

Communities and Local Government Select Committee Inquiry into the 'Fiscal Devolution to Cities and City Regions' (January 2014)

Written evidence submitted by the Centre for Urban and Regional Development Studies (CURDS), Newcastle University, UK NE1 7RU www.ncl.ac.uk/curds

Dr Peter O'Brien, Research Associate (peter.o'brien@newcastle.ac.uk)

Professor Andy Pike, Director (andy.pike@newcastle.ac.uk)

Professor Danny Mackinnon, Professor of Regional Development and Governance (danny.mackinnon@newcastle.ac.uk)

David Marlow, Visiting Professor of Practice (david.marlow@newcastle.ac.uk)

Liz Robson, Visiting Fellow (liz.robson@newcastle.ac.uk)

Executive Summary

- The UK has a highly centralised system of taxation and expenditure, in an international context. The UK therefore needs to consider appropriate forms of fiscal decentralisation and public policy reform as a set of tools that can help cities and city regions move beyond the narrow definitions of economic growth and instead focus on building sustainable and successful places, businesses, jobs and communities. There should be genuine decentralisation by Government and all Departments and Agencies need to subscribe to the process.
- Places are more likely to be successful if they possess effective, sound and high quality institutions and leadership driving forward effective visions and evidence-based strategies. Business involvement in local and regional development should be rooted in accountability and transparency. Different governance models may exist in different cities and city regions. However, the principles of openness, public accountability and scrutiny should underpin all decentralised governance arrangements.
- We support the creation of meaningful 'Centre-Local Contracts', such as 'Contrats de Ville', as exist in France, to manage decentralisation and multi-level governance.¹ In terms of accountability, it is important to distinguish between audit and scrutiny. It is insufficient for 'devolved' areas to introduce financial management processes without also being subject to broader public oversight. The use of public service outsourcing requires effective scrutiny of decision-making and delivery.
- International evidence suggests that decentralisation alone may not generate an automatic economic dividend. However, overt centralisation of activity and governance is likely to stifle local and regional innovation, decision-making, governance and development. Decentralisation should be seen within the context of the continued importance of national-local government relationships.

¹ Kamal-Chaoui, L. and Sanchez-Reaza, J. (eds.) (2012), 'Urban Trends and Policies in OECD Countries', [OECD Regional Development Working Papers 2012/01](#), Paris, OECD Publishing.

- Narrow forms of devolution and decentralisation could pose a challenge to macro spatial economic efficiency and equity. If the geography of fiscal decentralisation is fixed at too small a scale there are risks of inequalities in resource and policy outcomes – post code lottery issues – and displacement to neighbouring cities or local areas. Cities and city regions need to consider carefully the geography of areas seeking greater fiscal autonomy – and if necessary improve and build effective collaboration. Local authorities also need to consider the risks associated with having the responsibility for forecasting future Business Rate revenues.
- The call for greater fiscal decentralisation in England is taking place within broader debates about constitutional arrangements in the UK. The Core Cities proposal for a new legally binding agreement between local and national government is a useful suggestion. However, it is questionable whether Combined Authorities represent radical constitutional change. This raises questions about the UK's lack of a written constitution.
- Property taxes are most likely to be decentralised by Central Government, and in line with developments in Scotland and Wales. Yet, the experience to date suggests that any further fiscal decentralisation in England is likely to be incremental.
- The UK Government can borrow at the most competitive rates from the international capital markets. Local government requires certainty over the Public Works Loan Board interest rate in order to have sufficient confidence to borrow for investment purposes. Encouraging local institutions to innovate in their financing arrangements is welcome as long as their endeavour is supported by appropriate decentralised autonomy and support. Borrowing to invest in infrastructure is sensible if it is underpinned by evidence-based national and local infrastructure strategies.
- There are a range of initiatives that cities and city regions can introduce to raise new finance. As the municipal bond market has been relatively inactive in the UK, councils will need expert advice on how to engage with what is a costly and complex model.
- We believe that any move towards fiscal decentralisation should be based on a robust assessment of the costs and benefits to individual cities and local authorities. Decentralisation should build on the inherent strengths of all cities and regions to the benefit of the national economy and not exacerbate spatial disparities. If policy-makers are serious about the need for spatial balance in the economy and fostering a balanced recovery, then fiscal decentralisation should itself incorporate a significant element of geographical redistribution, directing greater resources towards areas of greatest need.

1. About CURDS

1.1 The Centre for Urban and Regional Development Studies (CURDS) is an internationally-recognised centre for the study of local and regional development.

