



National Audit Office

Local government report

by the Comptroller and Auditor General

Local government

The impact of funding reductions on local authorities

NOVEMBER 2014

Key facts

37%

estimated real-terms
reduction in government
funding to local authorities
2010-11 to 2015-16

25%

estimated real-terms
reduction in local
authorities' income
2010-11 to 2015-16, once
council tax is included

40%

largest local authority
real-terms budgeted
funding reduction,
2010-11 to 2015-16

- 80%** single tier and county councils that have added to their total reserves between 2010-11 and 2013-14
- 46%** budgeted real-terms reduction in spending on planning and development services, 2010-11 to 2014-15
- 7%** budgeted real-terms increase in spending on children's social care services, 2010-11 to 2014-15
- 40%** total savings between 2013-14 and 2014-15 made through reducing adult social care services
- 16.6%** reduction in full-time equivalent posts in local authorities, excluding the total school workforce, between 2010 and 2013
- 56%** metropolitan district and unitary councils that local auditors are concerned will not meet medium-term savings targets

Summary

1 Since 2010, the government has reduced its funding for local government in England as part of its plan to reduce the deficit. The government has also changed the nature of its funding for local authorities, to provide incentives for local growth. This has created financial opportunities for local authorities, but also increased financial risks and uncertainty.

2 Within this challenging context, local authorities must deliver a range of services. Local authorities have a statutory duty to provide certain services. These range from adult social care to collecting waste. They also provide discretionary services according to local priorities.

3 Ensuring that local authorities remain financially sustainable, in that they deliver their statutory services to a sufficient standard, is becoming more difficult. There is a robust financial framework in place that effectively prevents local authorities becoming insolvent. However, the impact on services caused by funding reductions is more difficult to discern. A lack of services affects service users and can be poor value for money. This increases costs in the long run or pushes costs on to other service providers.

4 The Department for Communities and Local Government (the Department) has overall responsibility in central government for local authorities' funding. This includes distributing the majority of funding voted by Parliament to support local authorities in delivering their core services.

Our report

5 This is the first local government report published under the Comptroller and Auditor General's new powers under the Local Audit and Accountability Act 2014. These allow the Comptroller and Auditor General to examine the economy, efficiency and effectiveness with which local authorities use their resources in discharging their functions. The purpose is to provide evaluation, commentary and advice of a general nature to local authorities.

6 This report aims to provide local authorities with detailed comparative analysis of changes in income, spending and financial and service sustainability across the sector. Our objective is to contribute to their ongoing financial planning by:

- allowing local authorities to compare their performance on key financial issues against trends in the wider sector; and
- disseminating information across the sector about the strategies and actions different local authorities have taken to tackle their financial challenges.

7 The report is comparative, allowing local authorities to assess their performance and experiences against similar types of local authorities or those that have experienced similar levels of funding reduction.

8 This report has 3 parts:

- **Part One** sets out the changes to local government income and spending since 2010-11.
- **Part Two** assesses the impact funding reductions have had on local authority service spending and provision since 2010-11.
- **Part Three** examines the financial sustainability of local authorities based mainly on a survey of local auditors.

9 This report complements our value for money report on central government's approach to local authority funding, *Financial sustainability of local authorities 2014*.¹

10 The report draws on detailed analysis of local authority data on spending and activities, along with information from case study local authorities. A separate methodology is available for this report (www.nao.org.uk/report/impacts-funding-reductions-local-authorities/).

Key findings

Changes in income and expenditure

11 **Government funding for local authorities has fallen by 28% in real terms over the 2010 spending review period. This reduction will reach 37% by 2015-16 based on illustrative data from the Department.** Metropolitan districts will face the largest fall in government funding, with a 41% reduction by 2015-16. County council funding, in contrast, will have fallen by 33%. There have been differences in the timing of the reductions, with district councils' reductions having an earlier impact than in other types of authority (paragraphs 1.2 to 1.6 and Figure 2).

12 **The 37% fall in government funding by 2015-16 is equal to a 25% fall in revenue spending power.** The Department uses 'revenue spending power', a combination of government funding and council tax income, to assess the scale of the financial challenge facing local authorities. Including council tax income gives a fuller view of the implications of funding reductions on authorities' spending capacity than looking at changes in government funding alone (paragraphs 1.7 and 1.8).

13 **Reductions in spending power vary widely, with authorities that depend more on government grants seeing bigger falls in spending power.** The significance of government funding to individual local authorities' spending power varies substantially (**Figure 1**). Reductions in government funding have a proportionately greater impact on the revenue spending power of authorities more dependent on government funding (paragraph 1.9 and Figure 3).

