

Local Government and Public Services Committee

LGPS(2)–05-06(p4)

Meeting date: Wednesday, 15 March 2006

Meeting venue: Committee Room 3&4, Assembly Office, National Assembly for Wales, Cardiff Bay

Title: Welsh Assembly Government Submission to the Lyons Inquiry

Purpose

1. To note the Welsh Assembly Government's submission to the Lyons Inquiry

Recommendations

2. That the committee takes note of the Assembly Government's submission to the Lyons Inquiry.

Background

3. Members will recall that I had originally proposed to make a submission to the Lyons Inquiry last Autumn but just as I was about to issue the paper it was announced that the Inquiry's remit was to be extended. As a consequence I decided to delay the submission so that I could take account of the new remit in our response. This also takes account of other developments since then and the Assembly Government has now made its submission, which is attached. A copy of the submission will be placed on the Assembly Government's web site under the Local Government section.

4. Member will also recall that I undertook to provide a factual paper setting out the background to the revaluation and rebanding of council tax. I have attached this as Annex B to the submission to the Inquiry. I have also provided this separately to the Committee Secretariat as a stand-alone paper.

Compliance

5. There are no issues of propriety or regularity.

Action

6. The Committee is invited to note the contents of this paper.

Sue Essex AM

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Llywodraeth Cynulliad Cymru
Welsh Assembly Government

WELSH ASSEMBLY GOVERNMENT

SUBMISSION TO THE LYONS' INQUIRY INTO LOCAL GOVERNMENT

PART 1 – Original Remit: Local Government Funding

The Purpose of the Local Government Finance System and the Principle of Partnership

1. The Welsh Assembly Government considers that a fundamental principle for any review of the local government finance system should be that consideration must be given to the purpose of the system and not just the mechanism by which it is managed. The finance system is a means to an end and should support an overarching philosophy of the nature of local government.
2. In Wales, since the establishment of the National Assembly, the overarching philosophy has been based on the key principle of partnership, underpinned by the primary legislation, which established the National Assembly for Wales. The creation of the Partnership Council by the Government of Wales Act 1998 gave form and substance to the different nature of the relationship between central and local government in Wales which still is very different to that in England.
3. The relationship with local government in Wales is key for the Assembly Government in terms of delivering its vision for a better Wales and better, more joined up public services across the nation. There are some shared priorities but also local diversity. However, so far the emphasis in the finance system has been on distribution of resources and the balance of funding rather than on outcomes. Some progress has been made in this direction through, for example, Policy Agreements and the Grants Protocol that we have introduced in partnership with local government to try and ensure that hypothecated funding is kept under review. It would be disappointing if any implications for Wales arise from the Inquiry that might undermine this progress.
4. The role of the Assembly Government is not only to provide a strategic framework and ensure a level of consistency in service delivery but also promote local identity and freedoms. It is of primary importance that the local government finance system should underpin this.

Potential Legislative and Financial Implications for Wales

5. In our submission to the Office of the Deputy Prime Minister-led Balance of Local Authority Funding Review Steering Group (attached in full at ANNEX A) we noted that there are close legislative and financial links between England and Wales. We said –

“The Welsh Assembly Government has a clear interest in the Balance of Funding Review being undertaken by the Office of the Deputy Prime Minister (ODPM)-led Steering Group. This is because of the primary legislative basis for funding local government in Wales. For example, the Local Government Finance Act 1988 which contains the primary legislation on National Non-Domestic Rates (NDR) and Revenue Support Grant, and the Local Government Finance Act 1992 which contains the primary legislation on Council Tax, are both common to England and Wales. Therefore, any proposals for consideration of changes that might follow on from the review would have an impact for Wales. “

6. We will have to wait and see this might develop as a result of the new legislation proposed in the Government of Wales Bill now before Parliament, to provide the National Assembly for Wales with greater powers and flexibilities in this area.
7. Any recommendations, which your Inquiry might make in terms of changing the funding arrangements for local government in England, will impact on the rules set out in the ‘Statement of Funding Policy’. We would expect that any implications resulting from your inquiry should be made clear and transparent in your final report.
8. Your interim report acknowledges that under the devolution settlement there are differences between what happens in England and Wales. The Assembly Government will want to continue to build on that and it is important therefore, that the Welsh Assembly Government has the flexibility to consider different options in Wales and that we should not be required to follow the same policies as England.

