

London Finance Commission

Minutes

Tuesday 16th October 2012, 15.00 – 17.30

Conference Room 5, City Hall, The Queen's Walk, SE1 2AA

Present

Steve Allen	SA
Roger Bright	RB
Martin Clarke	MC
Chris Duffield	CD
Steve Freer	SF
Julia Harrowsmith	JH
Nick Holgate	NH
Jeff Jacobs	JJ
Alexandra Jones	AJ
Gerald Jones	GJ
Sir Stuart Lipton	SL
Ed Lister	EL
John O'Brien	JO
Teresa O'Neill	TO
Jules Pipe	JP
Ben Rogers	BeR
Bridget Rosewell	BrR
Jeremy Skinner	JS
Tony Travers	TT

Apologies

John Biggs	JB
Mike Emmerich	ME
Stephen Hughes	SH
Nick Raynsford	NR
Martin Smith	MS

Actions arising

JH to circulate notes from stakeholder meetings to the Commission. **JH**

JH to circulate the Scotland, Wales and Greater London paper by email. **JH**

LFC to send comments on the Scotland, Wales and Greater London by email. **LFC**

No.	Agenda item	Action
-----	-------------	--------

1 Apologies

1.1 JB, ME, SH, NR and MS sent apologies.

2 Minutes and actions arising from 7th September

Minutes

2.1 LFC agreed the minutes from 7th September.

Actions arising

2.2 Actions have been completed or are underway.

No.	Agenda item	Action
3 Address from the Mayor		
3.1	EL reported that owing to a family emergency the Mayor was unable to address the Commission on this day. The Mayor sent his apologies and will appear at the November meeting instead.	
4 Update on external meetings		
4.1	TT has spoken at the London Financial Advisory Committee (LFAC) of the Society of London Treasurers (SLT) . He will address the London Assembly and the Chief Executive London Committee in the coming weeks. JH, JS and TT have met informally with the Cities Unit of the Cabinet Office, the London and Local Government Finance Unit of the Department for Communities and Local Government and with the Local Government Unit of the Treasury, as well as with the Institute for Fiscal Studies.	
4.2	BeR requested that the meeting notes from the above meetings be circulated to the Commission. JH will circulate these notes (but they will not be published on the website given the informal nature of the meetings).	JH
5 Scotland, Wales and Greater London paper		
5.1	This paper was circulated for the first time in this meeting for information.	
5.2	TT requested that the LFC send comments by email and that there would be chance for a fuller discussion of the paper in the December session.	LFC
5.3	LFC requested that the paper be sent by email.	JH
6 Allocation of questions for evidence session		
6.1	TT allocated the pre-drafted questions to LFC members to pose to the witnesses and explained there would also be a chance to pose additional questions freely.	
7 AOB		
7.1	No AOB.	
8 Dates of next meetings.		
8.1	16 th Nov 14:00 - 16:30 City Hall CR5 13 th Dec 09.00 – 11.00 City Hall, Chamber 9 th January 10.00 - 12.00 City Hall CR2 14 th February 10.00 - 12.00 City Hall CR1 14 th March 10.00 - 12.00 City Hall CR3 11 th April 10.00 - 12.00 City Hall CR3	
9 Oral evidence session		
9.1	The final two hours of the meeting were used to hold an oral evidence session with expert witnesses Sir Michael Lyons (SML), Jim Gallagher (JG), Paul Johnson (PJ) and Ken Livingstone (KL).	

