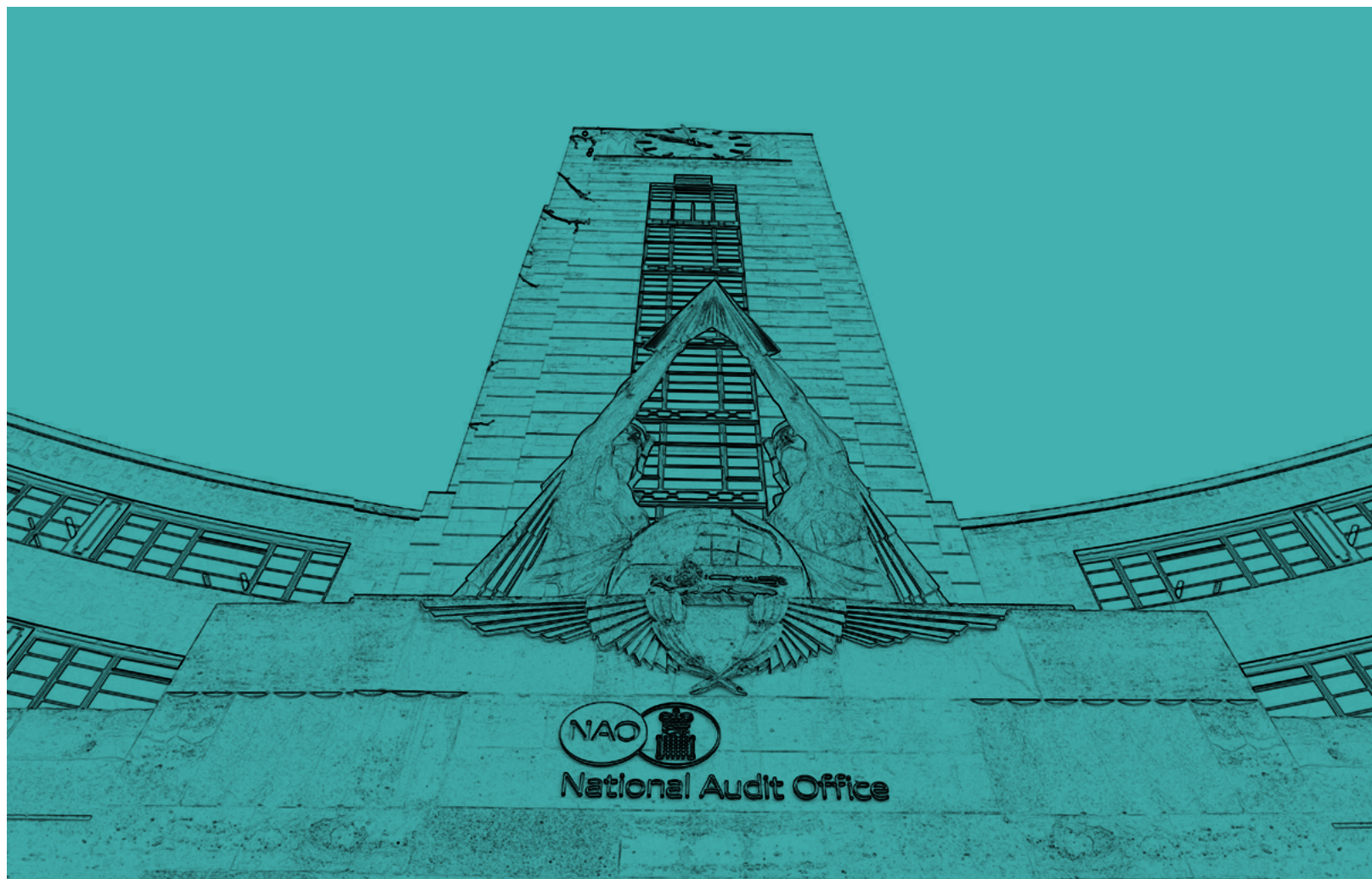


October 2016

Local government



If you would like to know more about the National Audit Office's work on local government, please contact:

Aileen Murphie

Value for Money Director,
DCLG and Local government
✉ aileen.murphie@nao.gsi.gov.uk
☎ 020 7798 7700

Colin Wilcox

Financial Audit Director,
DCLG Portfolio
✉ colin.wilcox@nao.gsi.gov.uk
☎ 0191 269 1859

