warning by the treasurer to his council that, if they were to undertake a particular course of action, he would be obliged to invoke these powers should normally be sufficient to cause them to reconsider the proposal. If a treasurer were obliged to take action, this could of course cause difficulties for his relationship with the majority group of councillors. Nevertheless the Government considers that the case for an additional statutory safeguard against financial misconduct by a small number of authorities is strong. The treasurer is best placed to provide that safeguard: and the ratepayers would expect him to proceed in the way suggested. The Accounting Officer system in Government Departments provides analogous arrangement which works well.

9.23 The Government considers that a duty along these lines which leaves the responsibility with the officers of local authorities to draw the risk of financial impropriety formally to the notice of their Councils, so that local electors are aware of potential problems would do much to ensure that authorities were not tempted to budget or tax imprudently, so that the relationship between their spending and taxation decisions was kept as clear and direct as possible. In this way, the accountability of authorities to their electors would be further enhanced.