No.	Agenda item	Action
9.2	The session was open to the public and journalists were invited to attend. It was streamed live and a recording is available online: http://www.london.gov.uk/london-finance-commission	
10	Sir Michael Lyons	
10.1	TT introduced SML and invited him to give an opening address.	
10.2	SML gave an account of his career, which has included 23 years working in local government, and several years as Professor of Public Policy at Birmingham University. He has chaired a number of reviews for the previous government, including an extensive report on local government functions and finance in 2007.	
10.3	TT posed the first set question: <i>Do you consider that funding arrangements for the capital are too centralised (that is, at the national government level)? Why/why not?</i>	
10.4	SML began by stating that he does believe funding arrangements for London are too centralised, but that this applies to the whole of UK/English local government as much as it does to London.	
10.5	In his opinion, a new constitutional settlement between local and central government (rather than a simple change to the balance of funding) is required for four main reasons set out in 10.6 – 10.9.	
10.6	There is a need for better governance, with greater clarity around where responsibilities lie for decision making. To this end, more spending should take place locally, where taxes are raised.	
10.7	It is clear that as places vary radically, local people deserve to have a voice in local provision. Although some needs and aspirations are the same nationally, judgements about how the marginal tax pound is spent differ most dramatically at the local level, and such decisions should be made closer to people's lives. For example, the free bus pass for senior citizens is considered to be extremely valuable in London where bus provision is extensive, yet in more rural areas where bus services are extremely limited, funds could be spent in better ways.	
10.8	All levels of government should focus on building the country's economic capability. The current system does not provide a strong enough link between the local economy and tackling supply side issues. Local government should be incentivised to give absolute priority to economic development.	
10.9	It is important to manage the expectations of the public about what can be achieved through public sector spending. Many assume that services can improve without any increase in public spending. Local government must be a major agency in the dialogue with citizens about provision and corresponding tax levels. The media dwell unhelpfully on the issue of postcode lotteries, but when taxation is remote from local spending, citizens fail to realise that increased taxation leads (for example) to better local services.	
10.1	BrR posed the question, <i>what should the emphasis of devolution be, value for money or delivery of services (ie supply or demand)?</i> SML replied efficiency is important and that greater accountability sharpens the responsibility of those spending, thus increasing value for money.	
10.1	<i>SF posed the second set question: What alternative options would you like to see considered, especially to promote jobs and growth? Is there a case for greater devolution of taxes, or more direct assignment of tax receipts, to London? Should any such options cover only existing services run by the GLA and the boroughs, or might they go wider as part of a greater devolution of power?</i>	
10.1	SML said that achieving change in the UK tax system is a longwinded process that can only be done over time. Therefore, with an eye to the long term, his report was purposely	

No.	Agenda item	Action
	drafted in a way that could appeal to different political parties in government.	
10.1 3	In his opinion council tax will remain for the foreseeable future and for this reason it should not be dismissed. Clearly, property-based taxes should be revalued regularly; at present some people pay too much and some people pay too little. Indeed, council tax could be used to generate additional income through extra bands, particularly in London where the housing market has received an injection of overseas investment over recent years (with many regarding London housing primarily as an investment rather than accommodation). It is not unreasonable to demand that those in the higher reaches of the housing market should pay more.	
10.1 4	While his report did not actively recommend a tourist tax, he does think the idea should be explored further. The debate is nuanced in that tourists impose costs but also contribute to the economy. It is very unlikely many other parts of the country would adopt a tourist tax but in London there may be an appetite.	
10.1 5	SML thinks that a local income tax is a step too far. It would shift the tax burden from the retired to the working population and this is undesirable, given that the balance of wealth is already in favour of the retired.	
10.1 6	He said that assignment should only be considered as a transitional option on the way to taxation powers, rather than an end state. It has merits because it emphasises lines of accountability, shows a clear link between taxes paid and services funded and allows for more local choice.	
10.1 7	He also believes that stewardship of place is important. Given that local government is the only elected body in any locality, it has a role to play in drawing other services together. It makes sense for public health to move back to this level, and there should be a conversation about which other areas may be suitable and might lead to a more efficient integration of activities and better value.	
10.1 8	SF commented that decisions about council tax are becoming increasingly centralised, exacerbated through the new grant awarded for council tax freezes for example. SML understands the concerns of the LGA about the current situation, as the history of centrally inspired freezes indicates there may be local problems when the grant is eventually phased out, as councils have to make up for the shortfall through steep council tax rises, and responsibility for this falls only to local rather than central government.	
10.1 9	TO commented that regarding council tax, property prices differ significantly between inner and outer London. Certain boroughs would benefit very little from additional bands, so she asked where additional money would come from, and where it would be used. TT added that under the current arrangements, if more were paid by some properties in some bands, additional revenue would be 'equalised away', meaning that local government would not be better off. Would there be any way of London local government being able to retain the benefits of any additional revenue? SML said that this is a fraught area. It is difficult on the one hand to argue for more inequality, and he understands the reasons for equalisation, but on the other hand it is unfeasible to increase tax and use it as an incentive without demonstrating benefits for those who pay more (which would usually have to be done locally). Perhaps it could be applied to London-wide services.	
10.2 0	CD questioned whether, with a tourist tax, additional revenues should be hypothecated for particular purposes. SML said that he is against hypothecation, but that for the sake of accountability revenues should be spent locally. A tourist tax would raise questions of national fairness but lots of these options raise difficult questions.	
10.2 1	Br asked: <i>in particular, regarding capital investment, do you consider that London requires greater financial autonomy to enable it to make effective investment decisions? How and in what regard? What implications would this</i>	