Key Principles

9. In our submission to the ODPM-led Balance of Funding Review Steering Group we identified the following as key principles for the local government finance system which we believe to be important enough to reiterate here:

Fairness

The financing of local services needs to achieve fairness in that the payment of taxes should reflect the ability to pay and distribution of resources should reflect the relative need for local services. The ability of individual taxpayers should be considered in relation to the nature and availability of benefits and/or credits and the impact of above inflation increases on those with low and/or fixed incomes. Fairness should also be considered between taxpaying groups, for example between domestic and non-domestic taxpayers. In addition, fairness should be paramount in the

context of ensuring that communities living in different local authority areas should all have access to the highest standards of service delivery.

Efficiency

The costs of collecting local taxes need to be proportionate to the yield of those taxes. Very careful consideration should be given to any change in the form of local taxes in ways which add significantly to the overhead of collection costs. The presumption must be that any local tax should not impose additional administrative burdens on taxpayers or those organisations required to collect the tax, which are disproportionate to the yield.

Transparency

The public are increasingly demanding to see a clearer link between the taxes they pay and the service they receive; and may be frustrated by the complex arrangement of local taxes and grants which provides little link between the levels of tax and service. Any reforms should aim to simplify the system of local government finance not serve to further confuse or cloud. The blame culture between authorities and Government needs to be addressed. It should be clear which decisions result in particular levels of taxation or service.

Accountability

The authority that levies a tax should ideally be held to account for the value of service achieved through the tax revenue. A lack of transparency confuses accountability. Increased transparency would lead to increased accountability, as the public would have better information and be able to make more informed decisions. (Assembly Government Submission to the ODPM-led Balance of Funding Review Steering Group, p.3)

10. To support these principles we put forward the following additional evidence and experience from Wales as set out in paragraphs 11-17 below.

Simplicity, Transparency and Accountability

11. The current system of local government finance has developed over a considerable period of time. There is a tendency for changes to be made in an incremental ad hoc fashion. This has led to a system, which is complex, completely opaque to the majority of users of local authority services and has some now unwelcome aspects such as the gearing effect.

12. Our recent experience of revaluation has highlighted the potential for the complexity of the current system to be used as a smoke screen to confuse where true accountability for decisions on levels of local taxation and budgets rests. It is essential that the finance system is simple and transparent so that local taxpayers and businesses contributing to the costs of local authority expenditure can understand how and why their contribution is calculated and needed, how it is used and which tier of Government is responsible for those decisions.
13. As your interim report acknowledges, the public perception of local government funding is mixed but most are confused by its complexity. The Assembly Government believes that it would be unfortunate if further complexities were to be introduced into the local government finance system and no attempt made to address the current situation.

Fairness and Efficiency

14. In respect of local taxation the overarching principle should be fairness. This may be thought of at two levels in terms of local taxation. Firstly, fairness within taxpaying groups: all taxes whether property, income or collected on other bases should be capable of reflecting the ability of taxpayers to pay the tax. Secondly, there should be fairness between taxpaying groups, in terms of local taxation this may be thought of in terms of fairness between domestic and non-domestic taxpayers.
15. The costs of collecting local taxes must be proportionate to the yield of those taxes. The costs of collection must be thought of not only in terms of the cost of collection and enforcement of the tax but also in terms of any potential burden on taxpayers in terms of their input into identifying their potential liability for the tax.
16. In the context of efficiency, the Assembly Government would like to draw attention to "Making the Connections: Delivering Better Services for Wales - The Welsh Assembly Government vision for public services (October 2004)". Among other things, the Making the Connections agenda in Wales seeks to maximise efficiency gains through the scale economies of more effective collaboration and co-ordination as opposed to competition between service providers. Local government in Wales is in agreement with this agenda and it would be unfortunate if any implications for Wales arose from your inquiry that might not be compatible with this emphasis on co-operation.
17. It would also be unacceptable if any implications for Wales arose which would prohibit or hinder the attainment of local government's contribution to the target of £600 million value for money improvements across the whole of the public service in Wales by 2010 to benefit service delivery. It is therefore essential that any proposed changes to the local government finance system that might have potential implications for Wales consider this objective.