Newcastle University is a partner in the EPSRC and ESRC i-BUILD (Infrastructure BUiness models, valuation and Innovation for Local Delivery)² in which CURDS is leading on the study of innovative forms of finance for city infrastructure, and associated governance and regulation mechanisms. Within the research, CURDS will be examining the role of City Deals in local infrastructure finance and delivery. In 2013, CURDS undertook the first National Survey of all 39 Local Enterprise Partnerships (LEPs) in England, as part of its involvement with the ESRC, BIS, DCLG and Welsh Assembly Government-funded Spatial Economics Research Centre (SERC).³

2. How public services, including employment, skills and welfare, should be organised to complement devolution

2.1 The UK has a highly centralised system of taxation and expenditure, in an international context⁴ (Table 1). Figure 1 illustrates how the situation has been getting more centralised in the UK. UK local authorities, including city councils, rely heavily upon inter-governmental transfers rather than local fiscal autonomy.⁵

Table 1: Tax Set at Each Level of Government as a Percentage of GDP (2011)

| | Local Government | State/Regional Government | Local + State/Regional | Central Government | Social Security | Total |
|----------------|------------------|---------------------------|------------------------|--------------------|-----------------|-------|
| Canada | 3.1 | 12.2 | 15.3 | 12.8 | 2.9 | 31.0 |
| France | 5.8 | 0 | 5.8 | 14.4 | 23.9 | 44.2 |
| Germany | 3.0 | 7.9 | 10.9 | 11.8 | 14.3 | 37.1 |
| Italy | 6.8 | 0 | 6.3 | 22.6 | 13.4 | 42.9 |
| Spain | 3.0 | 7.3 | 10.8 | 9.5 | 11.7 | 31.6 |
| Sweden | 15.9 | 0 | 15.9 | 22.8 | 5.6 | 44.5 |
| United Kingdom | 1.7 | 0 | 1.7 | 26.9 | 6.7 | 35.5 |
| United States | 3.9 | 5.2 | 9.1 | 10.3 | 5.7 | 25.1 |
| OECD (2010) | 3.9 | 5.0 | 8.9 | 20.2 | 8.3 | 33.8 |

Source: OECD Revenue Statistics Comparative tables, <http://tinyurl.com/revenuestatistics>

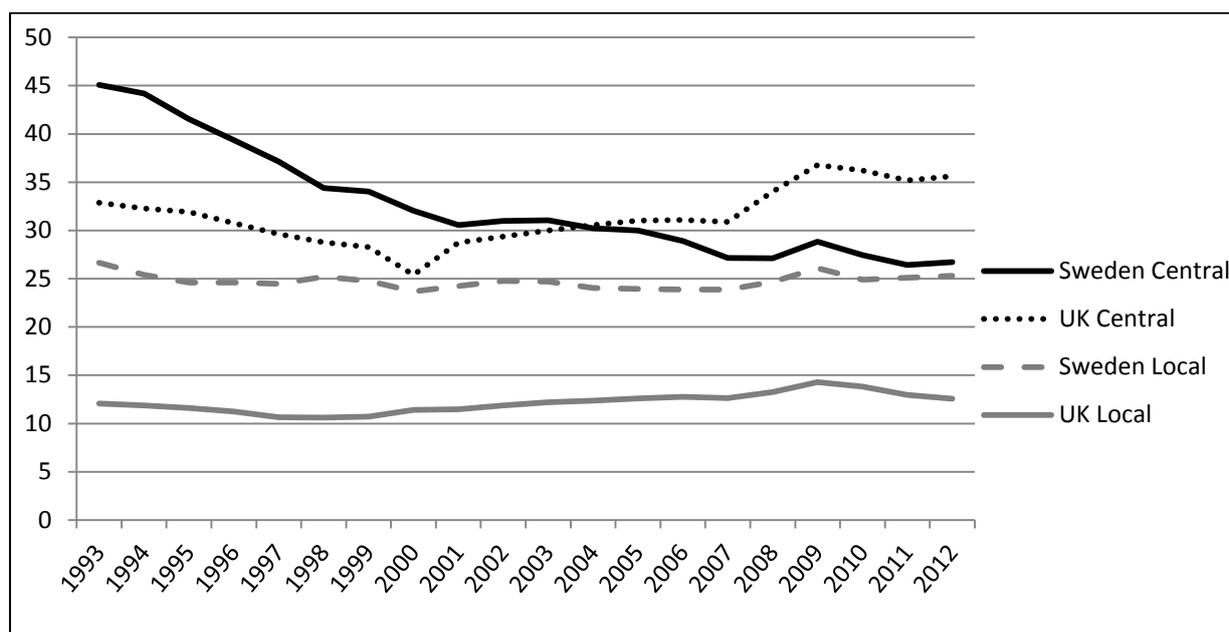
² See <http://research.ncl.ac.uk/ibuild>

³ Pike, A., Marlow, D., McCarthy, A., O'Brien, P. and Tomaney, J. (2013) Local Institutions and Local Economic Growth: The State of the Local Enterprise Partnerships in England – A National Survey, London, SERC Discussion Paper 150: www.spatial-economics.ac.uk/textonly/SERC/publications/download/sercdp0150.pdf

⁴ Travers, T. (2012) Local Government's role in promoting economic growth: Removing unnecessary barriers to success, London, Local Government Association.

⁵ Slack, E. (2013) International Comparison of Global City Financing: A Report to the London Finance Commission, University of Toronto.

Figure 1: Government (Sweden and UK Central and Local) Expenditure as a % of GDP⁶



Source: OECD Fiscal Decentralisation Database

2.2 The Coalition Government has placed significant emphasis on decentralisation as a means of shaping public service reform, strengthening ‘democratic engagement’ and creating more open and transparent government.⁷ Cities are a key area where the Government’s decentralisation effort has been focused.