No.	Agenda item	Action
	<i>have?</i>	
10.2 2	SML said that while he said he could not offer a full answer to this (his report only covered this topic briefly), he does think local government should have more freedom to decide what is needed in the locality, on behalf of local citizens.	
10.2 3	The supplementary business rate, which was one of the Lyons recommendations picked up by government, was levied to fund Crossrail. When government engages the business community about things that affect them and that they value, it is often willing to play a part and enter into additional funding, particularly on infrastructure investment, but only on condition that it is clear how the money is being spent and if they are able to influence decisions. This raises the need for clarity again, as well as the need for local government to be able to make decisions on behalf of its community.	
10.2 4	TIF worked well in Chicago and its further application in London makes sense.	
10.2 5	BeR asked SML whether or not it makes sense that central government has so much involvement with capital projects in London. SML replied that the place of central government should be to set the framework including the outer boundaries, not to micromanage local actors. If all local authorities have to apply for approval, devolution cannot be said to have taken place.	
10.2 6	TT commented that the Lyons report was relatively cautious in tone. He asked SML why Scotland and Wales could afford to be so radical, and whether the situations there imply that London could be more 'ambitious'. SML said that when the devolution settlements for Scotland and Wales were drawn up, the consequences as they are now were quite unforeseen. One of the reasons it has gone so far in those places is that the public have demonstrated clear volition. One interesting lesson to be drawn from Scotland and Wales is that devolution can lead to innovation, and that these two countries, which in many ways have much in common, have chosen, at the local level, to become quite different.	
10.2 7	TT thanked SML for appearing as a witness before the Commission.	
11	Jim Gallagher	
11.1	TT introduced JG and invited him to give an opening address.	
11.2	JG summarised his career. He worked for many years as a public servant and was closely involved with the work of the Calman Commission about devolution to Scotland. He now works as an academic.	
11.3	TT posed the first question to JG: <i>Do you consider that funding arrangements are too centralised for Scotland (that is, at the national government level)? Why/why not? In this regard, how does the London situation compare to that in Scotland?</i>	
11.4	JG commented that the devolution to Scotland and London was part of the same movement. While English regionalism failed to progress, in London it has been successful. However, the main difference between Scotland and London is that in Scotland the idea of 'nationhood' carries great weight. Scotland has more powers, including legislative ones, but there are similarities to be drawn between the finance arrangements in Scotland and London.	
11.5	JG then discussed the options for financing. Either it should be based on need or the origination principle (where taxation occurs where spending occurs). The origination principle is applied on a national level (where British taxes are spent on British affairs) but not on a local level. There must always be a trade off between financial autonomy and accountability on the one hand, and equity, administrative efficiency and avoidance of	