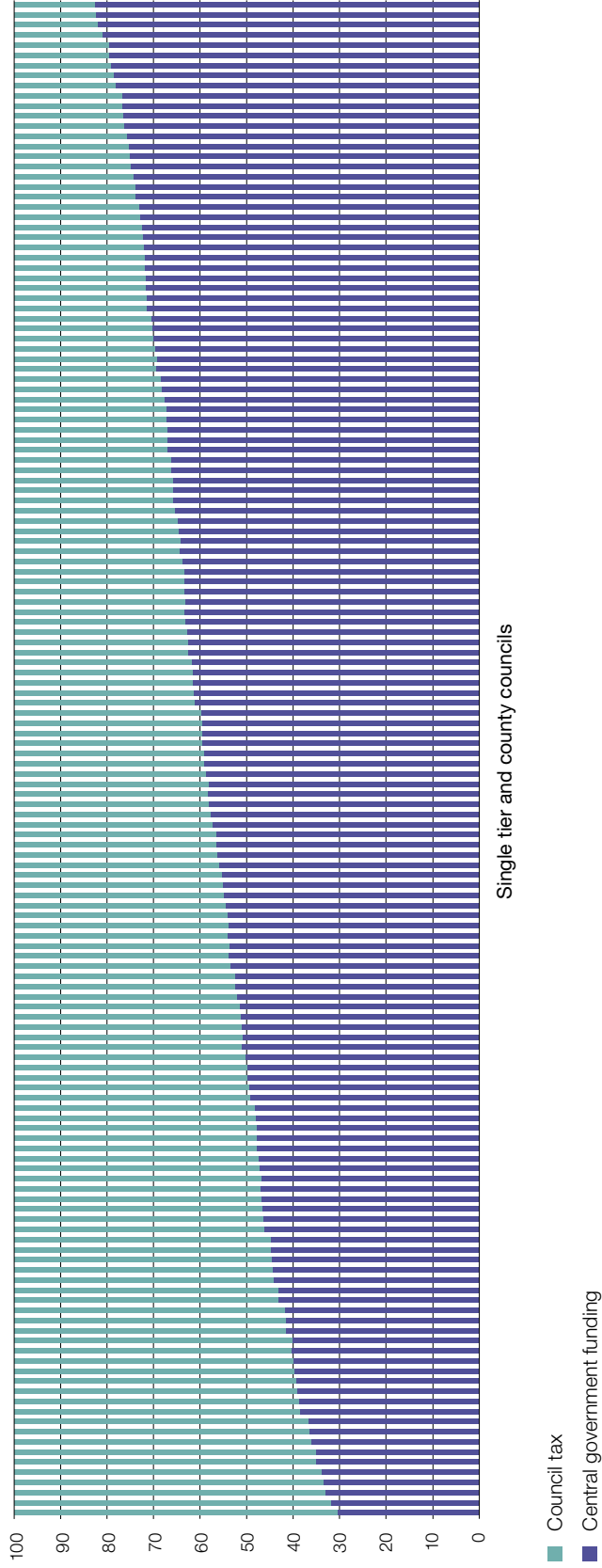
¹ Comptroller and Auditor General, *Financial sustainability of local authorities 2014*, Session 2014-15, HC 783, National Audit Office, November 2014. Available at: www.nao.org.uk/report/financial-sustainability-of-local-authorities/

Figure 1

Government funding and council tax as a share of 'revenue spending power'

Authorities that are more dependent on government grants will be affected relatively more by reductions in government funding

Share of revenue spending power by source (%) (average 2010-11 to 2014-15)



Note

1 Data are for single tier and county councils only.

Source: National Audit Office analysis of Department of Local Government and Communities data

14 Locally-raised income has fallen and has not offset reductions in government funding. The council tax freeze grant, along with the requirement for a local referendum to increase council tax above centrally prescribed levels, has suppressed increases in council tax. Real-terms council tax income between 2010-11 and 2013-14 fell by 3.1% for single tier and county councils and 2.3% for district councils on average. Similarly, authorities have not raised extra income from fees and charges. From 2010-11 to 2013-14, income from fees and charges fell by 0.4% in real terms for single tier and county councils, and 0.1% for district councils (paragraphs 1.13 to 1.16).

15 Local authorities have increased their reserves significantly. Between 2010-11 and 2013-14, 80% of single tier and county councils, and 78% of district councils, increased their reserves (earmarked and unallocated reserves combined). Reserves held by single tier and county councils have increased from the equivalent of 25% of net revenue expenditure in 2010-11 to 33% in 2013-14. District councils' reserves increased from 62% to 76% of net revenue expenditure. Our case study authorities told us they increased reserves because of uncertainty about future income (paragraphs 1.20 to 1.26 and Figure 4).

16 Local authorities have managed reductions in government funding mainly by reducing spending. Staffing costs have fallen more sharply than running costs. Local authorities reduced full-time equivalent posts, excluding the total school workforce, by 16.6% between 2010 and 2013. Activities that reduced local authorities' running costs, such as shared services, have been greatest in authorities with the largest reductions in government funding (paragraphs 1.27 to 1.36, Figures 5 to 8).

Impacts of funding reductions on services

17 Local authorities have tried to protect statutory services. Among single tier and county councils, spending on adult and children's social care has been relatively protected. Environmental and regulatory services, which include statutory duties to collect and dispose of waste, have also seen lower spending reductions than other areas. Areas with a higher proportion of spending on discretionary activities, such as planning and development, and housing, have seen much larger reductions (paragraphs 2.2 to 2.6 and Figures 9 and 10).