Property Tax

18. It is the view of the Assembly Government that a property based tax for both domestic and non-domestic tax payers should remain as one of the major sources of income for local government in Wales. Property based systems tend to be easy to understand and administer. There are inherent difficulties with property based taxes which relate to the period of time between revaluations and the use of property values as a proxy for the taxpayers ability to pay.
19. A factual presentation of the way the revaluation and rebanding was undertaken in Wales is attached at ANNEX B. Our experience of the recent council tax and business rates revaluations here indicate that the periods between revaluations, even in the case of business rates may be too long. This was reinforced by evidence from a visit to Denmark where the frequency of revaluations seemed key in maintaining the perceived fairness of the taxation system amongst taxpayers. Therefore, the experience of some other countries operating a property-based system of local taxation is that the period between revaluations is crucial. In Denmark there are bi-annual revaluations for both business and domestic properties. This significantly reduces the chances of steep rises between valuations, improves the transparency of the system, facilitates easier planning and budgeting for the tax payer, reduces the number of appeals against valuations, smoothes changes in the council tax base for the purposes of calculating the local government revenue settlement and means that issues relating to accountability for decisions relating to the level of local taxation are minimised. However, these benefits would need to be made clear to the tax payer to address the potential perception of increases in tax revenue being the main driver.
20. If a property tax is to remain part of the landscape of the local government finance system then it is imperative for domestic tax payers that the issue of fairness is considered. The Assembly Government remains of the view that property taxes for domestic tax payers should not be considered in isolation from the tax payers ability to pay. Our recent experience of council tax revaluation suggests that some form of amelioration of the tax liability is essential to address the tax payers ability to pay. We feel strongly that revaluation here was hampered by the inflexibility and complexity of the existing council tax benefit system, which is not devolved and is therefore not something we can change in Wales without the agreement and involvement of the UK Government.
21. We strongly believe that if council tax is to be retained then reform of the council tax benefit system is crucial. Our views on this matter were set out in our submission to the ODPM-led Balance of Funding Review Steering Group and are as follows:

“The Welsh Assembly Government believes that Council Tax has much to commend it in terms of the key principle of efficiency. Greater

fairness could be achieved by immediate reform of the Council Tax benefit system. Reforms which could be taken forward for immediate consideration include reviewing and revising both the income and the savings thresholds for eligibility and introducing some form of taper.

The Welsh Assembly Government is seriously concerned that responses to the consultation have highlighted the social stigma associated with claiming means tested benefits by some tax payers and believes this is a barrier to further improving the take up of Council Tax benefit. In light of this, as well as reform of the basis of eligibility, immediate reform of the processing of benefit claims should be introduced. These should include renaming the benefit as so to describe it differently, for example, a 'credit', and providing better and more widely available information and assistance to council tax payers. The current system needs to be extended to provide at least partial support, with tapers, for a wider range of income groups. The bureaucracy associated with the scheme needs to be reduced and replaced by innovative systems which help people understand and participate in the scheme. '(Welsh Assembly Government Submission to the ODPM-led Balance of Funding Review Steering Group, pp. 7-8)'. It is noted that you will deal with the question of Council Tax Benefit reform in your final report.

22. We are also of the view that both council tax discounts and exemptions and business rates exemptions and reliefs should be reviewed. There has not been a fundamental review since these systems were introduced and we believe that a review should therefore be considered to ensure that they are still relevant. Such a review would make a significant contribution to ensuring that fairness is maintained within both property tax systems. For our part, the Assembly Government is now evaluating the results of its consultation on options for rate relief for small businesses and in particular reviewing the current rural rate relief policy in Wales. ("Business Rate Relief in Wales – A Sustainable Future", December 2005).
23. Fairness is not only an issue of vertical equity within a tax paying group but also an issue of horizontal equity between tax paying groups. Therefore the relationship between the proportion of local taxation raised from local domestic tax payers and that raised from the business community should be considered. The background against which this should be assessed is the overall taxation burden for these tax paying groups, the services received from local government and the importance for local authorities of building a strong and healthy partnership and relationship not only with their citizens but with their local business community.
24. In terms of equity between tax paying groups there is an inconsistency in the basis of property valuation between domestic and non-domestic tax payers. The former being based on capital values and the latter being based on rental values. The rationale for this is the different make up of the two property sectors in the UK - the domestic market being dominated by owner-occupiers and the non-domestic sector by rented