If you are interested in the NAO's work and support for Parliament more widely, please contact:

✉ Parliament@nao.gsi.gov.uk
☎ 020 7798 7665

The National Audit Office scrutinises public spending for Parliament and is independent of government. The Comptroller and Auditor General (C&AG), Sir Amyas Morse KCB, is an Officer of the House of Commons and leads the NAO. The C&AG certifies the accounts of all government departments and many other public sector bodies. He has statutory authority to examine and report to Parliament on whether departments and the bodies they fund have used their resources efficiently, effectively, and with economy. Our studies evaluate the value for money of public spending, nationally and locally. Our recommendations and reports on good practice help government improve public services, and our work led to audited savings of £1.21 billion in 2015.

Design & Production by NAO External Relations
DP Ref: 11233-001

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Overview 2015-16

Local government

Executive summary

This Overview looks at the local government landscape and summarises both matters of likely interest to the Select Committee and the National Audit Office's (NAO's) work with local authorities. The NAO prepares statutory guidance on how local auditors should meet their responsibilities.

The NAO produces reports both for local government, and relevant to local government. Our work provides valuable insights for the sector to use in designing future delivery. The NAO has no role in the external audit of individual local authorities and we do not issue value-for-money opinions on individual local authorities. The content of the report has been shared with the Department for Communities and Local Government (the Department) to ensure that the evidence presented is factually accurate.

This report looks at the local government landscape and summarises both matters of likely interest to the Select Committee and the NAO's work with local authorities.

Part One sets out some facts about how local government is constituted and funded, together with its spending:

- Local government is comprised of several different types and layers of authorities.
- Local government is increasingly funded by revenue raised in the area where the service is delivered.
- Service spending by local authorities has fallen since 2010-11, with some service areas seeing significant reductions.

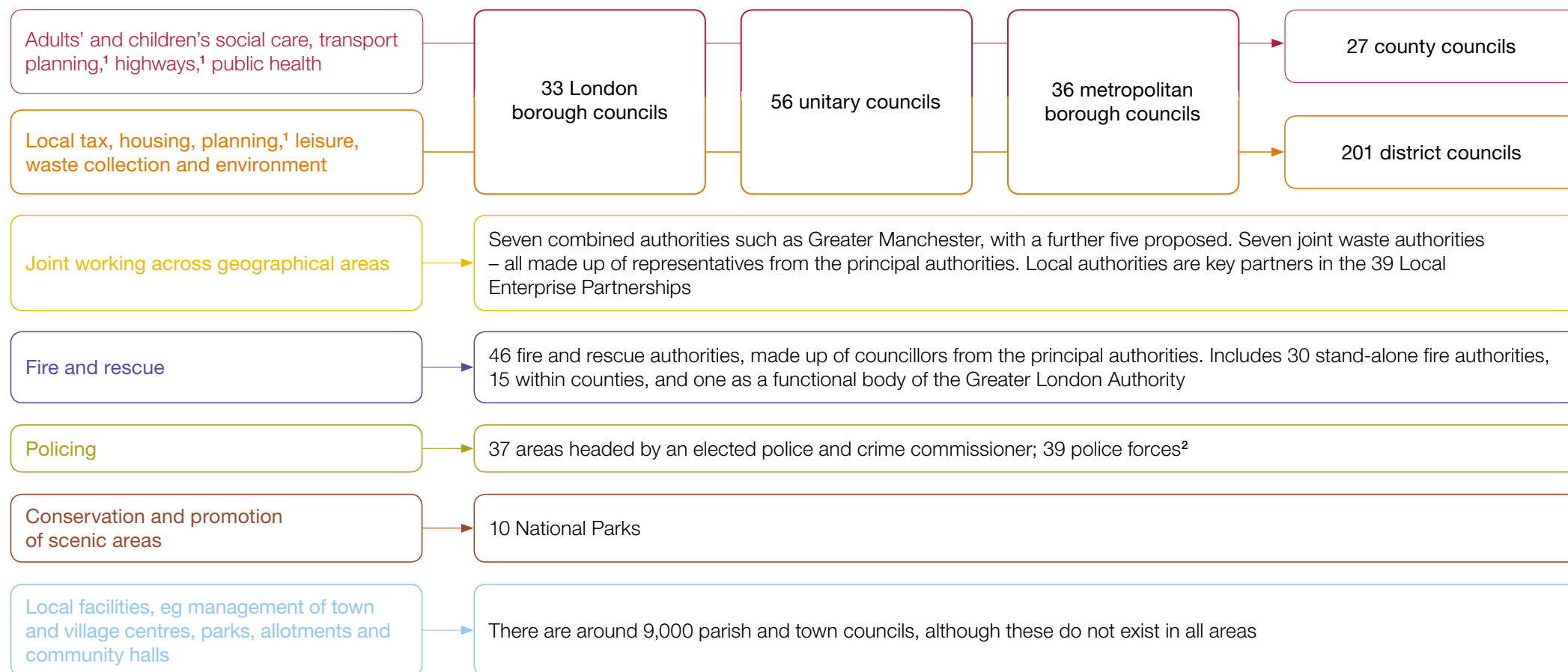
Part Two sets out our findings from our work on local government:

