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Grasping the nettle: the central–local constraints on local government funding in England

Kevin Muldoon-Smith [a] and Mark Sandford [b]

ABSTRACT
In England, the traditional method of central government redistribution and equalization between locations has been replaced with a greater emphasis on self-sufficiency and entrepreneurism. English local government now faces existential funding questions – a situation that is repeated around the world as the public sector manages the fallout from the Covid-19 pandemic. Financialization has figured large in the study of entrepreneurial behaviour. However, in England, legal and procedural constraints have driven authorities to seek revenue funding from other sources, principally seeking additional property-related revenues. In response, this article presents a novel typology of local government funding sources and offers an original analysis of their implications for local authorities' role. The empirical findings show that the buoyancy and quantum of many funding sources are constrained by prior evolution of location and central–local relations: they are not automatic routes to financialization. Conceptually, these findings reveal that methods of financialization, and the local government funding system within which they typically sit, are as likely to be constrained by the evolution and techniques of governance as they are accelerated by it. International debates around financialization, and wider concerns of how locations develop, would benefit from this account of the often-hidden nature and agency of local government funding systems.

KEYWORDS
financialization; central–local; tax; property; uneven development; local government funding

HISTORY Received 23 June 2020; in revised form 8 April 2021

INTRODUCTION

Local government studies is the Cinderella of political and territorial science; and local government funding is the Cinderella of local government studies. At the time of writing, there is a developing crisis in local government funding across the world. This is sharpened by the impact of the Covid-19 pandemic on local income and is largely passing beneath the scholarly radar. The funding context of local authorities has often been addressed, in recent years, in the context of the perceived or potential impacts of 'financialization' on local government decision-making and power relations. This article offers a different perspective, suggesting that the opportunities for the influence of financialization on local government funding are heavily contingent on

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structures of governance in any given state. The finance in financialization – typically used to capitalize the upfront costs of infrastructure and buildings – is now the subject of a prominent debate (Pike et al., 2019a). However, the funding of local services, overwhelmingly the greatest concern for local authority solvency in terms of quantum of money and impact on local areas, has received less attention.

This article examines the financial pressures on local government funding in England during the 2010s, in their structural context. The core research question addressed is: To what extent do existing and proposed sources of local government funding in England address (1) the 'solvency challenge' faced by local government and (2) allow for an increase in financialization?

The authors examine this question for several reasons. First, sharp reductions in central government grant funding in England since 2010 (Gray & Barford, 2018) have driven significant concerns over the current and future solvency of English local authorities. Second, these concerns have, in turn, generated advocacy and proposals for increased fiscal decentralization to those authorities, embedded in a long-term disquiet at British centralism. Third, this latter debate so far has been stunted. UK governments have avoided grasping the nettle of considering the structure of local government funding since the replacement of the Community Charge by council tax in the early 1990s, preferring no or incremental change. In particular, proposals for new sources of funding often fail to acknowledge the distinction between capital and revenue financing; and seek to link local funding to local economic health without taking account of national imperatives toward redistribution, nor the reality of place. Put simply, some places can access and use certain sources of revenue more easily than others can. This article seeks to explore these differences and their implications for the reconstruction of local government funding that is likely to be required in England following the coronavirus pandemic in the period 2020–21. In doing so, it offers a new interpretation of territorial development from the perspective of local government funding, but also offers a bridge between local government funding and financialization which is often obscured.

This debate links into questions around central–local government relations and considerations of how the local government system operates in practice in a given locality. The former arise from the extensive central control over local taxation and funding management in England, which frames the options available to local authorities facing threats to their solvency. The latter considerations take account of the influence of the local economy on the availability of funding sources in a given locality: the sums available via local revenue via local revenue-raising powers are path dependent and place specific.

The central arguments and findings in the article also have potentially broader application, as England has long been seen as a laboratory for new forms and techniques of policy and governance (Pike et al, 2019b). All countries have unique central–local contexts and administrative procedures for funding their public services. However, the initial findings and wider discussion in this article provide a factual source for policymakers (and those that provide scrutiny) to evaluate and propose new initiatives for funding local government. For professionals struggling with the day-to-day management of local government funding, the article provides an overview of the constraints on rewiring the funding of statutory obligations. This will serve to assist international efforts to stabilize and strengthen systems of local government funding, which can fall prey to abstract demands for 'more powers'. Examining the nature, agency and technologies of local government funding systems – and the path dependencies they can unwittingly introduce – sheds a new light on international academic debates surrounding (1) financialization; (2) how territories are funded, remain solvent and develop over time; and (3) how this interfaces with wider geographies of development and equalization between territories.

The remainder of the paper is structured as follows. The next section reviews the relevant literature on the influences on local government responses to solvency challenges, including financialization, and potential impacts on capital expenditure decisions. It then explains the local government funding system operating in England, arguing that several features of that system act as bulwarks against extensive financialization. Third, it collates a number of proposals for new sources of revenue that have emerged in think-tank and scholarly debate in England in the 2010s. It provides a typology of these sources of revenue and addresses the research question set out above with regard each category. We argue that, in the English context, most sources of funding – both current and novel – provide both peripheral and geographically uneven quantities of revenue, and the link to local economic development is fuzzy.

This latter point highlights that sources of revenue for local authorities – in any state – must be judiciously chosen, with an eye to the effects of economic variation and to local authority functions. However, we also highlight the relatively peripheral role likely to be assumed by financialization within English local government. Its effects will be felt principally through influence on decision-making around infrastructure, in a minority of premium locations. These effects will be muted where substantial profits are not available to investors. If English local government's current statutory duties and legal framework remain in place, an expanded menu of revenue sources for local government *could* point towards an entrepreneurial funding future for some localities, where some local governments seek to shape locations strategically in order to subsequently create income streams to pay for local services: but this is not likely to be a majority experience.