accommodation. This difference, however, should not mean that tax payers in the two groups are disadvantaged in any way and therefore what is important is the fairness and consistency of the valuation process and the way in which reliefs and exemptions are determined in both. Tax payers should be able to easily understand how their properties are valued, how their bills are calculated and the appeals process should be as simple as possible.

Local Income Tax

25. It is important to understand that any recommendations relating to a supplementary local income tax in England will have implications for Wales through the 'Statement of Funding Policy'. The Assembly Government will await with interest the Inquiry's findings relating to the potential advantages and disadvantages of introducing such a form of local taxation.
26. Since making our submission to the ODPM-led Balance of Funding Review Steering Group we have observed that countries which operate a local income tax, such as Denmark, tend to have a culture of higher levels of taxation overall. This culture includes expectations amongst citizens that these higher levels of taxation will result in high levels of good quality local services. We have also noted that more services tend to be delivered at the local level in these countries. In Denmark there is a closer link between government of all levels and the citizen and this is manifested in higher turnouts at both local and national elections. Also, there is a clear understanding of which element of the income tax is local and which element is national and which services these taxes make a contribution towards. Any such system proposed by the Inquiry should explain how such an understanding will be achieved as part of its implementation.
27. It is therefore important that consideration of this form of local taxation take into account not only mechanics and practicalities but whether this form of taxation has any strategic fit with the system of government in this country, tax payers expectations and the relationship between local government and its citizens.
28. Also of interest, in respect of local taxation based on a local income tax, is that in the example we looked at in Denmark the tax is levied on the basis of a flat rate percentage payable by all tax payers (over an earnings threshold). This local element of income tax is therefore, proportional to as opposed to progressive with income (national income tax is progressive). This is not a feature with which UK tax payers are accustomed.

The Balance of Funding, structures and services

29. The expression 'the balance of funding' has now become synonymous with arguments relating to a localism perspective of local government

versus a centralist view. It is arguably now impossible to consider issues relating to the balance of funding without considering issues relating to the services delivered by local authorities and Government's role in determining the nature, extent and quality of those services.

30. As stated above the Assembly Government is developing a particular approach to working with local government and other parts of the public services in Wales and the local government finance system should support this not drive it. The system must be flexible enough to ensure that the focus on outcomes is not undermined by an over emphasis on inputs and formula funding at the expense of equity and differential funding based on need.
31. An example of this is the approach that the Assembly Government is taking to funding schools through the local government revenue settlement. We have chosen not to follow the approach being taken in England which is to move to a specific grant for core funding of schools characterised largely by a guaranteed amount per pupil. We consider that it is, in most cases, appropriate for local authorities to determine funding for schools and in doing so to take account of local circumstances.
32. This is consistent with the policy of securing high quality education in all schools in Wales. The 'Narrowing the Gap' studies carried out jointly with the Welsh Local Government Association have the objective of identifying good practice in schools which can be disseminated and adopted so as to narrow the gap in the performance of schools in Wales (primary and secondary). This together with other activity to improve school performance is intended to ensure that wherever they live in Wales, pupils have access to high quality school provision.
33. It is important the Inquiry notes that if any recommendations are made that might relate to changes in funding arrangements of the sort described in paragraph 31, there may well be implications for Wales because of the 'Statement of Funding Policy'. It should be remembered that decisions relating to the nature, size and services delivered by local authorities and their standards have been devolved to Wales. As explained earlier in the submission, it would be unacceptable, if because of the way in which funding for the Welsh block is calculated, the Assembly Government's flexibility to determine what is best for Wales is undermined, removed or limited in some way because of a change in the way things are done in England.