- The NAO prepares statutory guidance on how local auditors should meet their responsibilities. The NAO produces reports both for local government, and relevant to local government. Our work provides valuable insights for the sector to use in designing future delivery.
- The NAO has no role in the external audit of individual local authorities and we do not issue value-for-money opinions on individual local authorities.

Part Three looks ahead to the coming year:

- Local government is facing increasing devolution of funding, power and accountability and has the option to secure medium-term financial settlements. This is taking place against a backdrop of increased uncertainty for some areas of funding and responsibility, following the referendum to leave the European Union.
- The funding of local government is changing with the move toward 100% of business rates being retained by local government.

About local government and its responsibilities



¹ In London, the Greater London Authority also has responsibility in these areas.

² The number of police and crime commissioners differs from the number of police forces because the Metropolitan Police Service and City of London Police have different arrangements compared to other areas.

Local government funding

Controllable income – £58 billion in 2016-17

- **Government grant.** In 2016-17, local authorities budgeted to receive **£25 billion** from government to support the delivery of their statutory functions and duties. This is funding that in general they have a significant degree of control over.

We include locally retained business rates income in this sum. Business rates are generated locally and 50% has been retained locally since 2013-14. However, owing to the national framework in place for this funding, currently business rates income falls within the Department's accounts, and is therefore classified as central funding.

- **Council tax.** In 2016-17, local authorities have budgeted to generate **£22 billion** from council tax. 144 out of 152 eligible local authorities have taken up the social care precept, raising £382 million.
- **Sales, fees and charges.** In 2014-15, (the most recent year where data is available) local authorities generated **£11 billion** from this source.

Non-controllable income – £52 billion in 2016-17

Local authorities receive a significant amount of funding from government which is **passed directly through them to other organisations or individuals**. Local authorities have little if any control over this funding and it is traditionally discounted in analysis of local authority income.

In 2016-17, this included:

- **£30 billion** for front-line funding for schools from the Department for Education. This funding is ring-fenced and **local authorities transfer it directly to schools**.
- **£22 billion** for grants that local authorities pass directly to individuals, principally Housing Benefit (£21 billion). Again, **this is passed directly through the authority**.

Other income and funding

Local authorities can also **generate income through their investment activities** but these sums are relatively minor in terms of income for the sector as a whole.

Additionally, **local authorities may build up reserves** and use these to fund services or deliver local priorities such as capital projects. Local authorities had **£17 billion of revenue reserves** on 31 March 2015. (This includes both earmarked and unallocated reserves but excludes schools reserves and public health reserves).

Councils are required to set a balanced budget each year so must find ways of managing with less government funding while responding to demand pressures.