“Decentralisation is not just an ideal. It has an essential role to play in achieving the Coalition’s core objectives.” (Rt. Hon Greg Clark MP)⁸

2.3 The 2013 Core Cities Prospectus for Growth sets out the case for fiscal decentralisation and the specific policies that should be devolved to local areas.⁹ These include: Jobs and Skills; Housing; Transport; and Business Growth and Innovation. The Core Cities also propose that new place-based settlements and integrated public services delivery arrangements are introduced, which echoes similar themes raised in the Local Government Association’s (LGA) ‘Rewiring Public Services: Rejuvenating Democracy’ campaign.¹⁰

2.4 The Greater Manchester City Region has played a leading role in bringing together the decentralisation of fiscal and economic responsibilities alongside emergent models of public services delivery, and provides evidence of local innovation when meaningful decentralisation has been exercised. Greater Manchester’s City Deal Earnback mechanism

⁶ The chart shows consolidated expenditure of each level of government as defined as total spending minus the inter-governmental transfer spending of that government level.

⁷ DCLG (2010) *Decentralisation and the Localism Bill: An Essential Guide*, London, Department for Communities and Local Government.

⁸ DCLG (2012) *Decentralisation: An Assessment of Progress*, London, Department for Communities and Local Government: p. 3.

⁹ Core Cities (2013) *Competitive Cities, Prosperous People: A Core Cities Prospectus for Growth*, Manchester, Core Cities.

¹⁰ LGA (2013) *Rewiring Public Services*, London, Local Government Association.

proposes to generate growth through infrastructure investment and then return a share of the 'proceeds of growth' (through higher tax takes and a lower benefits bill) back to the City Region. In the Community Budget Pilots, which have identified the scope for reorganising frontline public services, Greater Manchester estimates that it could achieve £270 million of net savings over five years.¹¹

2.5 Decentralisation and public policy reform are a set of tools that can help cities and city regions move beyond the narrow – and averaged over the area measures of GVA per capita that mask inequality – definitions of economic growth and focus on building sustainable and successful places, businesses, jobs and communities. David Marlow, Visiting Professor of Practice at CURDS, suggests that integrated community budgets could be aligned with 'economically-focused' City Deals:

"Greater Manchester's community budget sits explicitly alongside the Greater Manchester city deal and the combined authority as one of three major mechanisms for implementing a Greater Manchester strategy. The city region's focus on growth is, in some senses, progressed through the city deal. The community budget seeks to lower 'failure demand' for public services through early intervention to tackle early years, troubled families, criminal justice, health and social care issues. If successful, this would enable disadvantaged households and communities to participate in and benefit from Greater Manchester's city deal economic opportunities in a virtuous 'win-win' circle."¹²

2.6 The London Finance Commission also calls for an extension to the remit and scale of Community Budget Pilots¹³, and the idea of integrating local economic development with public service reform appears to have some momentum. The 2013 Autumn Statement saw the Government encourage the submission of "[public] service reform proposals made by local enterprise partnerships as part of the Growth Deals process".¹⁴

2.7 However, if fiscal decentralisation and public service reform are to succeed there should be genuine decentralisation by Government and then all Departments and Agencies need to subscribe to the process rather than working, as has been the case in the past, with different levels of enthusiasm, commitment and even definitions of decentralisation.¹⁵ In its assessment of the Community Budgets Programme the Public Accounts Select Committee suggests that:

"This early promise now requires continued support from across the Government to translate it into real change on the ground, such as support from the Department for

¹¹ NAO (2013) Case Study on Integration: Measuring the Costs and Benefits of Whole-Place Community Budgets, London, National Audit Office.

¹² <http://davidmarlow.regen.net/2012/10/08/are-community-budgets-an-alternative-to-city-deals>

¹³ LFC (2013) Raising the Capital: The Report of the London Finance Commission, London, London Finance Commission.

¹⁴ HMT Autumn Statement 2013, London, HM Treasury, p. 83.

¹⁵ CLG (2010) Research into multi area agreements: long term evaluation of LAAs and LSPs, London, Communities and Local Government.

Business, Innovation and Skills to help ensure local areas are able to align skills and training provision with their plans to generate economic growth.”¹⁶

3. How ‘devolved’ areas would be governed, including the role of business in decision making

3.1 Different models for overseeing and guiding local and regional economic development are surfacing in England. Places that are more likely to be successful are those areas that have quality institutions and strong leadership driving forward clear and effective visions and evidence-based strategies. In parts of northern England, future strategic economic leadership will be provided jointly by Combined Authorities and LEPs.¹⁷ The division of responsibilities between the two is still unclear but proponents see Combined Authorities as providing robust governance and accountability in local areas.¹⁸

3.2 In the CURDS National LEP Survey we found that those LEPs that had been absorbed into existing local structures had greater accountability and legitimacy.¹⁹ Business involvement in local and regional development should be rooted in accountability and transparency, and it is a source of concern that some LEPs do not know who they are ultimately accountable to.

