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THE FINANCE OF LOCAL GOVERNMENT IN GREAT BRITAIN

Local Government Finance in a Period of Retrenchment

1. Introduction

For almost a decade now, local government expenditure in Great Britain has been a matter of great concern to central government. This has been the decade in which the realities of national economix decline have come to be more fully appreciated, and successive governments have struggled to find ways of tacking inflation, unemployment and adverse balance of payments simultaneously. And throughout this period there has been a preoccupation with the size of public expenditure and particularly with finding ways to reduce it.

In Britain, public expenditure is widely defined to include the direct expenditures of central government, government lending to the nationalised industries and the expenditure of local authorities. Each year central government prepares its plans for public expenditure, which set out what levels are expected to be spent on each different service. And with almost relentless commitment, it has sought to ensure that its plans are realised in practice. But it has continually failed, and a succession of measures have been taken to try and bring local authority expenditure into line with the plans. All of which raises two critical questions. First, Why is the central government so concerned about local government expenditure? and second, What are the implications for local authorities and their independence of central government pressures on expenditure? To answer these questions,

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it is necessary to consider in more detail the ways in which central and local government finances interrelate, and the means by which the pressures have been pursued.

2. Exhortation and changes in grant levels

The pressure on local authority expenditure from central government is not new. For many years governments have taken every opportunity to press the case for local authorities to respond to the needs of the public sector economy as a whole. Repeated circulars and ministerial statements have relentlessly attempted to convey the message and there has been extensive dialogue between central and local politicians and officers particularly since the establishment in 1975 of special machinary of consultation, known as "the Consultative Council". More importantly there has been the opportunity created by the fact that central government makes a large grant contribution to local government, and each year the calculation and distribution of the grants has reflected strongly central goverment's objectives for the forthcoming year in local authority expenditure.

Local authorities in Britain receive two different kinds of grant, but both have been used in this way, and indeed shifts in the level of grant both to local government as a whole and to individual authorities represents the most powerful pressure from central government. On the one hand there are "specific grants" which are paid in support of expenditure on particular services, while on the other, there is a "general" grant, an allocation of which is made to each authority to be spent as is locally felt fit.

Each year in fact, central government calculates how much money it thinks ought to be spent by local government as a whole in the coming financial year, taking account of Treasury economic assessments and political priorities, likely pay and price changes which would affect costs of provision, of likely income to local authorities from charges for services and so on. Then an announcement is made (usually in December) as to the proportion of that expenditure which central government is prepared to finance in the forthcoming financial year. In the period 1968-1976 this proportion rose steadily, from 54 percent to 66 percent. However subsequently it has been reduced steadily, to stand at 52 percent in 1984/85. Clearly, by reducing the percentage grant contribution, central government has effectively been able to squeeze local government revenue, forcing authorities who receive a contribution either to make economies or to bear the burden through higher local rate bills.

Moreover it is worth noting that the proportion of total grants which specific grants represent has risen steadily in recent years, from about 13 percent in 1977 to almost 20 percent in 1983, a change which implies a more effective means of influencing local standards of service in line with central policies. It goes without saying that a number of central departments, most notably the Department of Education and Science, have argued forcefully for this type of grant, in preference to the general grant where no such central direction is implied.

The general grant, or "rate support grant" as it is known, certainly provides greater potential for the exercise of local discretion but with two important qualifications. First, the major proportion of local government expenditure is committed being governed either by statutes, for instance the requirement to provide education for all children up to the age of 16 years, or by past decisions which are difficult to revoke, for example, decisions to provide sports centres, and other public amenities which incur annual expenditure on upkeep. Thus the scope for discretion is any case likely to be only marginal, and unless financed locally by exceptionally high rate levies, is dependent on the grant allocation being much in excess of what is required to meet those commitments. In the recent years of retrenchment this certainly has never been the case.

Second, and not unrelated, is the point that the means by which the ratesupport grant allocations are calculated involves detailed assessments being made by central government of the expenditure needs of each service, and it is therefore unlikely indeed that substantial provision would be made for levels of service above those implied in central policy. The point to note therefore is that the general grant is not so general as it may seem. Indeed it tends to be viewed by many government departments as an aggregation of a number of grants for particular local services and even to particular areas of those services. Moreover this is not merely an attitude held in central government circles but is one which many in local government surprisingly often seem to share, and one which implies further power by central government over local authority expenditure.

3. Grant as a vehicle of central control

Although the task of assessing the grant shares of each authority purports to be objective, and attempts to compensate both for differences in local taxable capacities and needs for service provision across the country, it is in practice very much part of the central government control over local authority expenditure. Quite simply this is because although a detailed analysis is involved of the expenditure needs in each separate service, this is used merely to determine relative shares of grant between the local authorities. The actual amount available is felt by many to bear little relation to total "need", but simply conforms with what the governments public expenditure plans have indicated as affordable. At a time when central government has been seeking reductions in local authority expenditure, the formula and machinery for distributing grant has been an obvious instrument to turn to.

And so in recent years, a succession of steps in this direction have been taken. At first, the objective was to encourage each authority to spend at the level assessed by central government to be appropriate relative to other authorities. And a system of reduced grant support for expenditure significantly above this level was introduced in 1980.