No.	Agenda item	Action
	economic distortions on the other. Historically in the UK the Treasury has administered everything. This is now starting to change in Scotland, where around a third of Scotland's spending will come from local taxation. This shows that Scotland is a 'different beast' but JG believes there is still room to draw parallels.	
11.6	TT asked whether or not JG finds the block grant system sub-optimal. JG explained that changes in Scotland simply brought democracy to a pre-existing administrative system inherited from the Scotland Office, which was run like a government department. He commented that the Scottish system as it is now demonstrates an unusually high level of spending autonomy and a correspondingly low level of tax raising powers.	
11.7	BeR posed the second set question: <i>please outline the current arrangements in Scotland and what alternative options you would like to see considered there (eg greater devolution of taxes, or more direct assignment of tax receipts etc). Do these promote jobs and growth, or are other rationales used to justify recommendations? Could such proposals translate to the London situation?</i>	
11.8	JG said there is no unequivocal evidence that tax devolution causes growth. Usually its effect is to drive taxes down due to competition between areas.	
11.9	Devolving spending and legislative powers can be beneficial for supply side issues such as infrastructure and education, but there is actually no strong evidence to show that this has been the case in Scotland. Politicians are already incentivised to seek growth in order to be re-elected.	
11.1 10	TT asked why Scotland did not use the Scottish Variable Rate (SVR) when it had the power to do so. JG replied that at that time, government had ample funding (in light of the economic circumstances and so on), so the Scottish administration was not compelled to use it. The way the SVR worked meant that without accessing it, the government there still received the same funding. Under the new system the Scottish Parliament will rely on its income tax powers.	
11.1 1	CD asked how Calman's recommendations for Scotland might translate to London. JG said that in principle, any tax <i>could</i> be devolved, depending on how many economic distortions are considered acceptable. In practice, the matter of borders is more significant in London. Scotland is geographically and therefore economically less integrated with its surrounding areas than Greater London is. Because of this, local income tax would be much more difficult to implement in London. Aviation duty would be incompatible with the borders of Greater London. Corporation tax could be devolved but usually this leads to falling rates of corporation tax due to competition (as has happened in the Swiss cantons) and many companies find ways to move profits rather than economic activity in order to avoid the higher rates. Devolved corporation tax was considered in Wales but HMT showed little willing to pursue it.	
11.1 2	AJ asked what options JG would specifically recommend for London. JG said it is easiest to devolve taxes with immobile bases such as property taxes (council taxes and business rates), stamp duty land tax, landfill tax and air passenger duties. He would recommend the smaller taxes, such as a bed tax and stamp duty land tax. He would not recommend corporation tax or income tax.	
11.1 3	AJ posed the third set question: <i>In particular, regarding capital investment, do you consider that London requires greater financial autonomy to enable it to make effective investment decisions? How and in what regard? What implications would this have?</i>	
11.1 4	JG said that investment <i>choices</i> are the most important thing in creating jobs and growth and being efficient. In Scotland the changes have been more to financing than management. Scotland gets a capital line in its budget and is unable to borrow; in this respect it is more like a government department than a country. Calman recommended it should have greater borrowing powers.	

No.	Agenda item	Action
11.1 5	TT asked why it is that despite having the power to raise council tax in Scotland, the Scottish Parliament has chosen to freeze rates since 2007. JG responded that once Band D hit £1000 it was felt it had reached the limits of acceptability. It is also difficult to justify any increases when the valuation level is still that from 1991. It has also been a political move; the strong temptation to cater to populist concerns prevails.	
11.1 6	TT thanked JG for appearing as a witness before the Commission.	
12	Paul Johnson	
12.1	TT introduced PJ and invited him to give an opening address.	
12.2	TT posed the first set question: <i>Do you consider that funding arrangements for the capital are too centralised (that is, at the national government level)? Why/why not?</i>	
12.3	PJ commented that so far spending has been devolved rather than taxation in Scotland and Wales, so it may be prudent to explore these avenues for London before taxation. The implication of devolving tax-raising powers is that it can cause problems at borders. The underlying question is what can be achieved through devolution, aside from political control. London is not only the richest, but also the most unequal part of the UK, so it will matter how London manages itself. Transport is a very London-specific issue (over which the Mayor already has a degree of control) and the schools system is quite London specific. It is not always obvious how devolution of taxes could lead to behavioural change, offer incentives or have an economic impact, though the changes to business rates have achieved success and transport and education may also have an effect. However, there are also strong reasons for centralisation (beyond central government's desire for power), such as redistribution. The UK stands in stark comparison with the USA, where funding levels for schools differ dramatically between areas (and are significantly lower in worse-off areas). But devolution does not preclude equalisation; London could be afforded more freedom without additional funds, and this would not be detrimental to the rest of the country.	
12.4	TT questioned whether the UK system is strange in its extreme centralisation. PJ responded that the system exists for historical reasons. There are pros and cons of different models. With the current centralised model, tax competition does not come into play and the system is less complicated; with the more local model there is more innovation, eg through new sources of taxation.	
12.5	TT asked PJ whether or not it would be possible to retain current levels of equalisation while moving away from quite such a centralised model (in the context of the UK being so centralised in comparison to other international cities). PJ said it would be possible to do this; indeed, a 'devo-max' solution where London kept all its tax revenues would never be allowed to happen as the rest of the country would lose out.	
12.6	TT asked PJ to clarify whether or not it would be possible to retain inter-area equalisation as it is, but to offer more local freedom beyond this baseline position. PJ said that this would be possible. While a baseline would ensure no areas were worse off, the fact that richer areas could afford better services would still increase inequality.	
12.7	SF pointed out that the idea of the postcode lottery is very familiar in relation to spending, but the debate is not often applied to taxation. He asked whether or not PJ thinks this must always be a bad thing, and asked for his opinion on the ability for local authorities to set their own business rates. PJ responded that there are clear benefits. At present, there is a disjuncture between tax decisions and local decisions, so a more local system would increase accountability and bring decision making closer to revenue raising. This does still lead to inequality, but this inequality may well be judged acceptable; in	

