

PLAID CYMRU'S EVIDENCE TO THE INDEPENDENT COMMISSION ON FUNDING & FINANCE FOR WALES.

Plaid Cymru welcomes the establishment of the Independent Commission on Funding and Finance for Wales as part of the One Wales Agreement.

- Wales for much of the twentieth century has experienced economic decline compared with the rest of the UK: this was principally a consequence of the decline in traditional industries such as coal, steel, agriculture and slate quarrying. Wales has been funded through a block grant allocation distributed under the Barnett formula introduced in 1980. The formula, introduced only as temporary measure, takes no account of the disproportionate impact that this decline has had on Wales compared with the rest of the UK and the current funding formula not only reflects the spending needs and priorities of England but seeks to converge funding per capita across then four countries of the UK irrespective of the differing and diverging needs.
- In designing a funding mechanism for funding the countries of the UK a set of principles needs to be established.
 - The funds available should be related not only to need but to remediation of disadvantage
 - The Assembly Government should have some tax varying powers.
 - The Assembly Government should have borrowing powers.
 - The forum in which decisions are made regarding the allocation of funding to the four countries of the UK should be such that the governments of the devolved administrations have a key say in such decisions.
- The Barnett formula is both unfair and unsatisfactory and should be replaced. A detailed analysis of the strengths and weaknesses of the current formula is set out in an appendix to this submission.
- A set of proposals designed to ameliorate the unfavourable treatment of Wales under the current formula and an approach to replacing it with a more satisfactory system involving the establishment of an independent funding commission is included in this submission.
- Some fiscal powers should be granted to the Assembly Government which at present has responsibility for the expenditure of the block grant but has no responsibility for its size. This lack of accountability is a key weakness and the provision of tax varying powers would improve accountability and focus more attention on wealth creation in Wales.
- As part of fiscal devolution the Assembly Government should have borrowing powers within a prudential borrowing framework. Such a step would facilitate the planning and management of capital investment in Wales.
- To facilitate both borrowing powers and the ability to assume contingent liabilities the funding arrangements for the Assembly Government should be put on a statutory basis.

This submission will provide the background to the current position; propose the guiding principles for a fair and adequate funding mechanism; demonstrate the unsatisfactory nature of the current funding arrangements; and propose a set of measures to establish a more satisfactory approach. This submission will then propose tax varying and borrowing powers for the Welsh Assembly Government.

Introduction.

1. Plaid Cymru has a long record of opposition to the Barnett formula and welcomed the commitment of the Assembly Government, as part of the One Wales agreement, to establish a commission to review the funding and financing arrangements for Wales.
2. In economic terms Wales has long been a relatively poor country compared with other parts of the UK. The reasons for this are complex. Wales was slow to urbanise; was very dependent on an agricultural sector which suffered from a high proportion of poor quality, low productive land; and when industrialisation came it was concentrated initially on extractive industries with much of the added value being contributed elsewhere. Viewed from a UK perspective such specialisation may have made sense but it left Wales with an economy highly dependent on a few business sectors all of which suffered long term decline over much of the twentieth century (agriculture, coal, steel and slate quarrying). Although the Assembly Government is now making considerable efforts to strengthen and diversify the Welsh economy, most of the significant levers remain in the hands of Whitehall.
3. Thus Wales has the challenge of dealing with this legacy but during much of the last hundred years or more UK governments have regarded Wales as being on the periphery and have sought at best to ameliorate economic weakness rather than address the root causes. Since the implementation of the Barnett formula, which takes no account of relative need, GVA per capita has declined from 88 per cent of the UK average in 1978 to 78 per cent in 2007.
4. The way successive UK governments view Wales is reflected in the way that devolved services are funded: in particular both the formulation and operation of the Barnett formula reflect the peripheral status of Wales. Changes to the block grant are a *consequence* of spending decisions made with respect to spending departments in England. Indeed as is noted in the Treasury's Statement of Funding Policy 'in the vast majority of cases, the United Kingdom departmental programme covers England only' (this is further demonstrated in the next paragraph) yet it is decisions made by such departments that drive changes to the funding of Wales.
5. Out of UK total managed expenditure (TME) in 2007-08 of £590bn [1], the UK Government was directly responsible for:
 - non-identifiable expenditure for the UK (£108bn). This encompasses defence, interest on the national debt, cost of central government etc;
 - Social Security (£156bn) which is a standard, needs related UK wide set of programmes;
 - identifiable but non-devolved expenditure in Scotland, Wales and Northern Ireland (£3bn); and
 - all public expenditure in England (£243bn) excluding locally financed expenditure.
6. The devolved governments and local authorities of Scotland, Northern Ireland and Wales had responsibility for £60bn of expenditure.
7. Thus essentially the UK Government is, from a financial viewpoint, responsible for all public expenditure associated with the UK per se (central government expenditure including social security) and for all public expenditure in England. In addition it is responsible for a very small amount of spending on non-devolved, identifiable expenditure in the other three countries

[1] Pre Budget Report and Comprehensive Spending Review 2007. HM Treasury. Cm7227.

of the UK (£3bn) which is less than 0.5 per cent of TME. The UK Government has a dual role: it is responsible for central expenditure and it is responsible for all non-local authority expenditure in England. This duality is the source of many of the difficulties associated with the allocation of funding for devolved services in the other three countries of the UK.