PEGGED DOWN: THE MAZE OF LOCAL GOVERNMENT FINANCE

Local authorities face restrictions on their financial freedom that do not apply to nation-states. They cover comparatively small populations and geographical areas; they exercise specified legal duties; and they face legal controls over revenue raising and management. These contexts frame the policy choices they are able to make.

The influence of those contexts has been investigated by multiple academic literatures. The literature on fiscal federalism and multilevel governance has explored the situating of local authorities in terms of national equity and citizenship concerns, ranging from public choice perspectives (Tiebout, 1956) to progressive perspectives focusing on citizens' 'ability to pay' and redistribution (Musgrave, 1959). A state's position on these matters can significantly influence how exposed local authorities are to uneven economic performance. It may also govern the degree to which central governments seek to intervene in, influence and induce local authority behaviour. This may occur via contractual relationships between governments within a state, either transactional (with defined outcomes) or relational (committing to cooperation) (Charbit, 2020). Local governments may face financial or legal inducements to outsource functions to private providers (Ferry & Eckersley, 2020; Lowndes & Gardner, 2016), with the aim of saving money, and this too may influence strategic priorities.

In some states, local authorities have taken a path of 'urban entrepreneurialism' – emphasizing economic policy as an equal concern to public service delivery. This can lead to the privileging of market values, promoting 'collaborative efforts with market actors and engaging global markets and agendas, and the use of state powers to promote and protect municipal investments' (Deas et al., 2020; Fuller, 2018). Local authorities also face differing interpretations of the requirements of public accountability. These imply that financial decision-making is informed by the need for the local authority (the 'agent') to give account to the electorate (the 'principal') for its actions. This fundamental requirement can occur through a variety of mechanisms: transparency, external audit and regulation of financial management (Ferry et al., 2015; Hood, 2010; Murphy et al., 2019). In the English context, this was heightened by the abolition of local government performance management frameworks in 2010 (Ferry & Eckersley, 2020), which removed an alternative institutional logic to that of budgetary management from councils' decision-making processes.

The influence of legal and institutional frameworks has heightened significance during periods of 'austerity', as experienced by English local authorities since 2010. Innovative institutional responses (Kim & Warner, 2020; Lowndes & McCaughie, 2013) cannot avoid being shaped by the quantity – and as importantly, the source – of funding available to the local state. Local authorities unable to influence legal frameworks would naturally turn their attention to mechanisms of local government funding (non-statutory in England). This ostensibly technical matter 'plays an outsized, but often overlooked, role in the urban process' (Tapp & Kay, 2019).

The implications of this insight for public services and local authority roles have been largely absent from scholarly debate. For instance, an authority receiving much of its income from tied grants will tend to prioritize the policy areas associated with those grants. One receiving much of its income from volatile local taxes may be conservative in its service provision. Another may have much freer access to capital than to revenue funding, and may prioritize infrastructure-based policies and recycle revenue (e.g., transport fares, property rents) to service provision. Another might derive substantial revenue from income or corporation taxes, and thus pursue a policy aim of increasing its tax base by making the locality attractive for companies and individuals seeking to relocate.

Financialization

In a context of fiscal tightening, narratives of devolution and decentralization have prefigured notions of local responsibility for service provision. There has been far less consideration of how funding frameworks, instruments and revenue sources frame the local responsibility for service provision. Studies of this question focus most frequently on the conceptual framework of 'financialization': the increasing dominance of financial actors, markets, practices, measurements and narratives at various scales, resulting in a structural transformation of economies, firms, states and households (Aalbers, 2016). Fields (2018, p. 119) recently defined financialization as 'an idea that has taken hold as a means of understanding the distinctive role of finance in contemporary capitalism, and its influence on space, the economy, governance and everyday life'.

This framework suggests that local governments' policy priorities, individual investment or asset-related decisions, and thus the delivery of public service commitments, are increasingly determined by the financial priorities of private sector funding sources and intermediaries. Alternatively, local authorities may seek to use financial vehicles – joint ventures, special purpose vehicles – to seek additional revenue themselves. Inspired by the work of Weber (2010) and Peck and Whiteside (2016), Lin et al. (2019, p. 436) indicate that some 'American and European local governments have become reliant upon financial instruments to repackage and reschedule current fiscal problems temporarily by selling off city futures.' Novel financial incentives can also influence approaches to service provision: several authors have highlighted the influence of funders in the delivery of Social Impact Bonds (SIBs) during the 2010s (Fraser et al., 2018; Edmiston & Nichols, 2018; Kim & Warner, 2020). However, Lin et al. (2019) concede that it remains 'controversial and vague how the transformative process of financialisation has played out in different geopolitical and economic contexts' (p. 347). This is echoed by Peck and Whiteside (2016, p. 238) who caution that financialization is 'pervasive in reach yet uneven in effect.'

In summary, the concept of financialization has connected into debates of decentralized government provision (Rodríguez-Pose & Gill, 2003) and 'roll back' and 'roll out' neo-liberalism (Peck, 2010; Peck & Tickell, 2002). Moreover, in England, it has provided new insight into how local places and government adapt to measures of austerity introduced since 2010 (Christophers, 2018; Gray & Barford, 2018; MacKinnon, 2015) and some of the controversies associated with these efforts, such as the use of Lender Option Borrower Option (LOBO) loans (Mertens et al., 2019). However, we suggest that financialization has played a peripheral role to date in that story. Our findings suggest that such simplifying market conditions rarely exist: they are typically found only in major premium locations that are bounded within and undergirded by assistive rental conditions such as Central London, New York or Frankfurt and secondary cities such as Chicago and Manchester. Such locations are bountiful but form a narrow striation in the overall territorial expanse. Bound up within this simplification is the often-uncritical contention that territories are establishing and exploiting regulations and policy instruments in order to smooth the flow of investment into the built environments of cities.

