A devolution revolution?

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Local Government analysis: UK devolution has been ratcheted up a notch by a transfer of responsibility for local taxes from central to regional authorities. Diana Stirbu, of London Metropolitan University, notes a peculiarly top-down approach to devolving democracy, wary of whether we are seeing a genuine and equitable empowerment of the UK's regions, or merely a shedding of responsibilities by Westminster.

Original news

'Devolution revolution' means new powers for local government, LNB News 07/10/2015 24

Plans announced by the Chancellor will enable local government to retain 100% of local taxes--including all £25bn of revenue from business rates--by the end of the current Parliament. The aim is to devolve power from Whitehall to local government in order to promote growth and prosperity.

What are the powers being devolved and what is the timeline?

Considered by many as a long overdue fix to the anachronism of local government funding, the move announced by the Chancellor devolves the powers to:

- raise and retain local taxes
- modify local business rates as local authorities see fit, and
- introduce premium rates to finance infrastructure projects, provided they have elected mayors and the approval of Local Economic Partnerships (LEPs)

The Chancellor's recent announcement signals a major shift in the way local government in England is financed, away from the current redistributive model to a model of more direct finance through local taxation. Under the current proposals, local government will retain 100% of local taxes--including the total revenue from business rates. The national uniform business rate will be abolished, leaving greater flexibility for local authorities to set the rates locally and create a more competitive climate for local business. Local public services will therefore be financed entirely through the locally collected taxes, while the core grant element in local government financing will be phased out by 2020. Additionally, the current proposals include incentives for local authorities (or combined authorities) to move towards an elected mayoral system, which will allow greater flexibility in introducing premium rates to help finance infrastructure projects. The role of LEPs is enhanced as well by making them essential decision-making partners in financing infrastructure projects. While central government will gradually devolve tax powers to local government by 2020, it still means that local authorities have to contribute to the fiscal consolidation of this Parliament.

The move is expected to incentivise local government to set, collect and use local taxes responsibly, and to empower local government to plan and deliver for local economic development. The timeline set is that the changes will be fully operational by 2020. Seen in the bigger context of policy decentralisation to England, there are likely to be a series of key stages in the process, including:

- the forthcoming November 2015 Spending Review, which will reveal several devolution deals for cities and counties in England, including transfer of powers and responsibilities, and
- the Devolution to Cities and Counties Bill, most likely to receive Royal Assent in December 2015

What has prompted these changes, what are they intended to achieve?

We can trace these changes all the way to the first generation devolution of 1997 (devolution to Scotland, Wales and Northern Ireland), and to its unintended consequences--namely the growing dissatisfaction over and concerns with the poor governance of England. Consecutive UK governments left the English question largely unanswered.

In 2012, the Heseltine Review 'No Stone Unturned: In Pursuit of Growth' set out a roadmap for addressing the governance deficit in England. The document proposed:

- merging various funding streams to provide a much greater local responsibility over local economic development
- devolving powers to the local level in some areas (ie transport, skills, housing)
- transfer of additional budgets
- enhanced powers over local taxes, and
- the creation of combined authorities

In the aftermath of the Scottish Independence referendum, while Scotland and Wales were securing enhanced powers, including elements of fiscal and tax devolution (including tax borrowing powers, as outlined in the 2012 Smith Commission), calls to address the governance deficit in England intensified.

Greater Manchester Combined Authority secured the first devolution deal in November 2014, followed by Sheffield City Region in December 2014. In line with the government's Northern Powerhouse rhetoric--supporting growth in North England as a counterbalance to London's economic dominance--the Devolution to Cities and Counties Bill 2015-16 was introduced in Parliament after the Conservatives' electoral success in May 2015. The Bill, currently in the House of Commons (second reading) represents the government's policy of devolving the powers and budgets of public bodies to local authorities and combined authorities.

The current announcement needs to be looked at in the broader context set out by the Devolution to Cities and Counties Bill 2015-16 and the existing devolution deals already approved, as well as in the context of first generation devolution in the UK. While the current proposals seek to address the governance deficit in England, and are driven largely by economic growth/survival, devolution to Scotland, Wales and Northern Ireland sought to address a political democratic deficit.

What opportunities will these changes bring to local government?