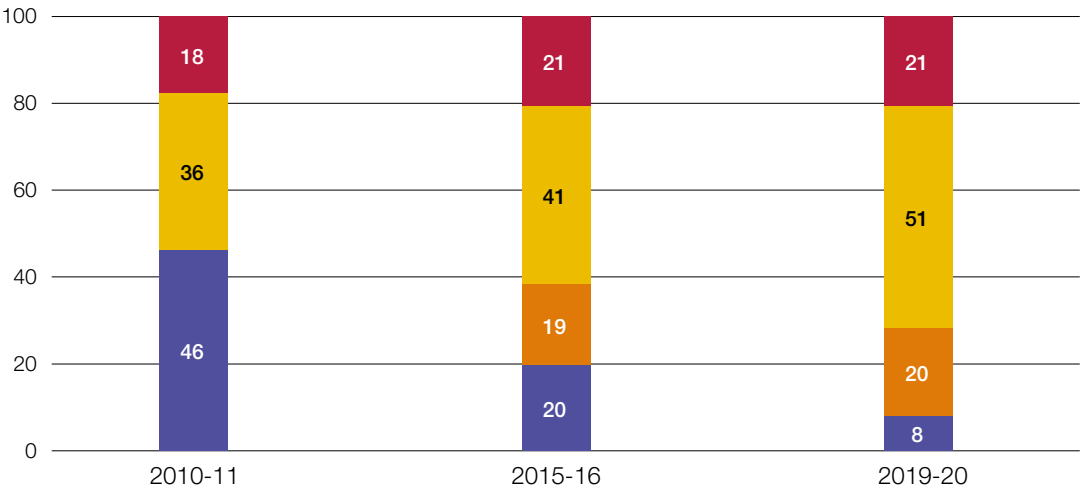
Local government funding *continued*

Patterns of change:

- Since 2010-11 the share of local authority revenue from local sources has increased.
- To a large extent this has been due to reductions in central funding rather than growth in council tax or sales, fees and charges income.
- However, the Department anticipates significant growth in council tax income from 2016-17 as authorities are now able to add additional precepts.
- **The Department plans for 100% retention of business rates by the end of this Parliament.** This is also likely to include relaxations in the current framework, such as allowing authorities to reduce the rate.
- 100% retention is a significant task that the Department will be working on throughout this Parliament. Primary enabling legislation is expected to be introduced in early 2017.

Figure 1
Change in the structure of local authority funding 2010-11 to 2019-20

Percentage of revenue income (excluding direct schools funding and grants outside aggregate external finance)



- Sales, fees and charges (estimate)
- Council tax
- Business rates (locally retained)
- Government grant (including nationally redistributed business rates)

Note
1 Figures do not sum due to rounding.

Source: National Audit Office analysis of local authority revenue expenditure and financing

Local government funding 2016-17 to 2019-20

The Department intends to introduce 100% local retention of business rates by the end of this Parliament. Plans for local authority revenue funding in the interim were set out in the **2016-17 local government finance settlement** which provided funding details up to 2019-20.

As part of the settlement the Department also changed arrangements in relation to council tax, **allowing authorities with adult social care responsibilities to add a 2% annual precept (on top of the standard 2% referendum limit)**, and district councils to increase their council tax by up to the greater of £5 and 2%, should they choose.

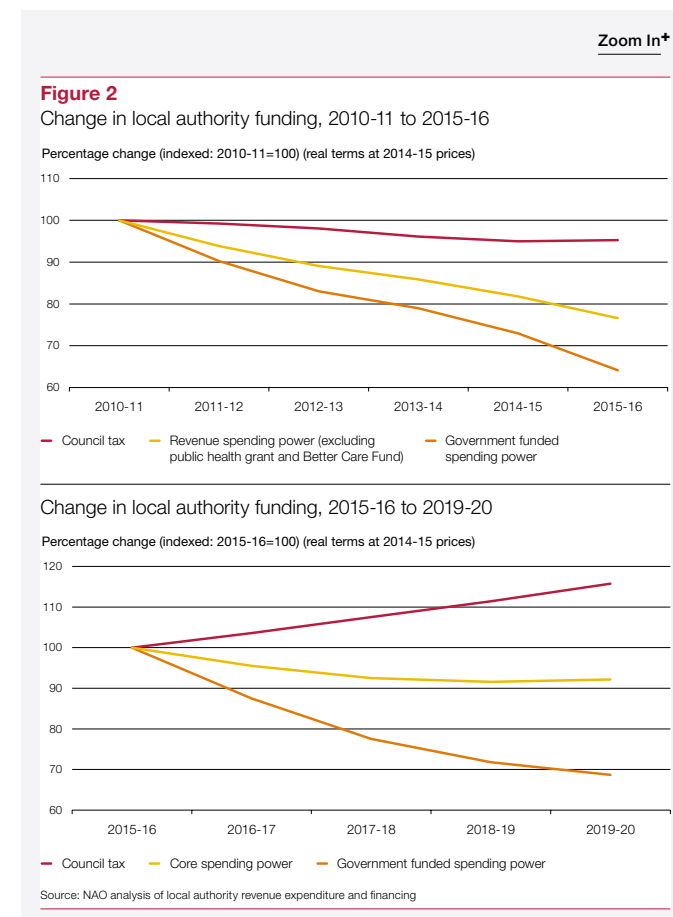
The settlement as a whole involves a 7.8% (2% per annum) real-terms cut in spending power (council tax plus government grants including business rates) from 2015-16 to 2019-20.