18 There have been significant changes in the focus of local authorities' spending reductions over the 2010 spending review period. Adult social care, for example, accounted for 40% of total savings between 2013-14 and 2014-15. This compared with only 15% from 2010-11 to 2011-12. Planning and development, in contrast, now contributes a far smaller component of savings. Unless spending in some service areas is to be run down completely, this pattern, where formerly protected service areas contribute more towards savings, is likely to continue (paragraphs 2.7 and 2.8, Figures 11 and 12).

19 Local authorities' spending decisions are influenced by the size of the fall in their spending power. Authorities facing larger reductions have protected adult social care, children's social care, and environmental and regulatory services less than those with smaller reductions. Aggregate figures show that local authorities have increased spending on children's social care by 7% between 2010-11 and 2014-15. However, among authorities with the greatest funding reductions, spending on this service fell by 4%. This indicates that, in some services, aggregate analysis of spending can be misleading and hide substantial differences between local authorities (paragraphs 2.9 to 2.11, Figure 13).

20 Local authorities have focused spending reductions on individual services within broader service areas. Within environmental and regulatory services, spending on community safety fell 47.1% in real terms, compared with a fall in spending of 11.7% in waste services. Within highways and transport, spending on traffic management fell by 43%. The fall in spending on street lighting was 4.1% in real terms. Analysis of spending changes at the aggregate service level means that significant changes in important sub-services risk being missed (paragraphs 2.12 and 2.13 and Figure 14).

21 There is little evidence of the extent to which local authorities have made savings through efficiencies rather than service reductions. Other than data on children's and adult social care, there are almost no data on local authority outputs and activities. Assessing how far savings have impacted on service users for most service areas, based on comparable national data, is not possible for the most part (paragraphs 2.14 and 2.15).

22 Evidence from adult social care shows that local authorities have made savings through both efficiencies and reductions in activity levels, but that savings from efficiencies may now be lessening. In the 2 years after 2010-11 there is evidence that local authorities made significant price-based savings from core elements of their adult social care services. In combination with a fall in service levels this produced large total savings. Price-based savings appear to have stopped in 2013-14, however (paragraphs 2.16 to 2.21, Figures 15 and 16).

Financial sustainability

23 Some local authorities are showing persistent signs of financial stress, particularly metropolitan districts. Local auditors reported that 16% of single tier and county councils had difficulties in delivering their 2013-14 budgets. Among metropolitan districts, the figure was 22%, with 19% having difficulties in 2012-13 and 2013-14. An increasing number of authorities also needed unplanned in-year actions to deliver their budgets. In 2013-14, 33% of metropolitan districts needed unplanned reductions in service spend to balance their budgets (paragraphs 3.4 to 3.14, Figures 18 to 20).

24 Local auditors' confidence that local authorities can make medium-term savings has fallen. Auditors are relatively confident about the future financial sustainability of district councils, but are increasingly pessimistic about single tier and county councils, particularly metropolitan districts and unitary authorities. Auditors have raised concerns about the capacity of 56% of both types of authority to deliver their medium-term financial strategies (paragraphs 3.15 to 3.21, Figures 21 and 22).

25 Auditors are concerned about 'funding gaps' within local authorities' medium-term plans, and the risks that could prevent authorities delivering savings through service redesign and transformation. Auditors are positive about authorities' financial management capabilities and take confidence from their record in delivering savings to date. Despite this, auditors are concerned that some authorities are unable to show how they will deliver savings required in 2015-16 and beyond. Furthermore, where they have identified methods to deliver savings over the medium term, these often involve substantial, but largely untested, restructuring and transformation of services (paragraph 3.22).

Overview

26 Overall, we found that local authorities have managed their finances successfully through a prolonged period of funding reductions. Authorities have used reductions in spending, rather than increases in locally raised income, as the main method of addressing falls in government funding. They have cut back on their staffing costs in particular. There has been an increase in levels of reserves as authorities have sought to guard against financial uncertainty and provide investment funding to support savings programmes.

27 Authorities have tried to protect spending on statutory services in areas such as adult and children's social care. But there is significant variation between authorities. Those with large funding reductions are less likely to have protected this spending. Within adult social care, savings have been made through efficiencies rather than service reductions alone. However, the large savings made through falls in unit costs in this area in the first 2 years of the 2010 spending review period have now ended. Aside from social care, there is no real evidence of the impact of spending reductions in different service areas on services and service users.

28 While local authorities have maintained financial resilience overall, some – particularly among metropolitan districts – are now showing persistent signs of financial stress, such as unplanned in-year reductions in service spend. Looking to the future, there is increased uncertainty about how local authorities can manage further possible falls in income. While local authorities are planning for continued savings, they are increasingly relying on untested service transformation programmes to achieve them. Local auditors have expressed concern about more than half of all metropolitan districts and unitary authorities, in terms of their capacity to deliver medium-term savings targets.