The more common reality is locations with inferior income conditions, bypassed by financial flows (Muldoon-Smith & Greenhalgh, 2015). Such locations are left reliant on more local and parochial methods and sources of income. It is therefore important to have a critical perspective of the situation in the 'everywhere else' to understand how economically uneven territories have developed – and will continue to evolve into the future. This perspective enriches debates around financialization. Local government funding mechanisms, particularly the receipts of income via tax, help ground global capital markets in place or bypass others because the income does not exist. This suggests a counterweight to 'roll out' neoliberalism (Peck & Tickell, 2002) – where increased privatization and assistive regulation catalyses global market interaction.

We argue that tensions within central–local relationships are more pertinent to the funding behaviour of local authorities. Central funding decisions have driven local decisions to explore unconventional financial initiatives; to sweat existing income sources; and proposals for many (often inchoate) forms of 'fiscal devolution'. This situation is then further distilled through the uneven reality of local place.

In any state, such decisions are influenced by the central–local government relationship. Some local authorities experience a high degree of central control, whether through limited local functions, supervisory powers, limited local sources of revenue, conditional grants, or bureaucratic audit. In other states, greater discretion may be permitted in some or all local responsibilities; taxation powers may be devolved to a greater or lesser extent; or the oversight of local decision-making may be more or less significant in practice. This balance may change over time, in response to short-term political concerns or, more rarely, more strategic constitutional concerns. Nevertheless, all real-world funding systems carry within them a perspective on the balance between equity and fiscal autonomy; the nature of accountability; and the balance between the importance of service delivery and economic management.

This suggests that complex interactions between methods of funding and structures of governance over time inform the development of territory and space. They are co-evolutionary and path dependent, and will not easily be overshadowed by a single new phenomenon such as financialization. All countries that fund public services through grant and tax exhibit this complex interaction. Just as infrastructure underpins the spaces and places of public life, local government funding helps define how these locations are (un)developed and supported. For example, in England, every school built, space maintained or public health emergency mitigated emerges via a public funding mechanism, a source of income and a decision to spend (or not). This fiscal 'decision space' delivers an alternative way of understanding how territories develop and how societies have access to and utilize spaces within these locations. Central–local relations, financial management and sources of revenue – bounded within central–local tensions and the relative performance of funding mechanisms – play a central, but often occluded, role in regulating territorial investment and structuring urban change. Territories are in part defined by the imprint of the path dependent funding institutions that produce them.

HOW ENGLISH LOCAL GOVERNMENT FUNDING STRUCTURES WORK

The UK government is responsible for local government finance policy in England. Allocations of central transfer grants, and some redistribution of business rates revenue, are fixed through an annual funding round (the 'local government finance settlement'), determined between November and February before the beginning of the UK financial year in April. The distribution of these funds is entirely in the hands of the UK government. These are supplemented by a small group of conditional grants. The remainder of local authority income comes principally from property taxes: council tax (domestic property) and business rates (non-domestic property), together with more minor contributions from local fees and charges and investment income.

The sustainability of funding is an ongoing concern for local government practice in England. This follows a sustained reduction in central transfer grants to English local authorities from 2010 onwards (local authorities in Scotland, Wales and Northern Ireland are the responsibility of their respective devolved institution and are thus omitted from this analysis). Analysis from the UK National Audit Office (NAO) suggests a 35% reduction between 2010 and 2014 (NAO, 2014), and the Institute for Fiscal Studies (IFS) suggests a 36% reduction between 2009 and 2015 (Innes & Tetlow, 2015). Local authorities have been unable to replace these transfer grants from local sources at this type of scale (Gray & Barford, 2018). In July 2019, the Local Government Association (LGA) indicated that one in five councils in England may be forced to impose drastic controls to stave off bankruptcy (LGA, 2019; see also Amin-Smith et al., 2019; Gray & Barford, 2018). Rising demand and population, alongside cost drivers such as increases in the minimum wage, increase these pressures still further.

The emergency support measures associated with Covid-19 in the spring of 2020 put such concerns into still sharper relief. Careful budget management of already pressurized local services was swept aside as the sector struggled to manage child and adult social care services, homelessness and enforcement issues. The government has made several billion pounds of additional funding available through 2020, but many councils have expressed fear of bankruptcy due to ongoing lost local income and pressure on services.

Opportunities for financialization in England

Kim and Warner (2020) set out a range of options available to local authorities facing fiscal stress. These include: cutting services temporarily; instituting or increasing user fees and charges; increasing local taxes; increasing tax revenue by promoting local growth; closing less politically critical services; driving down staff costs; drawing down reserves; and 'open[ing] up services to market-type competition and delivery' (outsourcing). 'Promoting growth' can include capital investment to drive economic boosterism: this is where the possibility arises of lenders seeking to influence local investment priorities, explicitly or by default (Mertens et al., 2019). Local tax revenue forms on average some 40–50% of local authority income in England, meaning that, in principle, promoting local growth and benefiting from increased tax revenue appears an attractive strategy to increase local revenue substantially. That in turn implies a greater potential exposure to financialization: tax revenues becoming more dependent on economic success, and more pressure to attract investment from global capital markets to drive that success. However, the current political landscape in England offers little prospect of such a change. This is for three main reasons.