This is an easing in revenue income pressures experienced to date by authorities. Over the period 2010-11 to 2015-16 authorities had seen a real terms reduction in spending power of 23.4% or 4.7% per annum.

However, **the easing in spending power reductions is solely the result of anticipated increases in council tax income.**

The Department's figures from previous settlements show council tax income as largely flat declining by 0.9% per annum from 2010-11 to 2015-16. However, from 2015-16 onwards council tax income is expected to grow by 3.9% per annum.

In contrast, **the rate of decline in government grant is relatively stable falling by 7.2% per annum in real terms from 2010-11 to 2015-16, and then 7.8% per annum from 2015-16 to 2019-20.**



Local government service spending

Once funding passed directly to schools is stripped out, it is clear that **local authority expenditure is dominated by social care.**

For 2016-17, authorities have budgeted (excluding sales, fees and charges income) to spend:

- 32.6% (£14.4 billion) of their non-schools expenditure on adult social care; and
- 16.7% (£7.4 billion) on children's social care.

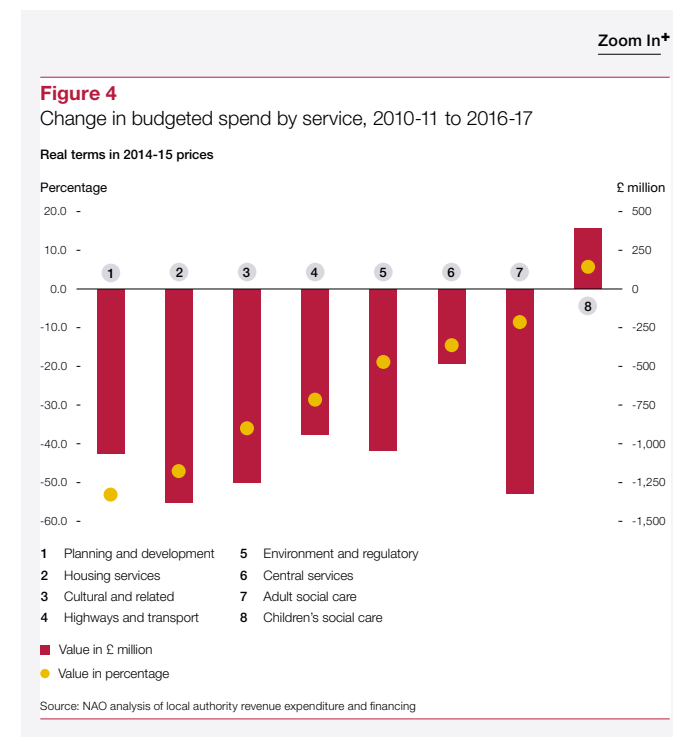
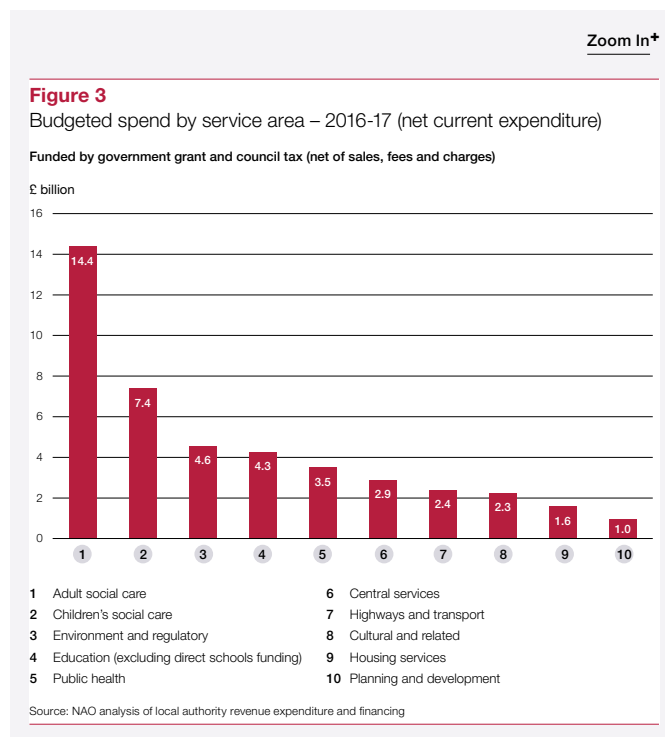
This is a combined total of 49.3% (£21.8 billion) of total non-schools service spend.