3.3 The role and status of the Private Sector LEP Chair is crucial to shaping the character and focus of LEPs, with the quality of leadership fundamental to defining the LEP and articulating its vision, strategy and priorities.

3.4 With LEPs facing a growing array of tasks and responsibilities, there is a paradox between the role of LEPs as strategic bodies (i.e. their original remit) and the partnerships being encouraged to act more as ‘delivery agents’. This is manifesting itself in LEP Boards where some Business Members are concerned at whether they possess the necessary skills and experience. As LEPs allocate and disperse greater amounts of funding, the issues of legal status and indemnities have arisen, which has provided a stimulus for more LEPs opting to become limited companies.

3.5 City Deals and Growth Deals are a means for local areas to decide strategic economic priorities and to negotiate and conclude agreements with Government. However, an evident practical challenge is to understand and deconstruct how these Deals are achieved. David Marlow’s recent blog offers an instructive contribution on the subject:

¹⁶ PAC (2013) Integration across Government and Whole-Place Community Budgets, Fourteenth Report of Session 2013-14, London, House of Commons.

¹⁷ Public consultations have been taking place on proposals to establish Combined Authorities in West Yorkshire, Sheffield City Region, the North East and Greater Merseyside.

¹⁸ Sir Howard Bernstein, Chief Executive, Manchester City Council, writing in The Guardian, Monday 15 October 2012, ‘Greater Manchester Combined Authority is a Model for other Regional Cities’: <http://www.theguardian.com/public-leaders-network/2012/oct/15/greater-manchester-combined-authority-regional>

¹⁹ Pike, A., Marlow, D., McCarthy, A., O’Brien, P. and Tomaney, J. (2013) Local Institutions and Local Economic Growth: The State of the Local Enterprise Partnerships in England – A National Survey, London, SERC Discussion Paper 150.

“When history comes to evaluate the Coalition Government’s approach to local growth, I suspect the fundamental critique of 2010-15 will be the subsuming of political values and conviction – whether to localism, city leadership, rebalancing, really to anything – in a series of tactical and one-sided ‘deals’. The ‘deal’ approach allows government to deconstruct 39 LEP, 28 City, and any number of other places’ ambitions into a series of bilateral negotiations with individual departments and agencies. The ‘deal’ model requires local leadership teams to ‘prove’ each individual proposition in a demonstration of their abilities to ‘haggle’ with an oligarchic patron. The default position is agreement to a slightly modified status quo where government retains the preponderance of powers, resources, flexibilities and influence.....”²⁰

3.6 Government emphasises the value of deals in encouraging innovation, bespoke local approaches and decentralisation. Yet the deal-making system and culture raises questions concerning effectiveness, consistency and equal treatment and the loss of scale economies in policy-making at the centre.

4. How ‘devolved’ areas would be held to account

4.1 In preference to the unbalanced deal-making system that is emerging, we support the creation of meaningful ‘Centre-Local Contracts’ to manage decentralisation. OECD analysis of international practice, such as the ‘Contrats de Ville’ that operate in France, suggests that it is possible to allow for innovation, tailored local approaches and decentralisation but within a more transparent, fair and accountable system.²¹ In terms of accountability, it is important to distinguish between audit and scrutiny. It is insufficient for ‘devolved’ areas to introduce financial management processes without also being subject to broader public oversight.

4.2 The use of public service outsourcing²² requires effective scrutiny of decision-making and delivery.

4.3 Some Combined Authorities, such as Greater Manchester, have established formal scrutiny arrangements that provide a check and balance on the executive.²³ Other measures, such as publishing papers and minutes of meetings, should form an integral part of the governance of cities, city regions and LEPS. Public meetings, in which individuals and communities have the opportunity to question decision-makers, should also be held.

4.4 In relation to executive and legislative responsibility, the Core Cities are seeking a change in Parliamentary Standing Orders to limit the questions that Ministers can ask of

²⁰ <http://davidmarlow.regen.net/2013/12/05/what-do-wave-two-city-deals-tell-us-about-potential-offers-and-asks-for-local-growth-deals/#more-636>

²¹ Kamal-Chaoui, L. and Sanchez-Reaza, J. (eds.) (2012), ‘Urban Trends and Policies in OECD Countries’, OECD Regional Development Working Papers 2012/01, Paris, OECD Publishing.

²² HMG (2011) Open Public Services White Paper, London, The Stationery Office.