No.	Agenda item	Action
	some ways a heavy price is paid for the current levels of equalisation.	
12.8	JP asked what other benefits beyond accountability this might have. PJ said he believed that through incentivisation, which does not have to be a zero-sum game, local decisions could increase the size of the economy and therefore the tax base. London could bear a higher tax burden, compared to other parts of the UK such as Northern Ireland.	
12.9	BeR asked if financial devolution would be appropriate in London. PJ said that it is more difficult for London than it has been for Scotland because London's economy is so closely integrated with the South East. Some elements of devolved spending would work better than others. For example it would be feasible to run schools at the London level but it would be more difficult to run Higher Education here. It would be impossible to run health services at the London level as they are so integrated with the rest of the country.	
12.1 0	CD asked that if 'devo-max' is unfeasible in London, what might 'devo-mini' look like, with relatively small financial or taxation powers devolved 'around the edges'. PJ said that immobile taxes would work the best but there are no obvious candidates that stand out particularly. Overall, income tax, National Insurance Contributions and VAT collect the highest yields and he does not think a strong case exists for these to be devolved. The congestion charge works well in the London context (as congestion is a local problem and abundant local public transport is available) while it may not in other places, and it can be used as a policy lever as well as a way of collecting funds. A bed tax may be worth considering and alcohol duties could be devolved. On the other hand, PJ thinks it is inadvisable to devolve stamp duty because this tax is inherently flawed and damaging in the first place in that it discourages transactions. Regarding council tax bands, PJ commented that currently this tax is regressive and poorly designed. Simply revaluing properties according to 2012 values would increase revenue in London substantially (without the need for any form of devolution).	
12.1 1	TO posed the third set question: <i>in particular, regarding capital investment, do you consider that London requires greater financial autonomy to enable it to make effective investment decisions? How and in what regard? What implications would this have?</i>	
12.1 2	PJ responded that while this is not his area of expertise, it is not clear to him that any clear differences exist in this regard between London and the rest of the country. HMT has good reason to keep borrowing down due to concerns about indebtedness.	
12.1 3	TT asked if PJ thought giving London more freedom to invest would generate greater returns from investments, which would be better for London and for the UK. He responded that this would be the case, but it would remain the case even if HMT kept control (so it is not necessarily a matter that could be resolved through devolution). It is also true of projects in the rest of the UK, which have not been allowed to happen either because of the government's concerns about the overall fiscal situation.	
12.1 4	TT thanked PJ for appearing as a witness before the Commission.	
13	Ken Livingstone	
13.1	TT introduced KL. JP posed the first set question: <i>Do you consider that funding arrangements for the capital are too centralised (that is, at the national government level)? Why/why not?</i>	
13.2	KL answered that the current arrangements are indeed too centralised; they are the most centralised of all western democracies. This was not always the case. When KL was working in local government in the 1970s it had much more freedom to borrow alongside its government grant, but from 1971 constraints started to emerge on capital spending and in the 1980s absolute control was transferred to central government. The situation as	

