CCN
COUNTY COUNCILS NETWORK

Press Release

PwC - *Independent review of local government spending need and funding*

<u>Technical Frequently Asked Questions</u>

Q) What's different about this study?

The relative impact of reductions to local government funding, and how to assess councils spending requirements, has been subject to extensive analysis. This includes recent reports by the Centre for Cities, the New Policy Institute and Cambridge University.

Using official data published by the Ministry of Housing, Communities & Local Government (MHCLG), these studies focus on the extent to which local government's Core Spending Power (CSP) and service expenditure have reduced since 2010. **However, it is CCN's view that this type of analysis has some key limitations that underestimate the financial challenges facing county authorities and their future spending needs.**

A comparison of trends in spending and/or reductions in CSP across different local authorities fails to consider the relative starting position of councils in levels of government funding and the impact this has on the level of service provided by different types of councils. It also fails to capture key drivers of future demand and cost pressures – such as demographics, inflation, and the living wage - which are not readily measurable based simply on analysis of historic expenditure.

PwC's analysis has drawn on the methodology adopted by the LGA in their funding gap analysis, however, there are several key differences within the modelling and assumptions (see below).

Q) Why does the study cover the period 2015 to 2025?

For the analysis PwC needed to arrive at a 'baseline year' to begin their analysis. This represents the year when actual aggregate spending across all local authorities is **assumed** for the *purposes of the modelling* to best meet aggregate 'demand/need' for the service.

Three different options could have been selected – 2009/10 (pre-austerity); 2015/16 (beginning of the current spending review period); or 2017/18 (the most recent data).

PwC use 2015/16 as it represents the final year before the previous Spending Review period – since then, local government has started to face new challenges and further pressure on its resources.

In the baseline year, PwC **assume** for the purposes of the modelling actual spending provides the best starting point from which to estimate the resources required to meet the demand for all services provided by local government – i.e. it most closely reflects the underlying spending need for local government as a whole, BUT NOT, at tier level.

Q) What is 'spending need'?

Spending need is an evidence-based estimate of the amount of resources local government, and specific tiers of councils, required to meet its demand and costs for services.

Spending need is the product of the number of recipients for a given service (volume/demand) multiplied by the unit cost of providing the service. In PwC's analysis they use 17 different *service* *specific* cost drivers (volume/demand indicators) across 10 different service areas, in addition to generic cost drivers, such as inflation, the living wage, pension obligations and the apprenticeship levy.

Q) What does PwC's estimate of spending need on a more 'consistent level of service' mean?

A key part of component of the study is to estimate unit costs to arrive at spending need. There is no nationally available data on unit costs, so the study uses revenue outturn statistics to estimate unit costs for each of the 17 different cost drivers.

If *actual spending* by each local authority type was used to arrive at these unit costs in the baseline year, it would incorporate differences in the level and quality of service provision across different areas. This would 'bake in' higher expenditure and political decisions over higher or lower service quality, rather than provide an estimate on what funding councils require to deliver a more consistent level of service.

PwC estimates spending need if all local authority tiers were to provide a more consistent level of service by adjusting unit costs at service and council level. Spending need based on a more consistent level of service recognises that while councils face different input costs arising from higher or lower geographical costs, historic funding levels may have allowed councils to deliver a higher quality or level of service for the recipient population beyond their actual real spending need.

Spending need based on a more consistent level of service does not mean that every council should be delivering the same services, nor that every council faces the same demands and needs. **Equally it does not mean this is the standard of service that every council should aim to provide**. <u>But it does allow a fairer approach to estimating spending need to ascertain the relative funding challenges facing different types of councils</u>.

PwC's approach involves an evidence-based calculation[1] to adjust unit costs for each tier of council for each cost-driver. **This does not mean PwC have presumed every council has the same costs and demands and it still recognises**:

- Different input costs (for labour and property), which are reflected in the Area Cost Adjustment (ACA) factors.

- Unit costs are also adjusted overtime to account for 'generic cost drivers', such as inflation, the living wage, pension obligations and the apprenticeship levy.

In addition to this, PwC use of 17 different *specific* cost drivers across 10 different service areas that ensures that the measurement of spending need recognises higher or lower demand for services for different types of councils, depending on underlying socio-economic characteristics such as demography, levels of deprivation and geography.

Q) How have PwC estimated council funding for the period?

For the period 2015-20 PwC use actual funding obtained from national data on Core Spending Power. This includes any additional funding announced in year and council tax rises. PwC exclude retained business rates growth.[2] For the period 2020-25 PwC use the funding model developed by Pixel Financial Management. This assumes funding levels are 'cash flat' from 2020/21 onwards, including key funding streams such as the Improved Better Care Fund and New Homes Bonus. We do not include the continuation of one-off funding, such as the Adult social care or roads fundingIt is important to note that

[1] See PwC full technical report pages 9-10
[2] See PwC full technical report pages 12-13

not only is a 2.99% rise above the statutory referendum limit, when the rate increase of 2.99% is combined with the council tax *base* growth, the *income* from council tax effectively rises annually to 4.98%. This assumption is significantly higher than Office for Budget Responsibility (OBR) forecasts of an average of 2.88%.

Q) What is a 'notional' funding surplus or gap?

This is an **estimate**, based on the analysis, of the difference between what the council types *actual* spending need is compared to the actual funding for the period 2015-20 or anticipated funding for the period 2020-25.

If a council type has a funding surplus, this means their actual funding exceeded PwC's estimates of spending need based on a more consistent level of service. This would indicate these councils have been providing a higher quality or level of service above their spending requirements if councils are expected to provide a more consistent level of service.

If a council type has a funding gap, this indicates that their spending needs to provide a more consistent level of service *exceeds* their actual funding for the period. In the baseline year (2015/16) if a council has a funding gap, this indicates these councils have historic spending needs that have not been recognised in funding allocations or expenditure. These councils have 'unmet needs' and/or have been providing a lower level or quality of service.

Q) What is the difference between the PwC's report and that the LGA's funding gap analysis?

The principles of the two pieces of analysis are similar, however, there are several different parts to the model and assumptions used to arrive at our respective funding gaps. PwC's model not only undertakes the analysis at tier-specific level (which is based on assumed adjusted local authority unit costs), it also uses a greater number of cost drivers in the spending need analysis. The LGA model also has a different baseline year of 2017/18 in comparison to our starting point of 2015/16 and includes a 'pre-existing adult social care provider market pressure'.

It is also important to note that there are key differences in our assumptions on the funding side. The LGA assumes growth in retained business rates after 2020/21 on the basis of OBR forecasts and the PwC analysis assumes no growth in that period. Moreover, when considering the post 2020/21 funding gaps, the LGA's assumptions on council tax are based on the OBR average forecast of an annual 2.88% growth in income compared to our higher estimates of 4.98%.

The table sets out the results for the period of the PwC analysis. After accounting for council tax rises post 2020/21, PwC's overall estimate of the cumulative funding gap is bigger than that estimated by the LGA. However, given the differences in the models, the two sets of results are broadly in trend over the period and demonstrate the severe financial challenges facing local government.

Table 8: Comparison of funding gap estimates (post Council Tax increase): PwC and LGA (£mn, 2015/16 to 2024/25)

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25	Cumulative gap
LGA analysis	n/a	n/a	1,449	2,662	3,854	4,765	5,345	6,054	6,883	7,814	38,826
PwC analysis	0	1,930	2,569	3,868	4,839	5,213	5,572	6,004	6,457	6,919	43,372

Source: PwC analysis and LGA funding gap analysis