But when it became clear that this would not be sufficient to ensure that all authorities reduced their expenditure to the desired level a further measure was adopted and added on to the grant system. This took the form of a set of expenditure "targets" for each authority, and more stringent grant-loss penalties for expenditure above them. Those authorities spending above their target would thus have to finance both the grant-loss and the extra expenditure from local rates implying large increases in rate levies, which the government hoped would be a sufficient disincentive. The introduction of "targets" was said to be temporary only, and necessary because many councils who were spending in excess of the government's assessed levels could not achieve the spending in excess of the governments assessed achieve the desired reductions fast enough without drastic impacts on services. The idea was that the targets would pressure those "over-spending" authorities to reduce their budgets by a "realistic" margin each year until the "overspend" had been eliminated. Unfortunately the actual method employed for calculating the targets and the penalty rules was ill-conceived, and meant that in practice many low-spending councilea found themselves facing grant losses without apparent justification. Central government, it seemed, was unable to find a method which would penalise only those authorities which it wished to. It was a case of a system generally applied, being wholly inappropriate to the situation which as the government acknowledged, amounted only to a "... handful of recalcitrant authorities ...". But Parliament had refused to sanction a grant system for England and Wales that entitled central government selectively to penalise authorities, unlike the situation in Scotland where the Secretary of State gained powers to withdraw grant from any authority whose expenditure was deemed "... excessive and unreasonable ..." Miscellaneous Provisions (Scotland Act, 1982).

Harsh though such measures might seem, the critical question is again whether they would produce the expenditure reductions which the government sough. And here the evidence is mixed. The fact that about two thirds of the local authorities were spending within 2 percent of the targets after two years of the new system, might indicate considerable influence being exerted. On the other hand, many of these councils were traditionally "low-spenders" and meeting targets involved little hardship, indeed in some cases even allowed for an increase in provision.

Nevertheless, such actions to effect reductions in local authority budgets were not taken in isolation. In parallel, a tight control was imposed on capital expenditure, on such items as housing, school and road building programmes, by limiting the amount that each authority couls spend each year. Moreover in 1982, the power of local authorities to levy supplementary rates once; the rate levy had been announced at the beginning of the financial year, was abolished to prevent any opportunity for increases in budgets; this being followed by the announcement of the intention to abolish the six metropolitan counties and the Greater London Council, all of whom featured prominently among the shrinking list of authorities continuing significantly to "overspend" their targets. And following the re-election of the Government in 1983 on an enhanced majority, a still more controversial step was taken in proposing legislation for a scheme to limit the level of rates which individual council could levy.

Ironically, the need for such action itself would be owed in part to the grant controls themselves. For a consequence of large grant-loss penalties to "over-spending" councils, was that a number received a diminished share of grant while a few received none at all, and were left dependent for almost all their revenue on the rates. In such circumstances, they would be able to ignore central dictates and to assert their new-found independence through radical localism, under the banner of local accountability. However what was now being proposed would halt this abruptly. For the rate limitation legislation allows central government to select local authorities which it considers to be "overspenders" and set a maximum legal rate for them, which takes account of grant entitlements, any financial reserves and other sources of income. The legislation has earned notoriety in Great Britain, partly because it is considered an unnecessarily cumbersome means to deal with just a handful of authorities, but mainly because it represents a major constitutional issue. For it means a fundamental shift from a central control over grant to one over grant and rates, and for this reason implies the erosion of the traditional and most cherished symbol of local government's autonomy, namely its freedom to decide its own level of expenditure and levy a rate accordingly.

4. Central control versus local financial autonomy

The recent experience in Britain has undoubtedly been of a significant shift in the balance of central-local government relationships in favour of the centre. Particularly with regard to finance, central government has increasingly been able to dictate the pattern of local decision. But the justification for, as well as the merits of such central control is questionable. In particular the view that the centre requires control of local government expenditure in pursuit of its macro-economic responsibilities is questionable, and confuses economic arguments with others that others that are essentially ideological. Although the obstensible purpose of seeking central control is economic, the actions represent an ideological preference for the monetarist economic approach. This places its emphasis on the control of inflation. Public expenditure,by increasing demand, is regarded as inflationary and resources devoted to the public sector are said to "crowd out" the private sector. Therefore, in order to hold down inflation and release capacity for the private sector the money supply must be controlled by curbing public sector spending.Since local government is responsible for a substantial part of public sector spending it is a major target. This argument has been challenged on several counts. Opponents argue that monetarist approaches are, in part at least, the cause of recession and that public expenditure cuts contribute to unemployment, the decline of consumption and a cut in the social wage. If local spending is financed from local taxes rather than borrowing it has no effect on aggregate demand; public goods simply replace private goods unless savings are reduced. In any case, an increase in local spending, even if not entirely offset by higher local taxes,would have only a very small impact on total demand.Furthermore, public spending could only "crowd out" the private sector in conditions of full employment, not in a situation where there is underused capacity in the economy. The proportion of the GNP devoted to public expenditure is lower than in most other developed economies and local spending accounts for only about 13 percent of GNP. While local spending has reduced, (by nearly 5 percent in the three years 1978 to 1981) that of central government, which accounts for 33 percent of GNP, has actually increased by over 4 percent, even after excluding social security programmes.

The impact of an individual local authority's expenditure on demand and inflation is clearly insignificant but it seems that the political arguments far outweigh such evidence. Here it is fair to comment that under the Conservative government the grant has been redistributed in a way which when compared with previous years, has benefited the County Councils, the majority of which are Conservative controlled.Moreover the introduction of spending targets for individual local authorities was designed to attack high spending councils, most of which, predictably, are Labour controlled. The demise of the supplementary rate has also afflicted Labour authorities which have, in the past, raised such rates to improve local services or avoid making cuts. Government policy inevitably represents a recognition of the political geography of local finance, and the proposal to abolish the metropolitan counties and the Greater London Council provides perhaps the strongest indication of all of this point. Such aproposal, and the new legislation to limit the increase in rates of certain high-spending councils illustrates,above all,the willingness of the government to put to the test the superiority of a national electoral mandate over a local one. And in this respect the specific matter of finance over into the wider, and evidently more fundamental, debate about the very nature of local government in this country and of its future.

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