

# General Grants and Specific Grants in England: An Increase in Flexibility Since 1997

*Discussion Paper for the Copenhagen Workshop: 17-18 September 2009*

## Background to Funding Local Government

In the United Kingdom, central government has set up three separate systems to fund the three main blocks of local authority spending in England. These blocks are:

- spending on capital projects such as roads, school buildings or computers;
- revenue spending on council housing; and
- revenue expenditure, mainly on pay and other costs of running services other than council housing.

In relation to revenue spending on council housing, the costs are mainly met through rents charged, but central government also operates a revenue account subsidy system. This expenditure is not covered by this paper, which is focussed on grant support provided by central government. For all other elements of revenue spending support by central government, grant is provided through either general grants or specific grants.

The overall amount available for grants to local government is decided in the context of Spending Reviews where the Government decides how much it can afford to spend, reviews its expenditure priorities and sets targets for the improvements which are to be delivered from additional funding. Each Spending Review covers a three year period. In October 2007, the Government announced the results of its latest Spending Review (known as the Comprehensive Spending Review 2007 (CSR07)) which set the framework for central government grant support to local government for the years 2008-09, 2009-10 and 2010-11.

Central government revenue funding (of all kinds) and business rates together are known as Aggregate External Finance (AEF). The different types of revenue funding are as follows:

- **Formula Grant**, which is a general grant pot made up of Revenue Support Grant (RSG), redistributed business rates and principal formula Police Grant. It is distributed by formula through the annual Local Government Finance Settlement and there are no restrictions on what local government can spend it on.

- **Specific revenue grants.** Some of these are ring-fenced grants which control council spending. These grants usually fund particular services or initiatives that are a national priority. For example, funding for schools is paid through the Dedicated Schools Grant reflecting the priority the UK Government places on education. Other specific grants are non-ringfenced which means that there are no restrictions on what councils can spend the money on.
- From 2008-09 local authorities were also provided with a new non-ringfenced general grant pot known as the **Area Based Grant (ABG)**. ABG is made up of grant streams that were previously provided to local authorities as specific revenue grants. ABG enables local authorities, working with their partners, to decide where best to invest their resources in the most effective and efficient routes to delivering local priorities.

A list showing examples of the main grants of each type, in the three years of the Spending Review period covered by CSR07 is shown below.

£ million	2008-09	2009-10	2010-11
<b><u>FORMULA GRANT</u></b>			
Revenue Support Grant*	2,854	4,501	24,622
Business Rates	20,500	19,500	
Police Grant**	4,136	4,253	4,374
<b>Total</b>	<b>27,490</b>	<b>28,254</b>	<b>28,996</b>
<b><u>AREA BASED GRANT</u></b>	<b>3,059</b>	<b>3,225</b>	<b>4,764</b>
<b><u>EXAMPLE OF NON-RINGFENCED SPECIFIC GRANT</u></b>			
Concessionary Fares	212	217	223
<b><u>EXAMPLE OF RINGFENCED SPECIFIC GRANT</u></b>			
Sure Start, Early Years and Childcare	1,281	1,392	1,543

\* Excludes Specified Bodies Top-Slice

\*\* Includes Metropolitan Police special payment

## Why does central government provide local authorities funding on a ring-fenced basis?

### Historical Background

In 1997, when the current administration came to power, **non-schools** ring-fenced grant accounted for **4.6%** of all central government funding to local authorities. The amount of ring-fenced provision in the main increased steadily up to 2007-08.

Funding for local government is 'ring-fenced' if it places a restriction on spending decisions of local authorities. This can typically take place through conditions which are attached to grant determinations on how the funding is to be used. But a grant can also be ring-fenced in other ways, such as through the way the fund is administered (challenge fund or project-specific). Funding can also be ring-fenced more informally through "soft controls" such as guidance or Ministerial/departmental pressure to use funding for a specific purpose.

By 2001, non schools ring-fencing had increased to **8.4%** before rising further to **13.3%** in 2003. Ring-fencing then started to decrease over the next two years before increasing again to a level of **14.0%** in 2007-08. Since then the UK Government has looked for opportunities to reduce the level of ring-fencing, and currently the level has decreased to **7.3%**.