No.	Agenda item	Action
	<p>it stands now depends entirely on the personal relationships the Mayor or local leaders can cultivate with Ministers. In KL's opinion, Ministers erroneously believe they have the capacity to run everything from Whitehall. In his opinion, central government should devolve all powers to local or regional government apart from macro-economic policy, foreign affairs and defence. As local government's competencies have diminished so dramatically, it no longer attracts the requisite talent.</p>	
13.3	<p>BrR asked for KL's opinion on the boundary of Greater London, itself a political artefact, which is very porous and sees a lot of commuters pass through it. KL replied that control over fares is a way the Mayor can decide to profit from in-commuters who benefit from London.</p>	
13.4	<p>SL commented that as council tax as it currently stands is considered by some as regressive, would KL advocate a local income tax or corporation tax? KL responded that he would prefer a local income tax or corporation tax (or a tax on local turnover to impede avoidance) to council tax, which he believes is severely regressive. However, while additional revenues are useful, the ability to control capital investment and make long-term investment in infrastructure is much more valuable than anything else, especially in light of the dramatic population increases forecast for the capital. The GLA Group should have the freedom to invest its pension funds in capital projects such as house building and Crossrail II and III.</p>	
13.5	<p>TT asked for clarification as to whether or not having greater control of a larger proportion of its own income would allow GLA to make decisions about investment over a longer period without the need to lengthily consult Whitehall. KL responded that when he was Mayor, most of his time was taken up with meeting, lobbying and building relationships with Ministers on a seemingly endless basis. This felt inefficient, especially given the high turnover of Ministers. The civil service were broadly hostile to doing anything.</p>	
13.6	<p>TT asked whether Mayors in other cities such as New York and Moscow had more decision-making powers. KL said that they do, and they are able to shift income and spending depending on economic cycles.</p>	
13.7	<p>SL asked why London cannot have more freedom over house building, when there is unlimited demand for it in the capital and severely limited supply. KL said that in the past, some considered it a problem that councils could build social housing in order to attract Labour voters to an area. However, KL does not think this would be the case any more, as voters move between parties and are not defined as much by social class anymore.</p>	
13.8	<p>Although KL had already spoken at length about capital investment, SA posed the final set question: <i>in particular, regarding capital investment, do you consider that London requires greater financial autonomy to enable it to make effective investment decisions? How and in what regard? What implications would this have?</i></p>	
13.9	<p>While KL does think London requires more freedom to invest in capital, he does not believe any government would allow this and the status quo of continued lobbying will remain. It is more likely government would devolve revenue streams and his advice would be to push for as wide a range of revenue streams as possible, and certainly to take anything offered by government.</p>	
13.1	<p>BeR asked if KL thought 'devo-max' for London might exacerbate existing inequalities in the UK. KL responded that London itself has the biggest inequalities in the country, so this kind of solution would give the Mayor a chance to redress what he considers a lamentable London-specific problem. He supports regional pay differentials as costs in London are extremely high (but he believes the effect of this should be higher pay in London, rather than lower pay elsewhere).</p>	

No.	Agenda item	Action
13.1 1	TT asked what the content of KL's recommendations to the Labour leadership would be for their next manifesto. KL said he would recommend the idea of house building (rather than infrastructure). He would consider the idea of giving London the power to access pension funds and to go to the bond markets, particularly because in KL's opinion public-private partnerships do not work as the private sector can get better returns elsewhere. TT commented that it must help to have greater freedom over revenue streams, as this indirectly allows local government to make capital investments.	
13.1 2	SL asked why KL thought several local authorities had opposed Crossrail. KL responded that this was because it took too long for a decision to be made by government. In KL's opinion, the Mayor should not have to go to Parliament for approval of London projects, as it severely delays any proposals and many MPs responsible for decisions have no connection to or interest in London (indeed, some display animosity towards it).	
13.1 3	TT asked KL what London government, including the boroughs, would look like if he could design it. KL said that around half of state spending would be incurred by Greater London (as is the case in German Laender). Education would be devolved to the London level and the Mayor would have oversight over health and social services. There should be five strong boroughs instead of 32 weak ones. The powers that borough councils have now are so diminished from the ones they were designed to accommodate that it no longer makes sense to have this many.	
13.1 4	TT thanked KL for appearing as a witness before the Commission.	