Local authorities have also sought to protect spending on social care. From 2010-11 to 2015-16 real-terms budgeted spend:

- increased by 5.7% for children's social care; and
- decreased by 8.6% for adult social care

Other service areas that do not contain as many statutory responsibilities have seen much larger real-terms planned reductions over the same period with falls of:

- 36.0% for cultural services;
- 47.1% for housing services (excluding housing revenue account spend); and
- 53.1% for planning and development.



The NAO's role in local authority audit

The NAO prepares a statutory [Code of Audit Practice](#) and guidance on how auditors of local government should meet their responsibilities. We are not the auditor of individual local authorities. Our functions are part of a new audit framework for local public bodies in England.

The Local Audit and Accountability Act 2014 (the 2014 Act) made the Comptroller and Auditor General (C&AG) responsible for preparing and issuing the Code of Audit Practice (the Code) and guidance which set out what auditors of local public bodies (which includes councils, fire and rescue authorities, local health bodies and police and crime commissioners) are required to do to meet their statutory responsibilities. The first Code and guidance took effect for the audits of the 2015-16 financial statements.

Under transitional arrangements, auditors are those firms that were appointed by the Audit Commission before its closure on 31 March 2015. The contracts with the firms are held by Public Sector Audit Appointments Ltd (PSAA) until new local audit appointment arrangements are fully implemented. Under the new arrangements, to be eligible to be a local auditor under the 2014 Act, firms will need to be registered as part of a scheme overseen by the

Financial Reporting Council (FRC) and Recognised Supervisory Bodies (RSBs) who are the professional institutes, the Institute of Chartered Accountants in England and Wales and the Institute of Chartered Accountants of Scotland. The FRC and the RSBs will also be responsible for monitoring the quality of audits.

For audits of 2018-19 accounts onwards local authorities will be able to appoint auditors themselves or opt into 'sector-led' collective procurement arrangements by which a specified person will appoint their auditors. PSAA has been specified for this purpose for principal local authorities. Local health bodies are already appointing their own auditors for audits of 2017-18 onwards.

PSAA publishes reports summarising auditors' opinions on local authorities and some health bodies. The latest report on local authorities, covering 2014-15 accounts, was published in December 2015 and can be found on the [PSAA website](#). There were two public interest reports on local authorities; [Derby City Council](#) had failures of governance in the management of major projects and in relation to Member conduct, and [City of York Council](#) had failures of governance related to payments by a wholly-owned subsidiary company of the Council to two of that company's executive directors who were also officers of the Council.

The 2014 Act also gave the C&AG new powers (from April 2014) to undertake value-for-money studies and 'provide evaluations, commentary and advice of a general nature' in the local government sector. This power enables the C&AG to provide an 'end to end' view of public services by providing insights into issues impacting on the local government sector, and to increase transparency about how central and local bodies use public funds.

Further information on the NAO's role is contained in our [June 2016 briefing](#).



The NAO's interactive outputs on local government

The NAO has produced an interactive tableau for local authority capital expenditure, which relates to investments in assets such as buildings and transport infrastructure, and resourcing, which relates to how this expenditure is paid for.

This tableau complements our June 2016 report *Financial sustainability of local authorities: capital expenditure and resourcing*, and describes changes in capital expenditure and resourcing since 2010-11 for individual local authorities using information published by the Department.

The tableau can be used to view individual local authority data and is available via the [NAO website](#).



Findings from our work on value for money – Sustainability

The NAO produces both reports aimed at local government, and reports on matters that are highly relevant to local government. The two big issues are sustainability and accountability; taken together are whether local government is maintaining effective local services under financial constraint. The NAO does not seek to issue an opinion on individual local authorities' spending.