First, central government maintains control of most of the critical levers of local government funding in England. This is evident from examining the availability in England of the options identified by Kim and Warner (2020). Many of these options provide local authorities with little leeway to control their financial destiny. Local authorities are under statutory duties to provide many local public services. Property tax rates are subject to very tight 'tax and expenditure limitations'. Most fees and charges are set to scales set by central government, or may only cover the cost of providing a service. Outsourcing has been common in English local government for 30 years but has largely ceased to provide transformative savings (Sasse et al., 2019). In this context, it is no surprise that the most recent high-profile expansion in local revenue has arisen from the large-scale development of commercial property portfolios, in some cases running into the hundreds of millions of pounds of capital spending (Christophers, 2018). This is one of the few areas in which central control was, for a time, comparatively lax.

Second, central government control of funding aligns with the established UK practice of seeking equity in public service provision. The English local government finance settlement redistributes significant quantities of funding between localities. The government's Business Rate Retention System was intended to increase incentives for local economic development by tying it to individual authorities' revenue levels; however, it has been stymied, partly by equity concerns (see below).

Third, the UK's financial management system requires English local authorities to adhere to the standard distinction between capital and revenue accounting. Capital spending is defined as spending to purchase or improve physical assets that may depreciate in value over time, such as property or infrastructure (land, buildings, rail, road, utilities). Capital receipts cannot be used to plug gaps in the revenue account. Critically, English local authorities may only borrow for capital investment, not for revenue spending. This distinction is sometimes blurred (e.g., Mertens et al., 2019): borrowing at unfavourable rates of interest, or using unfamiliar instruments such as tax increment financing or LOBO loans, has implications for the cost of capital programmes and the overall financial health of an authority, but it does not directly influence revenue spending decisions directly. Additionally, local authorities must follow a number of statutory codes concerning treasury management, investment guidance and minimum revenue provision, and undergo annual internal and external audit. These statutory codes form core 'institutional logics' within English local government, and influence 'material practices' decisively (Ferry & Eckersley, 2020).

Exposure of local authorities

UK government policy has promoted reforms to local government funding practice during the 2010s. The underlying policy objective has been to increase local authorities' control over their own financial health, but their effect has been constrained. Taking the first factor above – central control – the 2010s has seen some reduction in ring-fencing of transfer grants, and a tacit encouragement of commercial property development. But the substantial reduction in transfer grants noted above reduces local authorities' control over their financial health. A policy that nominally increases local accountability has, in practice, been accompanied by severe service reductions (Kim & Warner, 2020; Lowndes & Gardner, 2016). The unpredictable consequences of Brexit and Covid-19, at the time of writing, are magnifying the long-term risk to English local authority finances from this source.

In principle, local revenue-raising could compensate for these reductions. However, English local authorities have also seen restrictions on raising domestic property tax – the government sets a limit in the region of 2–3% each year. Consequently, their total revenues have been unable to keep pace with costs and identified need (Amin-Smith et al., 2019). In response, there are indications that local authorities are sweating existing taxation and revenue-raising powers to the maximum. Examples include reductions in council tax discounts for those on low incomes and on empty properties, and wrongly charging students council tax outside term periods. In parallel, business rate payments have been sought far more assiduously from properties previously rarely held to be liable: for instance, agricultural land with occasional use (for instance, festivals for a few weeks per year) and automatic teller machines. The headline rates of both taxes rise year on year, increasing taxpayer disquiet and potentially eroding the legitimacy of both taxes in the long term.

In the second case, the UK government has attempted to draw closer links between local authorities' policy decisions and their revenue levels. It reformed the non-domestic rating system in England in 2013, permitting local authorities to retain up to 50% of the increase in rate revenue against a 2013 baseline (Mor & Sandford, 2017; Muldoon-Smith & Greenhalgh, 2015). The purpose was to incentivize local authorities to grow their local economy and benefit financially from a resulting increase in business rate revenues. However, the system features several shortcomings. It assumes a link – between local gross value added (GVA)[1] and property rateable value – which research demonstrates to be low to non-existent (Mor & Sandford, 2017; Muldoon-Smith & Greenhalgh, 2015). The implementation of the policy provides limited incentives for local authorities: as the UK government retains control over the valuation of property and the tax rate, the only source of growth is building additional commercial property rather than to attract or grow high-value firms. This incentive is available only to a minority of authorities, contingent on the sectoral structure of their economies and the availability of land. Even those authorities that can grow revenue in this way see it mitigated by a redistribution mechanism (the tariff and top-up system) designed to ensure that less wealthy authorities can meet their statutory duties (Mor & Sandford, 2017).

The web of incentives plays well to lower tier authorities in the South-East of England outside main urban areas with robust economies and space to build (Bates, 2018), and to some extent buoyant Northern cities. Other locations, such as buoyant city economies lacking space to build, benefit far less if at all from their economic success (Muldoon-Smith & Greenhalgh, 2015). Thus, the centrally designed structure creates inconsistent incentives to pursue growth in productivity and innovation across different locations.

This is a manifestation of a more pervasive conundrum within local authority finance: how to balance national imperatives toward equity and redistribution and local accountability for local public spending. These two principles work against each other: where a local authority receives substantial transfer grants to compensate for a shortfall in local revenue, local financial accountability is reduced. This conundrum is inherent in the fiscal federalism literature (Musgrave, 1959; Oates, 1972; Tiebout, 1956), but it rarely features in public accountancy research or in political debate. The balance between these two principles governs the sources of any individual local authority's funding and thus strongly influences its policy choices: this is visible from the many authorities that have sought actively to expand their business rate revenue through large-scale redevelopments and grants of planning permission.