²³ Greater Manchester City Region has announced a ‘root and branch’ review of its Combined Authority, LocalGov, 20 December 2013: <http://www.localgov.co.uk/Combined-authority-review-launched/35266>

local politicians.²⁴ While the UK Parliament has a crucial role, concerns have been raised about the suitability and capacity of Parliament to monitor local government spending, particularly as the Audit Commission is wound down.²⁵

5. The strength of the evidence that devolution would lead to economic growth, local improvement and better local governance, including examples of what areas could do with their new powers such as use them to invest in infrastructure and local services

5.1 Decentralisation is an international phenomenon.²⁶ Within new and emergent forms of local and regional economic development there has been a resurgence of local and regional levels of government – driven by the devolution of powers from central governments.²⁷ Detailed studies of OECD member countries – between 1980 and 2005 – suggest that there is a weak correlation between decentralisation and economic growth,²⁸ whilst recent analysis indicates that it is difficult to draw firm conclusions about local fiscal autonomy and the economic success of cities.²⁹ Studies of the UK’s distinct experience have also found inconclusive evidence to date of an economic dividend emerging from devolution.³⁰

5.2 The Core Cities contend that there is a “[S]trong relationship between the ability of cities to drive growth, the levels of local financial control and the freedom to make policies match the needs of places”,³¹ derived from the perceived benefits of ‘tax competition’ and the power to raise *additional* revenue to fund goods, services and infrastructure. Other studies suggest that sub-national and local governments could assist with national fiscal consolidation (and reduce central transfers) if they raised more taxes locally.³²

²⁴ Core Cities (2013) Competitive Cities, Prosperous People: A Core Cities Prospectus for Growth, Manchester, Core Cities.

²⁵ The Chair of the Public Accounts Select Committee, Margaret Hodge, has expressed concerns about the ability of Parliament to monitor the spending of local authorities:
<http://themj.co.uk/article/?id=195103&typeid=1>

²⁶ DCLG (2010) Decentralisation outcomes: a review of evidence and analysis of international data: a report prepared by CURDS, Newcastle University and the Department of Geography and Environment, London School of Economics, London, Department for Communities and Local Government.

²⁷ Mackinnon, D. and Cumbers, A. (2011) Introduction to Economic Geography: Globalization, Uneven Development and Place: 2nd Edition, Harlow, Pearson.

²⁸ Rodríguez-Pose, A. and Ezcurra, R. (2011) ‘Is fiscal decentralization harmful for economic growth? Evidence from the OECD countries’, Journal of Economic Geography, pp: 619-643; Ezcurra, R. and Rodríguez-Pose, A. (2013) ‘Political Decentralization, Economic Growth and Regional Disparities in the OECD’, Regional Studies, 47(3): pp. 388-401.

²⁹ Slack, E. (2013) International Comparison of Global City Financing: A Report to the London Finance Commission, University of Toronto.

³⁰ Pike, A., Rodríguez-Pose, A., Tomaney, J., Torrissi, G. and Tselios, V. (2012) ‘In search of the ‘economic dividend’ of devolution: spatial disparities, spatial economic policy and decentralisation in the UK’, Environment and Planning C: Government and Policy, 30: pp. 10-28.

³¹ Core Cities (2013) Competitive Cities, Prosperous People: A Core Cities Prospectus for Growth, Manchester, Core Cities: p. 7.

³² OECD (2013) Fiscal Federalism 2014: Making Decentralization Work, Paris, Organisation for Economic Co-operation and Development.

5.3 Research led by Professor Michael Parkinson CBE, on ‘Second Tier Cities’, offers a useful perspective on decentralisation and the contribution of cities to national competitiveness and welfare. It suggests that genuine decentralisation to cities (including but crucially also beyond capital cities), alongside recognition of the importance of the continuing different roles of, and relationship between, national governments and local actors, underpinned by balanced territorial public and private investment, will provide the basis in the long term for successful national economies and higher performing cities.³³

5.4 The call for cities and localities to be given new tax and borrowing powers is predicated on a view that the benefits of fiscal decentralisation could be (re)invested in infrastructure to support urban growth,³⁴ albeit within a national framework.³⁵ This represents, in part, an attempt to reverse the trend of successive UK Governments in favouring consumption over capital spending.³⁶ To illustrate, the proposed new fiscal powers for the Welsh Assembly Government are being linked directly to the upgrade of the M4 Motorway.³⁷ Whilst in London, the Greater London Authority (GLA) sees fiscal decentralisation as a key element of the London Infrastructure Investment Plan 2050.³⁸

6. The impact on areas not included in any new devolution arrangements, including those on cities’ borders and those affected by resulting changes to national financial equalisation and distributive arrangements

6.1 Decentralisation of authority and resources from nation-states to regions and localities could pose a challenge to macro spatial economic efficiency and equity.³⁹ A highly unequal map of resources and prosperity could result. A narrow definition of fiscal decentralisation, stemming from a highly competitive model of urban development, could harden the inequality between core and peripheral areas shaped by market processes, agglomeration economies and increasing returns.⁴⁰ If the geography of fiscal decentralisation is fixed at too small a scale there are risks of ‘tax flight’ as businesses and individuals seek the benefits of lower taxes in neighbouring cities or local areas.⁴¹

³³ Liverpool JMU (2012) Second Tier Cities in Europe: In an Age of Austerity Why Invest Beyond the Capitals? Liverpool, ESPON and European Institute of Urban Affairs, Liverpool Sir John Moores University.

³⁴ LFC (2013) Raising the Capital: The Report of the London Finance Commission, London, London Finance Commission.

³⁵ HMT and UKI (2013) National Infrastructure Plan, London, HM Treasury and UK Infrastructure.