The growth in ring-fencing was accompanied by a growth in the total of Government grant support to councils. Since taking office in 1997, the UK Government have provided significant investment in services for local authorities in England. In their first 10 years the current administration increased total central government grant to local authorities in England by 39% in real terms (up to 2007-08) on a like for like basis, after taking account of changes of finance or function affecting councils over that period (such as the shift in responsibility for sixth form education from local authorities to the Learning and Skills Council in 2002-03).

The following table sets out the growth in Government grant and the changes to ring-fenced funding over that period.

*Increases in Aggregate External Finance and Non-Schools Ring-fencing*

	1998-99	1999-00	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
Cash Increase (£billion)	1.0	2.1	2.2	3.0	3.3	3.8	3.7	3.6	2.7	3.1
Ring-fencing	4.6%	5.5%	6.9%	8.4%	13.1%	13.3%	11.1%	9.4%	10.5%	14.0%

*Ring-fencing of Funding for Schools*

Since 1997 it has been a priority of the UK Government to ensure that education funding intended for schools reaches its intended target. For this reason the majority of the ring-fenced revenue grants that are provided for funding schools are provided on a ring-fenced basis.

The largest grant that is provided to schools is the Dedicated Schools Grant (DSG). Introduced in 2006-07, DSG is the main grant used by local authorities to fund their schools budget. The current level of DSG is £29.8 billion in 2009-10. Additional to DSG local authorities also receive a number of other schools specific revenue grants on a ring-fenced basis.

For 2007-08, the non-schools figure for ring-fenced funding is **14%**. If schools funding is included, then this figure increases to **53.9%**.

*Main reasons for using ring-fencing*

The Government considers that ring-fencing was, and still remains, a valuable tool for bringing about change. As such there are some circumstances where the Government believes that a ring-fenced grant would be better than providing funding on a non-ring-fenced basis. These reasons for a ring-fenced grant may include:

- Existing policy commitments for a specific grant for a particular purpose
- Where UK Government Ministers collectively consider that there is a recognised need to designate specified resources to specific purposes
- Bid-based grants or grants for pilot work

One of the areas where the Government believes that it is right to ring-fence provision is the Sure Start, Early Years and Childcare grant where it relates to a national priority. Sure Start funding has always been ring-fenced.

As mentioned above the Government has also always made clear that education is their number one priority. Ring-fencing schools funding ensures it is devolved to the appropriate level, which is the school.

However, by ring-fencing individual pots of funding to local government, central government is prescribing how councils should use 'inputs' (money), rather than what outcomes they should achieve. The next section looks in detail at what steps have been taken to provide funding to local authorities on a more flexible basis.

### **What is the rationale for providing funding to local authorities on a non-ringfenced basis?**

In 2007, a Government report produced by Sir Michael Lyons concluded that ring-fencing of grants, particularly the new Dedicated Schools Grant, taken alongside the strong expectations from central government about the use of resources, and local government's limited capacity to raise additional resources led overall to a regime which gave local authorities limited scope to manage their services in the most efficient way possible. Sir Michael Lyons called on Government to set clear targets and timetable for a further reduction in both formal and in-formal ring-fencing.

The Government believes that ring-fencing can be:

- inefficient (because the council is not free to deploy its resources across the piece, to achieve maximum value for money);
- less likely to deliver quality services tailored to the needs of the area – the weight of recent research suggests that users have increased expectations of personalised services and are increasingly diverse and that, against that backdrop, central government is increasingly not well-placed to make detailed decisions about the amount of funding local government should spend on individual services;
- against the Government's general devolutionary approach, in which it signs councils up to a restricted number of priority targets and then allows them to work out how best to deploy resources to deliver those targets.

## How has the Government reduced ring-fencing?

Following the 2001 review of ring-fenced funding the UK Government started to remove the ring-fences on a number of long standing specific grants. Some of these grants were also moved into non-ringfenced general grant.