The third factor – the distinction between capital and revenue accounting – has generated specific pressures in England during the 2010s. Faced with multiple constraints on their use of revenue spending, many English authorities have pursued an area in which they are relatively unconstrained by law: investment of capital funds, often in commercial property, to raise revenue (Christophers, 2018; Pike et al., 2019a). The logic is simple: UK authorities can borrow at near-sovereign rates, purchase commercial property, and rent it out for a net profit; the profit constitutes revenue funding and can be reinvested in services. This activity overlaps with the conventional purchase of buildings in order to de-risk development opportunities, which subsequently incentivizes new development and wider urban regeneration. The government has welcomed the inherent entrepreneurialism around property investment whilst tightening up statutory codes of practice and scrutiny to discourage borrowing for investment alone (NAO, 2020; Sandford, 2020): a further obstacle to financialization.

In summary, the windows of opportunity for financialization in English local government are few and far between. This is due to central–local relations, public service equity considerations, and the regulatory framework. Under these conditions, it is unsurprising that practitioner and policy attention has clustered around ideas for new sources of finance. In the next section, we seek to shed some light on this debate, currently often hazy and lacking in detail.

Classifying sources of revenue

Access to new sources of finance has been a staple demand from the English local government sector for many decades. It is currently accompanied by calls for devolution of power, local responses to falling transfer grants, and 'place-based leadership' (Beer & Clower, 2014; Sotarauta, 2016). The increase in such behaviour has coincided with the emergence of, and interest in, financialization and statecraft (Pike et al., 2019a) and fear that global capital markets have greater influence over local authority finances in the medium term (Beswick & Penny, 2018). Additionally, at the time of writing, the effect of coronavirus on English local government finance seems likely to be at a scale which demands long-term changes to the balance of revenue sources available.

However, we argue that most of the novel sources of revenue proposed in current debates in England are not susceptible to financialization. This is not merely because they promise little impact on the features of central control, equity concerns, and regulation: there are three other features that militate against large-scale financialization. First, its primary impact occurs through capital finance-related transactions, whilst English local government is struggling for revenue funding. Second, most of the proposed sources of funding would produce peripheral quantities of funding. Third, the incidence of the proposed sources varies starkly in geographical terms, essentially because of the significant variations in wealth, income and property values that characterize England. These second and third features also create difficulties for any policy seeking to increase the funding available to local government in a way that can be applied to all or most geographical areas.

Table 1 provides a typology of sources of local government revenue in England, in order to illustrate the three features of the current debate noted above and to provide an initial analysis of opportunities for financialization and their potential contribution to addressing the 'solvency question'. Methodologically, the authors have used a combination of government policy analysis, examination of financial techniques and institutions, and publicly available secondary data sources to assemble these sources, rather than the creation of new empirical data. The originality resides in the bringing together and categorization of opaque and disparate methods of local government funding for the first time, in order to form a staging post for new enquiry into the role of local government funding in territorial development. The methods themselves currently lack transparency, and the data associated with such methods is often relatively hidden. This is

Table 1. Typology of local government funding instruments.

Category	Examples from England	Capital	Revenue
Recurring transfer grants	Revenue support grant, public health grant, better care fund, new homes bonus, rural services delivery grant and educational services grant		Yes
Local taxes	Council tax and business rates (including empty property rates; revaluation; empty homes premium)		Yes
Bid-based grants	Local growth fund, regional growth fund and earn back/gain share	Yes	Yes
Asset sales	Sales of land, property and other assets	Yes	
Land value capture	Section 106, Community Infrastructure Levy, betterment levies and London's Development Rights Auction Model	Yes	
Transport charges	Congestion charging, workplace parking levy and low-emissions zones		Yes
New taxes	Local income tax, tourism tax, land value tax, stamp duty and value added tax (VAT)		Yes
Capital financing of borrowing	Tax increment financing (TIFs), bonds and national loans funds (Public Works Loan Board – PWLB)	Yes	
Commercial investment	Commercial property investments		Yes

considered by the authors to be a key impediment to meaningful analysis of local government funding.

In Table 1, the column 'Examples from England' lists existing sources of revenue and, critically, groups the most common terms used within the debate to describe proposed novel sources of revenue. A feature of the English debate is a lack of clarity around the meaning of these terms. To remedy this, the leftmost column groups the sources and proposed sources according to how they (would) function. It also indicates whether the funding produced by each source constitutes capital or revenue funding, or potentially both: this is critical for assessing these sources' potential contribution to the 'solvency question'.[2]

The sections below provide commentary and analysis on each of these categories in turn, assessing their potential contribution to the 'solvency question' and to processes of financialization.

Recurring transfer grants

Recurring transfer grants are available for revenue spending. Many are unringfenced, the major exception being the Public Health Grant. Amounts are distributed at the annual local government finance settlement. In 2018–19 the grants listed in Table 1 totalled some £14 billion. The amount and distribution of transfer grant in England is entirely at the discretion of the UK government. Thus, a generous grant settlement can be an effective source of funds for local authorities; but local authorities have no power to resist a less generous settlement.

Transfer grants are a double-edged sword in respect of solvency. The financial struggles faced by English local authorities in the 2010s derive principally from reductions in Revenue Support Grant (from £15 billion in 2013–14 to £3 billion in 2019–20), a gap which local authorities have been unable to fill from other sources. Equally, an increase in transfer grant would likely be the quickest and simplest way of solving the issue. Grants, however, inevitably generate political debate around how needs assessment drives distribution between areas (Gibson & Asthana, 2012; Stone, 2012; Vadean & Forder, 2018). Ambitious councils can see distribution methodologies as a hindrance, preventing any financial incentive to invest in their areas.