³⁶ Travers, T. (2012) Local Government’s role in promoting economic growth: Removing unnecessary barriers to success, London, Local Government Association.

³⁷ HMT and Wales Office (2013) Empowerment and responsibility: devolving financial powers to Wales, London, HM Treasury and Wales Office.

³⁸ Presentation by the Senior Manager, Growth and Enterprise, GLA, at the Engagement Event on the ‘London Infrastructure Investment Plan 2050’, 16 December 2013.

³⁹ Rodríguez-Pose, A. and Gill, N. (2003) ‘The global trend towards devolution and its implications’, Environment and Planning C: Government and Policy, 21: pp. 333-351.

⁴⁰ Garretsen, H., McCann, P., Martin, R. and Tyler, P. (2013) ‘The future of regional policy’, Cambridge Journal of Regions, Economy and Society, 6: p. 179-186.

⁴¹ Mikesell, J. L. (2010) ‘The Contribution of Local Sales and Income Taxes to Fiscal Autonomy’, in G. K. Ingram, and Y.-H. Hong (Eds.) Municipal Revenues and Land Policies (pp. 147-78). Cambridge, Massachusetts, Lincoln Institute of Land Policy.

6.2 We would caution policy-makers against seeing fashionable ‘off the shelf’ policy prescriptions as instant remedies for tackling low growth. Local context and historical paths of development shape, to a large degree, the socio-economic, political and cultural geographies of particular places, including cities and city regions.⁴² Certain strategies and policies may work in one particular place but may not be appropriate in others.

6.3 New local government finance arrangements have been introduced in England and Wales, against a backdrop of real term reductions in local government formula/grant funding of a magnitude not seen recently.⁴³ In the new Business Rate Retention Scheme (BRRS), safety net payments will be made to local authorities whose income drops below baseline funding. This risks entrenching the inequalities between more and less prosperous places with different growth potentials. In addition, the Government has encouraged authorities to pool BRRS to manage risks. Crucially, however, councils will now share the risks of any overestimations of business rates. As a footnote, according to the National Audit Office, between 2006 and 2011, the Office for Budget Responsibility overestimated the net yield of business rates in four out of five years.⁴⁴

7. Whether reform of the existing system (for example, re-banding council tax, revaluing business rates, Community Budgets, Government grants, formulas and taxes such as stamp duty) would be a precursor to, or run along with, large-scale constitutional change

7.1 The call for greater fiscal decentralisation in England is taking place within broader debates about the constitutional arrangements in the UK.⁴⁵ The UK is out of step internationally and especially its cities and localities in England outside London. Scotland, Wales and London have existing structures that the UK Government can negotiate with and devolve powers to. In England, beyond London, the recipients of possible fiscal devolution are still to be finalised. Although the Government sees Combined Authorities as bodies that it can devolve powers and funding to, it is questionable whether such structures represent radical constitutional change.^{46 47}

7.2 The Core Cities are proposing a new legally binding agreement between local and national government to set out new roles and responsibilities. Other changes include the co-

⁴² Pike, A., Rodríguez-Pose, A. and Tomaney, J. (2006) Local and Regional Development, London, Routledge.

⁴³ House of Commons (2013) The Local Government Finance Settlement 2013/14 and 2014/15: Research Paper 13/10, London, House of Commons Library.

⁴⁴ NAO (2013), Financial sustainability of local authorities, London, National Audit Office.

⁴⁵ Yorkshire Post (2013) ‘Boris demands tax powers for cities as boost for economy’, 18 December 2013: <http://www.yorkshirepost.co.uk/news/main-topics/general-news/boris-demands-tax-powers-for-cities-as-boost-for-economy-1-6322307#.UrMNYqKfqR4.twitter>

⁴⁶ Marlow, D. (2013) ‘Combined Authorities are a tactical device for councils to gain funding’, The Guardian: <http://www.theguardian.com/local-government-network/2013/jul/04/combined-authorities-manchester-sheffield-leeds>

⁴⁷ In the proposal to establish a Combined Authority for Durham, Northumberland and Tyne and Wear, the Department for Communities and Local Government writes that it recognises that there are ‘substantive material differences between a regional assembly and a combined authority’ and that ‘a combined authority is more an enhancement of existing joint [local government] arrangements’.

design of policies that affect cities.⁴⁸ The LGA is pushing for multi-year budgets, new powers to raise bonds and ‘constitutionally-embedded’ local government.⁴⁹

7.3 Nations and cities/city regions compete with each other but also collaborate when there is a shared strategic interest. London, for example, sees the objective of fiscal decentralisation as a collective endeavour with the Core Cities.

8. What taxes might be devolved – for example council tax, stamp duty and business rates?

8.1 The London Finance Commission recommends that the full suite of property taxes (council tax, business rates, stamp duty land tax, annual tax on enveloped dwellings and capital gains (i.e. Mansion Tax) should be devolved to London. The Core Cities want the devolution of property taxes; limited powers to raise taxes (e.g. a VAT supplement or hotel room tax); the possibility of a local business bank; and the extension of the single pot approach to capital funds.