The Chancellor's proposal has been welcomed by many (for example by, the Local Government Association and the Chartered Institute for Public Finance and Accountancy) who highlight the obvious benefits of reducing the dependency of local government on central government funding and the implications this has on:

- simplifying the tax collection--local public spending cycle
- allowing greater flexibility in economic planning at local level by modifying business rates, or by introducing premium rates to finance infrastructure projects

Similarly, additional benefits include:

- giving local authorities responsibilities in planning local spending
- creating a more competitive environment to attract and retain local business, and
- allowing flexibility for local authorities to design multi-year spatial economic development programmes

An indirect benefit of current changes would be a possible re-vitalisation of local democracy, an increased scope for citizen-driven scrutiny and participation in economic planning.

Are there any foreseeable drawbacks to this change? Is there anything that could create unintended consequences?

There are concerns that the new funding system will leave local authorities vulnerable in the face of economic adversity (economic recession, further central government cuts etc). The removal of the redistributive element in local government funding, currently acting as a national safeguard, is--according to TUC General Secretary, Frances O' Grady--likely to widen regional inequalities, whereas the variable tax intake at local level could lead to rate distortion that impacts some local authorities negatively on growth. These arguments echo earlier theoretical concerns and empirical evidence of the existence of poverty traps, in which individuals, regions or countries can get stuck, inhibiting their prospects for growth. This concept was clearly developed in 'The Economics of Poverty Traps' by Costas Azariadis.

Additionally, there are fears that, as an unintended consequence, rather than providing a competitive and attractive environment for business, local authorities will introduce additional business rates to close funding gaps in public services.

The current proposals will also prove a tough leadership test for local authorities. One critical concern is what scrutiny arrangements will be set up in order to ensure that this significant devolution of power and responsibilities is matched by adequate scrutiny. The enhanced role of LEPs should be looked at with caution, as it can give way to patronage, lack of transparency and weaken democratic accountability around local economic development.

Looked at more broadly, there are questions whether this financing model is sustainable given that most of the devolved policy areas are areas that have suffered most of the cuts in recent years. There should be scepticism as to whether the new funding system can adequately match the budgetary requirement of the policy decentralisation (via devolution deals and the provisions of the Devolution to Cities and Counties Bill 2015-16). An unintended consequence is that this could effectively create a 'pay as you collect' public services system and areas with severe problems (homelessness, unemployment, ill heath etc) would be disproportionately affected.

What should lawyers advising in this area take note of? Is there anything that should be done now to prepare for the changes?

These new arrangements will create a lot of confusion in terms of local governance and accountability. This could potentially be nightmare or heaven for those in the legal profession (as the Welsh devolution has demonstrated). There will be a lot of variation in terms of governance arrangements across England. Of particular interest to lawyers is to oversee the legality and status of these arrangements.

The issue of scrutiny and accountability is critical. With such an enhanced role for the LEPs, clarification about their legal personality is essential. The Centre for Public Scrutiny has raised numerous questions with regards to some existing deficiencies in scrutiny, accountability arrangements and transparency in relation to LEPs. For more information on this concern, see 'Scrutiny and local economic partnerships'.

How do these changes fit in with current trends?

Notable is the lack of consultation involved in the Chancellor's decision to devolve tax powers to local government. The reform of local government financing represents a unique instance of major devolution of power, responsibility and taxation in the UK in the absence of political devolution, public deliberation and public endorsement. The same applies to the broader policy decentralisation programme across England. It is rather peculiar that 'localism' and devolution in England has such a strong dimension of central government imposition.

One of the lessons from devolution to Scotland, Wales and Northern Ireland so far has been that devolution has been highly dynamic, differentiated and, more recently, disputed. If devolution in England is to follows the same pattern, we can expect further flux in the governance and financing arrangements for England. Similarly, future calls for political devolution should not be discounted, given the impact devolution can have on shaping regional identities in the long run. Policy differentiation is likely to occur, given the level of asymmetries in the English devolution. Competitiveness among regions is likely to increase as with untested effects.

A future and possible reform of the Barnett Formula, as well as developments in Scotland and Wales (ie the current re-organisation of the local government there) should also be considered.

Interviewed by Julian Sayarer.

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