Local property taxes

Council tax and business rates each produce some £25 billion of revenue each across England – a hugely significant part of local government's funding. As noted above, in practice, local authorities do not control tax rates for either, meaning that their contribution to the 'solvency question' is limited. Total increases in revenues from each source have amounted to several hundred million pounds per year in cash terms during the 2010s, a substantial amount but insufficient to fill the gap left by Revenue Support Grant reductions. Rises in council tax and business rates revenues are very geographically uneven (Mor & Sandford, 2017; Muldoon-Smith & Greenhalgh, 2015), reflecting the unevenness of England's economy and land markets.

Tensions also arise from the erratic incentives arising from the interaction of rates retention and local policy priorities. For instance, the incentive to add to the overall property stock incentivizes retail over manufacturing properties (Muldoon-Smith, 2019). Rates are payable irrespective of occupation, reducing the incentive to actually encourage businesses into an area or to encourage those with high growth potential (Greenhalgh et al., 2018; Muldoon-Smith, 2019). Almost two-thirds of the properties in the tax base potentially benefit from full relief, removing any incentive for the government to encourage growth of small business units.

As both council tax and business rates are property taxes, one might expect them to provide a ready path of influence for financialization. Authorities might seek to increase their stock of properties in order to generate tax revenue for securitization purposes. The sources of income, for example, office parks and shopping centres, may be financed and therefore, in part, owned by a variety of real estate finance entities that are subject to global capital markets. However, local authorities cannot hope to add to the property stock in substantial quantities (Muldoon-Smith & Greenhalgh, 2015), meaning that income increases of any size are elusive for the majority of authorities (Amin-Smith et al., 2016; Mor & Sandford, 2017).

Bid-based grants

English local authorities have long had access to a range of bid-based funding schemes. These are characterized by funding being distributed according to the quality of the business case made by the bidder, instead of (or in addition to) need-based criteria and the deal making negotiations between local area and centre (O'Brien & Pike, 2019) Such schemes may distribute capital and/or revenue funding, and they normally feature conditions deriving from central government policy. The distribution of the funding will often reflect political priorities. Most such funds are ringfenced to the extent that they cannot be used to bolster funding for core services, thus their contribution to addressing the 'solvency question' is marginal at best. Nor do they provide a ready avenue for financialization.

Some English localities have sought to negotiate payment by results elements within bidding structures: for instance, the concepts of 'earn back' and 'gain share' in Greater Manchester (NAO, 2017). The aim is to incentivize local authorities to invest in policies which will financially benefit other public bodies. Originally, Greater Manchester had hoped to negotiate a deal whereby additional revenues would flow to them automatically, but ultimately both 'earn back' and 'gain share' were implemented via transfer grants.

Asset sale and investment

Local authorities are free to own, buy and sell land and property assets. Their ownership of assets varies widely, based on historical practice. Some English local authorities have developed commercial property portfolios in recent years (NAO, 2020). For example, as Pike et al (2019b) note, Portsmouth City Council purchased property interests in Birmingham, Somerset and Swindon and let parts of its ferry terminal to an international insurance institution during the late 2010s. These are capital assets, and therefore the proceeds of sale constitute capital funding and cannot be spent on services. Asset sales can be used to plug gaps in service provision in limited circumstances (via 'capitalization'), but this is an exceptional procedure. Local authorities could not use it at a scale that would address the 'solvency question'.

Property sales, and related initiatives such as leaseback and joint ventures, do offer some opportunity for influence from financialization. A local authority might, for instance, purchase a property jointly with a corporate investor. They would need to negotiate the use of the building, and revenues from it, with the investor, and these might conflict with local priorities due to profitable use being favoured over social impact. One method that has gained some degree of notoriety is the 'income strip' model. For example, Legal & General recently bought the Sovereign shopping centre from North Somerset Council for £21 million and then leased it back to them for 35 years with the council paying £717,696 per annum rising with inflation but, importantly, capped at 4%. The plan is for the council to sublet the property and benefit from any additional rent and at the end of the lease reclaim the asset at nil value. However, this is subject to risk with income being cyclical and dependant on market forces, while the asset is likely to be severely depreciated after the 35-year lease term without significant investment.

Local authorities owning commercial property is not a recent phenomenon: a report from the Local Government Chronicle (Calkin, 2017) indicated that many authorities had substantial property holdings before 2010. However, the late 2010s saw a trend towards much more explicit use of such mechanisms to generate revenue income, with the purchase of assets often backed by capital borrowing. Rental income from property assets is not treated as capital funding. These property holdings are mostly not critical to service provision, thus financialization would not directly influence local choices about public services.

Certainly, processes of financialization will have an impact upon the ownership, use and trade of assets with the local government system. However, this impact is likely to be minimal. Financial institutions require the securitization of a significant stream of buoyant and sustained rent. Evoking Graham and Marvin's (2001) conceptualization of premium locations and splintered development, only a distinct subset of centrally located city centre locations have the potential to consistently offer this resource, that is, those with lucrative rental markets.

The rental income from commercial investments is unlikely to be of the same order of magnitude as income from local taxes. In 2018–19, 'commercial income' for all local authorities in England totalled just over £1.5 billion (most, though not all, of which likely derived from property investments).