8.2 The UK Government plans to devolve, to the Welsh Assembly Government, landfill tax and stamp duty land tax; and to legislate for a referendum on whether a percentage of income tax should be devolved to the Welsh Assembly Government.

8.3 Our view is that the nature of the arrangements for local authorities to retain business rates points towards some further limited decentralisation of property taxes. However, given the economic context, political sensitivities and Central Government influence over local taxation⁵⁰, any additional fiscal decentralisation in England is likely to be incremental in nature.

8.4 Greater fiscal autonomy should not intensify spatial disparities or impact negatively upon those unable to pay additional tax. Transfers and safety net systems should not be compromised and unpicked as part of greater decentralisation. In the United States, property taxes are typically regressive, and poorer homeowners pay more of their incomes in property taxes than any other group.⁵¹

9. What changes should be made to “devolved” authorities’ borrowing powers?

9.1 The GLA is asking for local authority borrowing limits (within the Prudential Code) to be relaxed whilst the Core Cities wants the Government to raise the Housing Revenue Account borrowing cap.

⁴⁸ Core Cities (2013) Competitive Cities, Prosperous People: A Core Cities Prospectus for Growth, Manchester, Core Cities.

⁴⁹ LGA (2013) Rewiring Public Services, London, Local Government Association.

⁵⁰ In the Autumn Statement 2013, the Chancellor of the Exchequer indicated that the Government expects local authorities to freeze council tax bills in 2014/15.

⁵¹ ITEP (2013) Who Pays? A Distributional Analysis of Tax Systems in All 50 States, Washington DC, The Institute on Taxation and Economic Policy.

9.2 In October 2010, HM Treasury made borrowing for councils more expensive by raising the Public Works Loan Board (PWLB) interest rate.⁵² However, the desire by the centre to encourage local institutional innovation for borrowing is potentially costly, uncertain and risky relative to HM Government. The UK Government could borrow at a cheaper rate than local authorities, but deficit reduction is the overriding objective of the Coalition.⁵³ New forms, instruments or business models of debt finance need to be explored where Central and Local Government can work together/co-operate to reduce costs, pool risks and provide effective finance for investment – e.g. like the kinds of guarantees that HM Treasury is prepared to give London’s Government.⁵⁴

9.3 Following the PWLB rate rise, local authority borrowing fell by 93 per cent.⁵⁵ Subsequently, in the 2012 Budget, the Chancellor of the Exchequer announced a 0.2 per cent decrease in the PWLB rate. Furthermore, in the 2012 Autumn Statement, the Government announced that it was creating a concessionary PWLB ‘Project Rate’ for LEPs. This was followed by a further announcement in 2013 that cheaper borrowing, of up to £400 million, was to be made available for priority local infrastructure projects in Scotland and Wales. In England, LEPs and local authorities will have also access to an additional £800 million of borrowing as part of the new Growth Deals.

9.4 The UK Government accepts that the Welsh Assembly Government should have new capital borrowing arrangements subject to a proposed referendum on income tax powers.⁵⁶ The Welsh Government will also be offered early access to limited capital borrowing in order to fund immediate improvements to the M4 Motorway.

9.5 The relationship between devolved areas’ borrowing powers and use of the UK Government balance sheet is also evident in London, where the Treasury is providing a guarantee to enable the GLA to borrow £1 billion from the PWLB to help fund the Northern Line Underground extension.

9.6 Under the Prudential Borrowing Framework (PBF) local authorities can borrow for capital expenditure purposes without obtaining prior UK Government approval. Within the PBF, local government officers assess the sustainability of borrowing and set limits in line with the Prudential Code, which requires councils to have the financial capacity to repay debt as borrowing is unsecured by assets.⁵⁷ However, because PBF increases overall public sector borrowing, the Treasury retains the ability to cap PBF.

⁵² HMT (2010) Pre-Budget Report, London, HM Treasury.

⁵³ LGC (2011) ‘Councils deny borrowing binge accusations’, Local Government Chronicle: <http://www.lgcplus.com/5020944.article>

⁵⁴ Greater London Authority Report (November 2013) to the Mayor setting out the details (including the financial arrangements) for the Northern Line Underground Extension: <http://www.london.gov.uk/sites/default/files/MD1269%20NLE%20Part%201%20PDF.pdf>

⁵⁵ LGC (2011) ‘Borrowing slumps following shock rate rise’, Local Government Chronicle: <http://www.lgcplus.com/briefings/corporate-core/finance/borrowing-slumps-following-shock-rate-rise/5025329.article>

⁵⁶ HMT and Wales Office (2013) Empowerment and responsibility: devolving financial powers to Wales, London, HM Treasury and Wales Office.

⁵⁷ Bailey, S., Asenova, D. and Hood, J. (2012) The UK’s Prudential Borrowing Framework: Professional Discipline and Control’, Local Government Studies, 38(2): pp. 211-229.