Police Funding

34. While it would not appear to be an explicit part of the Inquiry's remit, police authority funding is an integral part of the council tax system. Police authorities are council tax precepting authorities and it is therefore important that when considering local taxation matters, the police precept should not be forgotten. In your report you have highlighted the complexities of the local government funding arrangements and the

confusion this causes to the public. Nowhere is this more starkly demonstrated than in police funding in Wales which is through an amalgam of Home Office, Assembly Government and council tax payer. These are the same basic principles as the arrangements for funding police authorities in England. Where they differ is that despite the fact that responsibility for police is not devolved, council tax policy is the responsibility of the Assembly Government and as a consequence it has the power to restrict police authorities spending by capping budgets if these result in excessive council tax precepts. After reorganisation it would seem that the Home Office has no plans to change the arrangements for funding police authorities. It is the Assembly Government's view that the opportunity for change should come with the restructuring of police forces. If police restructuring were to be considered alongside work of the Inquiry there would be an opportunity for a significant reform of the funding of the police service. As mentioned earlier, it suffers from an astonishing complexity and lack of transparency but if the police service was centrally funded, and council tax made a greater contribution to other local services there would be a general improvement in transparency and accountability.

PART 2 – Extended Remit

35. It will largely fall to the Welsh Assembly Government to address the issues set out in part 2 of the remit in respect of Wales. The Assembly Government is responsible for policy on local government and on most aspects of local service delivery. In this context, the Assembly Government is awaiting the conclusions of the review into local service delivery which it commissioned last year from Sir Jeremy Beecham (terms of reference at Annex C). Sir Jeremy will be reporting in the summer and the Assembly Government is expecting to respond at an early stage. The review is looking at local service delivery across all the main sectors: its remit is wider than local government although the role of local authorities in service delivery will be central to its considerations.
36. It is worth emphasising that the review is focussed on how existing structures might work more effectively together, not re-drawing boundaries.
37. Although the Extended Remit only has limited application to Wales, we set out some points, which may be of interest. The strategic role of local government in Wales is increasingly expressed as organisations that create coherence at the local level across the public service, including collaboration and co-ordination. The Beecham Review is, among other things, looking at mechanisms such as local area agreements and public service boards as a way of joining up local service planning and delivery and the roles of the various stakeholders.
38. The Wales Programme for Improvement has a strong emphasis on self-assessment and increasingly on peer support from within the sector. So the role of local government as a regulator of its own performance is important going forward. In terms of services meeting national standards in

Wales, the Assembly Government, WLGA and Local Government Data Unit have just completed the new Performance Measurement Framework for Local Government in Wales. The work on this project has led to discussion on the possibility of appropriate national standards and minimum standards for Wales' local services. The Wales Audit Office has also raised the question of minimum standards in its current annual report on the Wales Programme for Improvement. These issues continue to be explored.

39. Other developments, which may be of interest, include the research into the role of the elected member jointly sponsored by the Assembly Government and WLGA. .
40. The Assembly Government's public service reform agenda is set out in 'Making the Connections'. At the heart is the vision of public services, which are increasingly joined-up and integrated, more efficient, more citizen-centred and driven by a commitment to social justice and equality. It stresses the need to develop diverse public services that can respond to the diversity of citizen's needs. The view has been taken that this is often more likely to be achieved through collaboration between services providers, with effective mechanisms for challenge and accountability, rather than through competition. There has been a long history of collaborative working between neighbouring local authorities in Wales. The emphasis now for local authorities and others is delivering a more collaborative approach at a sub-regional and regional level that yields real benefits on service delivery.
41. The public service in Wales has developed in an increasingly distinctive way since devolution. The Government of Wales Bill now going through Parliament promises a further strengthening of the devolution settlement through enhanced legislative powers. There have been clear and demonstrable improvements in local service delivery in recent years but there is a wide recognition that the current pace of change in service delivery arrangements will need to accelerate to respond to the pressures of affordability, demography and social change. It is too early to prefigure the conclusions of the Beecham review or the Assembly Government's likely response but there is no doubting the challenge.

Welsh Assembly Government
March 2006