Land value capture

Land value capture, also known as 'uplift' or 'betterment levy', is a concept with a long pedigree. Put simply, where public sector infrastructure investment has led to a rise in land or property values in an identifiable area, land value capture mechanisms seek to return some of that rise in value to the public sector. Land value capture systems have been relatively underdeveloped in the UK. 'Section 106 agreements' constitute agreements between large-scale developers and local authorities: large developers agree to pay certain sums to a local authority that grants them planning permission, and the authority spends the money on infrastructure related to the development. The Community Infrastructure Levy (CIL) is a rate per square foot that local authorities may levy on new commercial floorspace at completion. Business rate supplements can be used as a blunt form of land value capture, when linked to future developments in the area subject to the supplement.

Recent figures indicate that these sources of income are marginal. CIL generated £269 million in England in 2018–19. Section 106 agreements generated some £5 billion, but this revenue is ring-fenced to the development generating it. This latter point suggests that financialization could influence capital infrastructure decisions under certain conditions, but the funding from this source could not be switched to balance the revenue demands of public services.

International experience suggests that land value capture is disproportionately effective in very high-value areas (Urban Land Institute, 2016). This is borne out by the UK experience (TfL, 2018). For instance, the Battersea/Nine Elms development in inner London is being funded by £266 million in CIL and Section 106 agreements over a number of years, plus a TIF scheme borrowing £1 billion against projected increases in business rates in a local enterprise zone over 25 years. New high-value housing and office accommodation in very close proximity to central London should generate sufficient value for these tax revenues to materialize. In contrast, most areas will not be able to access significant sums from land value capture, because developments do not generate sufficient rises in land values and are less elastic (TfL, 2018). This implies local tensions for any comprehensive system of LVC – between buoyant city locations and 'the rest'.

New taxes

Multiple suggestions have been made for the creation of new local taxes in England. The most prominent recent example is the idea of a 'tourist tax': a small charge on accommodation providers per bed occupied per night. There are no legal powers to introduce such a charge in the UK at present. Interest has been forthcoming from a number of sources (Peters, 2019; Scottish Government, 2019), with estimates that a levy of £1 per person per night would generate some £420 million per year (Amin-Smith et al., 2019). The IFS suggested that incidence of the tax would be uneven, generating local tensions: though some more deprived parts of England, such as Devon, Cornwall and Cumbria, would benefit substantially.

Further options include local income tax, stamp duty and the assignment of VAT revenues (Amin-Smith et al., 2019; London Finance Commission, 2017). Estimated revenues from these taxes are at a different scale from those generated by the options discussed above. Stamp duty generated some £12.8 billion in England in 2017–18; 1p on the basic rate of income tax would generate £6.4 billion in 2018–19; and VAT generated £108.4 billion in England in 2018–19 (Amin-Smith et al., 2019). Devolution of these taxes, or assignment of part of their revenues, would provide revenue of a scale that could address the 'solvency question'. This explains their prominence in debates over fiscal devolution to Scotland and Wales (Smith Commission, 2014). However, applying the same logic to localities within England would reveal a very uneven revenue incidence: the contrast would be particularly stark between London and the rest of England (London Finance Commission, 2017).

The option of replacing the current property taxation regime with a system of land value taxation has also been raised (Corlett et al., 2018; London Assembly, 2016). This is designed to bite down upon and secure revenue from contemporary modes of using cities and the new world of work, which cannot necessarily be entirely captured from bricks and mortar or traditional methods of property taxation. There is no consensus in the English debate on how a land value tax would work: but any such tax is still likely to suffer strongly from uneven incidence, reflecting the variegated potential and economic strength between different areas of England.

The central contention within land value tax is that the value of land is defined by what is happening in the immediate location and wider region. For this reason, land value tax is considered progressive because it captures value invested by society in a given location and aids current calls for local wealth building and inclusive growth. However, a great deal of land simply has no value and demands a certain degree of investment for development readiness. This suggests that there will still need to be a complex system of equalization between locations and grant funding (Sandford, 2017). Indeed, research recently carried out by the Liberal Democrats (Corlett et al., 2018), into their proposals for Commercial Landowner Levy, indicates that the tax yield will significantly decrease in certain locations in comparison with the business rates system.

Local governments can introduce road pricing ('congestion charges'). This has so far only been done in Greater London (plus a minimal scheme in Durham), though in 2020 other English cities have begun to reconsider instituting schemes. The London congestion charge (which includes the London Low Emission Zone and Ultra Low Emission Zone) raised a total of £146 million in 2017–18. All local governments also have the power to introduce a 'workplace parking levy' – a charge on businesses' car-parking spaces. The only existing levy is operated by Nottingham City Council, and it raises some £10 million per year.

These sources of revenue constitute additional taxes, and are thus relatively sheltered from the effects of financialization. However, as the sums noted indicate, most provide only marginal contributions to the 'solvency question'; and their revenues will be concentrated in economically active areas, where all modes of transport use are at their highest.

Commercial investment and capital financing of borrowing

As noted above, English local authorities are free to borrow for capital purposes. They may borrow from the government-backed Public Works Loan Board (PWLB), or from any other lender; they may also issue bonds, alone or via the Municipal Bonds Agency established in 2016. Several have obtained credit ratings from one of the three major ratings agencies. The funds borrowed cannot be spent directly on public services but can be invested in order to generate that revenue, thus indirectly addressing the 'solvency question'. For example, the much-vaunted system of tax increment financing consists of borrowing for construction of building and infrastructure funding purposes, using as collateral the rises in tax rates that will result from the building of the infrastructure (for instance, higher property taxes, increased tourist tax revenues). This relies on the success of the infrastructure project in question, and means that those additional tax revenues cannot be used for other purposes.