Examples of findings from recent reports relevant to local government

Local government new burdens (June 2015)

Inadequate information systems limit how well the Department uses intelligence from the new burdens regime to understand local government pressures, but this is improving ... Departments take the cost assessment process seriously but have struggled in some cases to get reliable cost data from local authorities ... Departments rarely outline explicitly the uncertainty of cost estimates in their assessments, even where this is high ... Some departments' approaches for calculating costs created risks that new burdens would be under or overfunded

... Departments have consulted well with local authorities, using different methods ... Departments' new burdens funding to local authorities is not always transparent and can be reduced quickly, resulting in concerns about underfunding ... There is little evidence of departments reviewing new burden assessments after introducing new requirements.

Financial sustainability of fire and rescue services (November 2015)

Funding for fire and rescue authorities has fallen significantly between 2010-11 and 2015-16 ... The sector has coped well with financial challenges to date ... Fire and rescue authorities have changed the scope of their emergency response services and the scale of their prevention and protection services since 2010-11 ... Despite reductions in funding, and reductions in the number of firefighters authorities are sending to certain incidents, the number of fires and casualties have continued their long-term downward trend ... The Department's understanding of fire and rescue authorities' financial sustainability could be improved.

Local welfare provision (January 2016)

Councils' provision is aligned with other forms of support ... Councils provide different types and levels of support but there is no widespread benchmarking to help improve cost-effectiveness ... Commonly, councils either did not collect information on applicants and their needs or made limited use of this. This information would help them target support more effectively ... Since April 2015, some councils have stopped or curtailed the provision they introduced in 2013 because there is no longer specific grant funding ... Councils have limited understanding of the effectiveness of their spending on local welfare provision or the consequences of reducing this ... Demand for local welfare provision will vary from place to place and over time. Councils need to understand the factors that impact on the communities they serve in order to plan an appropriate level of support.

Findings from our work on value for money – Sustainability *continued*

Personalised commissioning in adult social care (March 2016)

Local authorities across England report a wide range in the proportions of users taking up personal budgets, including direct payments ... Recent evidence suggests that personal budgets benefit most, but not all, users and that the way a personal budget is implemented is key to whether users benefit from it ... Some local authorities are constrained in how, and the extent to which, they can personalise care by the need to reduce overall spending ... It is not clear whether local authorities will achieve the spending reductions they have forecast without putting user outcomes at risk ... Some local authorities are struggling to manage and support their local care markets as well as we would expect of a well-functioning public service market ... Authorities are taking different approaches to implementing personal budgets; some are struggling to find workable approaches.

Financial sustainability of local authorities: capital expenditure and resourcing (June 2016)

Since 2010-11, local authorities have faced less pressure on their resources to support capital expenditure relative to revenue ... The primary challenge facing authorities in managing their capital spending and resourcing has been to minimise the revenue cost of their capital programmes ... Authorities' debt servicing costs have grown as a proportion of revenue spending ... If interest rates start to rise, new borrowing will become more expensive, and authorities may also take on more external debt in order to lock in relatively low interest rates ... Counterparty risk has increased as levels of investments on deposit have grown ... Capital spending by authorities increased slightly from 2010-11 to 2014-15, but this is not even across authorities or service areas ... Authorities have focused capital spending on meeting their statutory responsibilities, engaging in 'invest to save' activities

and promoting local growth ... Authorities face a growing challenge to continue long-term investment in their existing assets ... The Department takes assurance from its devolved framework for capital which is robust, but it needs to combine this with a deeper understanding of sector-wide issues ... The Department rightly focused on revenue issues in the 2015 spending review but it will need to focus more on capital in future reviews ... The Department made a significant change within the capital control framework in 2016-17 without assuring itself sufficiently on the likely outcomes ... Authorities and the Department need to strike an appropriate balance between short- and long-term considerations with regard to capital arrangements.

Findings from our work on value for money – Accountability

Disposal of public land for new homes (June 2015)

Government recognised that disposal of surplus land, at an accelerated rate, would not necessarily lead to increased homebuilding ... Departments do not routinely monitor what happens to a site after disposal so there is no information on how many homes have been built on sold land ... DCLG does not collect information on the amount of money raised from the sales ... Without data on the number of homes or sales proceeds, DCLG cannot assess the value for money of the programme ... Accounting Officers have a responsibility to ensure sales of individual sites represent value for money.