10. The scope for areas to introduce new taxes and funding methods such as bonds and crowd-sourcing, fees and charges

10.1 Faced with higher borrowing costs and changes to the Housing Revenue Account system some local authorities see bond issuance as an alternative source of finance.⁵⁸

10.2 In the United States, states and cities have borrowed from the municipal bond markets for many years. By the end of 2011, there were over one million different municipal bonds outstanding in the US, in a total aggregate principal amount of more than \$3.7 trillion.⁵⁹ The GLA became the first UK local authority for seventeen years to issue bonds when, in 2011, it raised £600 million towards Crossrail. The GLA needs to borrow a total of £3.5 billion, which is being secured against a business rate supplement.⁶⁰

10.3 Bond issuance suits bigger local authorities, which is why the LGA wants to create a local authority collective bond agency for all authorities.⁶¹ However, the municipal bond market has been relatively inactive in the UK, and councils will need expert advice and support on how to engage with a model that is more complex and more costly than the PWLB.⁶²

10.4 The GLA, in its emerging London Infrastructure Investment Plan 2050, identifies crowd-financing as a way of providing new finance. The Authority is also exploring the possibility of hypothecated taxes to deliver specific projects – subject to ballots. In the United States voters can decide whether local areas should levy taxes or borrow to fund capital projects⁶³ or whether the public or community sectors should own infrastructure assets.⁶⁴

10.5 There is also renewed interest in the UK in the merits of a Land Value Tax (LVT).⁶⁵ Proponents argue that a LVT could stabilise house prices and raise funds.⁶⁶ At present, increases in land values usually come from external developments – such as infrastructure – which, in the past, have not sought a financial contribution from the land owner.

⁵⁸ Financial Times (2011) 'Council Bond Issuing Plans Gaining Momentum', <http://www.ft.com/cms/s/0/7e8b9ffa-d3c3-11e0-bc6b-00144feab49a.html#axzz2nqTdhc8o>, 31 August 2011.

⁵⁹ SES (2012) Report on the Municipal Securities Market, Washington DC, US Securities and Exchange Commission.

⁶⁰ Powers were granted to the GLA to introduce this under the 2009 Business Rates Supplements Act.

⁶¹ LGA (2012) Local Authority Bonds: a local government collective agency, London, Local Government Association.

⁶² Symonds, T. (2011) Capital Futures: local capital finance options in an age of recovery, London, New Local Government Network.

⁶³ Lee, J. A., Muro, M. and Katz, B. (2013) Using Ballot Measures to Drive Economic Investment in States and Metropolitan Areas, Washington DC, Brookings Institute.

⁶⁴ Renew Economy (2013) 'Boulder votes to buy back the grid to accelerate renewables': <http://reneweconomy.com.au/2013/boulder-votes-to-buy-back-the-grid-to-accelerate-renewables-16411>

⁶⁵ The Guardian (2012) 'IFS backs land value tax', 2 February 2012: <http://www.theguardian.com/business/economics-blog/2012/feb/02/ifs-backs-land-value-tax>

⁶⁶ Seely, A. (2013) House of Commons Library Note Sn6558 on Land Value Tax, London, House of Commons.

10.6 Other funding initiatives include the Community Infrastructure Levy and evergreen funds where capital funding is loaned at or near commercial rates to public and/or private sector, paid back and subsequently re-invested in other projects. A number of LEPs and city regions are creating Revolving Infrastructure Funds, drawing on ‘pump prime’ resources from the Regional Growth Fund, Growing Places Fund, European Regional Development Fund, European Investment Bank, Enterprise Zones and Pension Funds. Cities and city regions are also turning to local authority pension funds to finance capital projects. Birmingham City Council is actively marketing the city to international investors, specifically global sovereign wealth funds.⁶⁷

11. The extent to which high-performing areas would be expected to redistribute their proceeds of growth via the Treasury

11.1 Both the London Finance Commission and Core Cities are seeking greater tax and borrowing powers within a framework that has a neutral effect on the remainder of local government finance (allowing for equalisation). We believe that fiscal decentralisation should be based on a robust assessment of the costs and benefits to individual cities and local authorities – and not undermine fiscal safety nets or transfers to less prosperous places with less growth potential.

11.2 The role of UK Government, working with cities, local authorities and LEPs should also not be overlooked. We think there is genuine merit in the Core Cities suggestion of a new constitutional agreement between Government and local authorities.

11.3 The tentative recovery of the UK economy is geographically unbalanced. Fiscal decentralisation to cities and city regions should build on the inherent economic strengths of all cities and regions⁶⁸ to the benefit of national economies, and not exacerbate (inadvertently or otherwise) disparities between different places. If policy-makers are serious about the need for spatial balance in the economy and fostering a balanced recovery, then fiscal decentralisation should itself incorporate a significant element of geographical redistribution, directing greater resources towards areas of greatest need.

11.4 Decentralisation alone may not generate an automatic economic dividend. To maximise the potential for creating more rounded and enduring local and urban growth, we would recommend that Government creates the conditions for more balanced territorial investment by introducing a new non-competitive sub-national strategic (capital) investment framework for England.

⁶⁷ Birmingham City Council (2013) Birmingham Sovereign Wealth and Institutional Funds Investment Prospectus.

⁶⁸ Garcilazo, E. (2012) Promoting Growth in All Regions, Paris, OECD.