Borrowing and commercial investment offer substantial discretion for most English authorities. Overwhelmingly, borrowing practice in English local government does not permit direct lender influence over the use of the funds. Local authority trading companies, Joint ventures, special purpose vehicles and social enterprises, permitting substantial decision-making power to lending institutions or partners, are comparatively rarely used, again limiting the reach of financialization in practice. It is therefore unsurprising that commercial investment has formed a high-profile approach to the 'solvency question' in late 2010s England: it offers a source of unringfenced revenue, which can be relied on as long as the property market remains healthy. Local tensions are also limited. Perhaps counter-intuitively, borrowing is one activity in which variations in access between buoyant and less buoyant areas are less pronounced. Most authorities borrow from the PWLB, and councils in the latter areas do not face inferior terms. However, while access to borrowing is relativity equal, the ability to repay is not because it is dependent on a given local authority having the means to service debt. Government has expressed concern about the levels of borrowing incurred by some councils – some in excess of 40 times their annual income.

CONCLUSIONS

This research provides a stepping-stone to reflect upon how local government funding behaviour and decision-making is influenced and constrained by central–local relations and the prior evolution of place. The analysis above suggests that, in the English context, central–local relations, and the legal framework they underlie, are a more significant influence on local government financial practice than financialization. We present this as a staging post for new enquiry in the role of local government funding in studies of territory, politics and governance. Further research could explore each funding method presented in this paper in international perspective, with case-study analysis, exploring the influence of their structures on local decision-making and place management. In addition, further research into the interface between path dependent local government funding mechanisms and the capital circuits of global financialization has the potential to shed a new light on (1) the intermittent fiscal decision-making space of both; and (2) how each evolves and is grounded within territorial constraints.

Further research could improve the quality of debate on local government funding at a critical point for English local government. Solvency problems were building in English local government from a number of quarters during the 2010s, but the coronavirus pandemic has sharpened their urgency. Local authorities are likely to face shortfalls from existing revenue sources for several years. The legitimacy of the current key sources of income – property tax and commercial revenues – was already facing challenges, and simple increases in tax rates and investments are unlikely to be politically palatable. These pressures suggest that the clamour for alternative sources of revenue is likely to increase during the 2020s. However, in response to the research question in this paper, the analysis above suggests that a large number of the alternative sources of revenue currently being debated are peripheral in revenue terms and uneven in geographical terms. The actual and potential sources of funding presented in this article are not simply 'treasure chests' that can be unlocked at will in order to stave off financial struggles.

Central government enthusiasm for funding local authorities via the financial benefits of growth has been echoed, throughout the 2010s, in the local government sector's support for greater capacity to raise local revenue in order to drive local growth. However, the sources of local revenue highlighted in this article do not generate revenue at the scale required to maintain existing public service levels. The increasing interest in these sources simply reflects that English local government has exhausted the options available to it to maintain its portfolio of service provision and community maintenance (Christophers, 2018). More recently, the Covid-19 situation has remagnified the enduring importance of the local state. Local government faces substantial, potentially permanent gaps in its local and commercial income resulting from the mid-2020 'lockdown'. At the time of writing, there is much speculation in the sector about multiple authority bankruptcies. It is conceivable that the Johnson government's 'levelling up' agenda, and its commitment to a 'fundamental review' of business rates, offers a new opportunity to grasp the nettle of substantial local government finance reform in England.

In the field of financialization and local government studies, we respond to Fields (2018) who argues that the process of financialization is often poorly understood, and utilized as an all-encompassing explanation in itself without any investigation into how the process of financialization occurs. We take a circumspect position, arguing that financialization is not all encompassing. Drawing on the work of Graham and Marvin (2001) we argue that in England, financialization only has a direct bearing on local government funding in premium locations with buoyant economic conditions and projects associated with capital financing. More influential are the often more mundane technicalities of local government funding regulation (Christophers, 2018) and the institutional logic of orthodox financial management practices (Ferry & Eckersley, 2020). Such techniques are ultimately like algorithms, ultimately made up of opinions embedded in mathematics. The detailed design and operations of local government funding sources tend to be the purview of a narrow band of people with specialized knowledge and interest – hidden from public discourse.

However, we caveat our circumspect position by arguing that these examples of financialization could, in certain circumstances, be strategized to ultimately create new revenue for local public services. There is potential for a conscious gaming strategy (Buller & James, 2012) where local government consents to the construction of new buildings that ultimately provide much sought after revenue. This last point provides a new insight into financialization related studies, which typically investigate the mechanisms of directly securitized assets – for example Tax Increment Financing (Weber, 2010) and Single Family Rental assets (Fields, 2018).

Our empirical findings suggest that, if a number of additional sources of revenue did become available to English local authorities, this would likely increase authorities' exposure to economic volatility, but it would be unlikely to presage large-scale financialization of decision-making. That would require the ending, or dampening, of one of three critical characteristics of English local government: centralization, bureaucratic regulation and equity concerns. Certainly, financialization may influence decision-making in a small number of high-value locations, and politically, the optics of such decisions could be unduly influential: this has already been visible in media debate over commercial property investment, which is dominated by a focus on a very small number of authorities. However, it seems unlikely to lead to systemic instability, unless English local governments were to become dominated by local growth responsibilities akin to some of their counterparts in the United States (Harding, 1991).

DISCLOSURE STATEMENT

No potential conflict of interest was reported by the authors.

NOTES

1. GVA is the value of output less the value of intermediate consumption; it is a measure of the contribution to gross domestic product (GDP) made by an individual producer, industry or sector.
2. Table 1 is based on a table that appeared originally in Strickland (2013) and subsequently in Pike et al. (2019a). However, that table was used specifically to assess the progress of financialization rather than to develop a typology of revenue sources.

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