Financial sustainability of fire and rescue services (November 2015)

Fire and rescue authorities are subject to legal controls that make it difficult for them to fail financially ... The Department's assurance over national resilience – the ability of fire and rescue authorities to respond to national incidents – is robust, but stronger in some areas than others ... The Department has largely devolved assurance over the running of fire and rescue authorities to a local level, but there are gaps in this localised system ... The Secretary of State has a statutory duty to assure Parliament on the standards of fire and rescue authorities, but the Department's evidence to support these statements is limited.

Local Enterprise Partnerships (LEPs) (March 2016)

The English devolution landscape is changing considerably and it is not yet clear how LEPs fit into it ... The Department has not set specific quantifiable objectives for what it hopes to achieve through Growth Deals, meaning that it will be difficult to assess their contribution to economic growth ... The Department's light touch assessment of LEPs' bids for Growth Deal funds relied on processes in LEPs that are not yet fully in place ... The Department has acted to promote standards of governance and transparency in LEPs ... The Department had not tested the implementation of assurance frameworks at the time that Growth Deals were finalised, and we found that there are considerable gaps in LEPs' compliance with the Department's requirements ... We found variation in the availability and transparency of financial information across LEPs.

Devolving responsibilities to cities in England: Wave 1 City Deals (July 2016)

The deals have been an important catalyst for cities to develop their capacity to manage devolved funding and responsibilities ... The government and the cities are providing the capacity and capability to manage the deals from existing resources ... There have been early impacts from some of the individual programmes agreed in the deals ... The government and cities

continue to find it difficult to know what works best in boosting local growth without a robust and shared evaluation approach.

English devolution deals (April 2016)

The scale and scope of English devolution deals increased substantially in the last 18 months... The government has announced new additional investment funding of £246.5 million a year alongside the devolution deals announced so far, but there are other financial implications of devolution deals that await confirmation ... As more devolution deals have been agreed, some aspects of more coordinated and effective management have emerged ... There are significant accountability implications arising from the agreement of devolution deals that central government and local areas will need to develop and clarify ... The devolution deals agreed so far involve increasingly complex administrative and governance configurations, and there are risks around alignment with the administrative geographical areas for other linked policies ... As devolution deals are new and experimental, good management and accountability both depend on appropriate and proportionate measures to understand their impact ... There are risks, in central government and local areas, in progressing devolution deals within a challenging financial environment, and questions about the future role of government departments.

What do the next 12 months look like?

What do the next 12 months look like?



The government is pressing ahead with plans to devolve more powers and funding to local government, accompanied by greater local accountability and increased reliance on locally raised income.



There is **uncertainty for local government following the referendum to leave the European Union**. This affects the receipt of structural funding from European institutions and the statutory requirements placed on local authorities from the adoption of European law.



Devolution deals respond to broadly-framed objectives to **support economic growth and rebalancing, public service reform and improved local accountability**. The last set of deals were announced in March 2016 during the Budget. The government has also recently **reiterated its commitment to the Northern Powerhouse** initiative.



Sustainability and transformation plans are being developed in 44 areas covering the whole of England. These plans cover all areas of NHS spending, and are expected to have **significant impacts on local health provision**. Each plan is led by a senior individual; most are from NHS Trusts or Clinical Commissioning Groups, but in Birmingham, Manchester and Nottingham the local authority is leading.



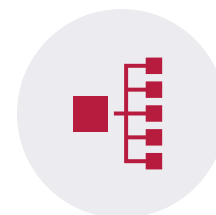
The government is running a consultation on 'Self-sufficient local government: 100% business rates retention'. **It seeks views on the government's commitment to allow local government to retain 100% of the business rates that they raise locally.**



Local authorities have been given the option to take up the former Secretary of State's offer to **agree efficiency savings in exchange for a four-year financial settlement**.



The expectation that local government will provide like-for-like replacements for homes sold through Right to Buy is likely to present a challenge during 2016-17 and beyond, as **rates of replacement need to accelerate to meet central government's expectations**.



The Cabinet Office published the response to 'A public service ombudsman: a consultation' in December 2015. The outcome **directly affects the Local Government Ombudsman, which will be merged with the Parliamentary and Health Service Ombudsman**.