The Chancellor of the Exchequer then announced in Budget 2007 that the Government agreed with Sir Michael Lyons that more needed to be done by central and local government alike to enhance the ability of councils to deliver for their local communities. Budget 2007 therefore committed the UK Government to setting out a clear target to reduce specific grants and ring fenced funding and examining the scope to minimise complex and time-consuming reporting and data provision as part of the CSR07.

As a direct result of this commitment, the major achievements in reducing the level of ring-fencing and increasing the amount of funding provided by general grant pots came during the outcome of CSR07.

By shifting more money into RSG, and as much as possible of the remaining revenue funding into ABG, thus reducing the number of grant funding streams, levels of bureaucracy, and the level of ring-fencing, the Government was able to provide greater flexibility for local authorities, by specifically:

- Moving at least £5.7 billion into RSG or ABG by 2010-11; and
- Reducing the number of specific revenue grants from 83 in 2007-08 to 46 by the end of 2010-11.

The following table provides a summary of the position on reducing the level of ring-fencing and the number of specific revenue grants over the CSR07 period:

	2007-08	2008-09	2009-10	2010-11
<b><u>Specific Revenue Grants</u></b>				
Number of Specific Revenue Grants	83	47	47	46
Number of Specific Revenue Grants Announced on 3 Year Basis	-	25	27	26
Number of Funding Streams in Area Based Grant	-	43	43	44
<b><u>Non-Schools Ring-fencing</u></b>				
Level of Non-Schools Ring-fencing	14.0%	11.2%	7.3%	8.0%
Value of Non-Schools Ring-fencing (£ billion)	5.0	4.1	2.8	3.2
<b><u>Ring-fencing (including Schools)</u></b>				
Level of Non-Schools Ring-fencing	53.9%	52.3%	50.2%	51.2%
Value of Non-Schools Ring-fencing (£ billion)	36.0	35.9	35.9	38.2

## **How can the Government be sure that non-ringfenced funding provided is being used to deliver statutory services?**

All local authorities have to operate within a legal framework which is set out by central government. However, it is important to note that local authorities are independent organisations from central government and as such they have their own audit arrangements.

Local authorities are therefore responsible for their own finances. This responsibility includes:

- Setting their own budgets
- Raising income locally through council tax, fees and charges
- Borrowing money within prudential limits
- Maintaining and investing reserves

Each council's Chief Financial Officer has a statutory responsibility to report on the council's revenue budget and reserves and to certify annual accounts.

### **Local Authority Audit**

Local authorities are subject to an annual audit by auditors appointed by the Audit Commission. The Audit Commission is an independent body that is responsible for ensuring that public money is spent economically, efficiently and effectively, to achieve high quality local services for the public. The Audit Commission therefore use the information provided by local authorities to produce an overall judgement on a councils' use of resources. Each council is scored on five themes:

- *Financial Reporting* – covering how the council prepares and publishes its accounts
- *Financial Management* – how well the council plans and manages its finances
- *Financial Standing* – how well the council safeguards its financial position
- *Internal Control* – how the council ensures money is spent properly and that significant business risks are managed
- *Value for Money* – whether the council achieves good value for the community from the money it spends

### Performance Framework

The 2006 White Paper, *Strong and Prosperous Communities*, promised a new era of freedom for local government, with greater flexibility to set priorities and greater discretion over how to meet them.

This meant among other things that up to estimated 1,200 indicators assessing performance would be reduced to around 200. Currently, there are 189 performance indicators in the National Indicator Set.

This set of 189 indicators represents what the Government believes are the national priorities for local government, working alone or in partnership. They provide a framework for local authorities to look less to central government for legitimacy and direction, and more to the communities that they serve.

Local authorities are therefore responsible for working towards delivering against this National Indicator Set. This new performance framework provides a robust assessment regime to scrutinise progress against priorities, as well as how effectively local authorities use their resources. It also provides a clear ladder of intervention and support to address cases of poor performance.

The provision of funding of a non-ringfenced basis simply maximises local flexibility over the use of resources to deliver priorities effectively and efficiently.