8. In addition the UK Government is responsible for fiscal policy i.e. setting and collecting all taxes and duties in the UK with the exception of council tax and business rates. A third financial role is that the UK Government is responsible for macroeconomic policy including the setting of overall public expenditure levels in the UK and determining the level of public sector indebtednesses.
9. The Welsh Assembly Government:
 - a) is responsible for public expenditure on devolved services in Wales;
 - b) has no fiscal powers;
 - c) has no control over the amount of funding it has at its disposal for public expenditure; and
 - d) has no long term borrowing powers.
10. Of total identifiable public expenditure of £24.2bn in Wales in 2007-08, the Assembly Government and Welsh local authorities were responsible for £15.2bn. The balance of identifiable public expenditure was Social Protection (£7.5bn) and other programmes (£1.5bn) which were controlled by Whitehall departments [1].

Guiding Principles.

11. In reviewing the funding and financial arrangements for Wales we believe that certain principles should be agreed:
 - a) the funds available should be related not only to need but also to the remediation of disadvantage. Funding should be sufficient to enable the devolved administrations to address the underlying causes of any relative underperformance of the economy and its consequential social impact;
 - b) the Assembly Government should have tax varying powers;
 - c) the Assembly Government should have borrowing powers; and
 - d) the forum in which decisions are made regarding the allocation of funding to the UK and to its four member countries should be such that the governments of the devolved administrations have a key say in such decisions and the conflicted position of the UK government in its dual role as the government of the UK and of one of the four member countries of the UK should be recognised.
12. It is not sufficient to set funding levels in terms of relative need. It should be the objective of the UK Government to ensure that the devolved administrations have the means to address and materially reduce economic and social disparities between the member countries of the UK. The present funding arrangements appear, at best, designed to ameliorate the effects of economic and social disadvantage. It is noteworthy that in recent times the UK Government has to a marked extent abdicated to the EU its responsibility for the additional funding of disadvantaged areas. Even in the case of EU funding the UK Government sought initially not to pass on to Wales the EU Objective

[1] PESA 2008. HM Treasury. HC489.

1 funds but sought to treat these funds as part of Treasury receipts to be used for the benefit of the UK as a whole. The UK Government continues to refuse to provide additional funding over and above the Barnett determined increases for the purposes of public sector match funding. As a result the Assembly Government has had to use the block grant to provide its share of the matching funds for the Objective 1 and successor Convergence Funding programmes.

13. According to Eurostat 2008 Statistical Handbook the UK is the most regionally unequal country in the EU. In the case of the UK there is a factor of 3.9 between the two extreme values of regional GDP per capita. (The lowest values are in Sweden and Ireland where the factors are 1.6 and 1.5, respectively.) This outcome is indicative of the hitherto highly centralised nature of the UK state and of the failure of central government effectively to address the issue of regional disparities. The inevitable strain caused by this issue calls into question the continuing existence of the UK state.

Pros and cons of the present formula-based approach to the distribution of public expenditure resources to the Welsh Assembly Government.

14. The strengths and weaknesses of the Barnett formula have been the subject of much analysis and comment and the balance of independent and academic opinion has long been unfavourable. No doubt the Commission will receive many submissions drawing attention to weaknesses of the formula particularly from the point of view of its unfair and damaging impact on Wales over the last thirty years.
15. A summary of the strengths and weaknesses is set out here and covered in more detail in the appendix to this paper. It is in the context of the principles set out in paragraph 11 that the pros and cons of the formula are assessed.
16. In summary the weaknesses of the formula are:
 - a) the arbitrary setting of the baseline expenditures in 1978;
 - b) the inaccurate population ratios used between 1978 and 1997 to the detriment of Wales;
 - c) the application of the formula is not subject to independent audit;
 - d) it is a mechanistic rather than needs based formula;
 - e) it is an arbitrary convergence formula;
 - f) there is a lack of transparency in its application particularly with respect to the determination of comparability factors and the resulting consequential changes to the block grant;
 - g) the formula is driven by the public expenditure priorities of England;
 - h) no account is taken of the massive structural changes that have taken place in Wales since 1978 (e.g. the closure of the coal mining industry) – changes which were proportionately far greater in Wales than in England; and
 - i) it is an outdated formula whose operation does not reflect devolution and the existence of the National Assembly.
17. It is claimed that the formula has certain strengths:
 - a) the formula reduces the need for negotiation with the Wales Office and the Assembly Government;
 - b) the formula leads to predictable outcomes; and

- c) the way the formula operates in practice offsets Wales's weak negotiating position.
18. As noted all these points are developed at greater length in the appendix to this paper. It is our conclusion that the Barnett formula is unfair and inadequate and should be replaced.

Possible alternative funding mechanisms including the scope for the Welsh Assembly Government to have tax varying powers as well as powers to borrow.

Replacing Barnett.

- 19. It is clear from the above and our detailed analysis set out in the appendix that Plaid Cymru considers the current funding formula both unfair and unsatisfactory. We advocate a number of steps to reform and then replace the current formula. The first three steps proposed would be simple to implement but would not address the key weaknesses of the Barnett formula.
- 20. A useful first step, albeit a modest one, would be more clearly to identify within government reporting, expenditure by Whitehall departments which is for those services in England which in the case of the other three countries of the UK are devolved. This would enhance transparency and facilitate comparisons between the member countries of the UK. This would also reflect the recommendations of the Treasury-sponsored Allsopp Review.
- 21. A second step would be for the National Audit Office and the Wales Audit Office to review and report annually to Parliament and the National Assembly, respectively, on the operation of the Barnett formula. It is clear that many of the decisions made regarding the comparability factor of spending programmes are questionable and should be open to independent challenge (for examples see paragraph 6 of the appendix).
- 22. A third step would be to stop the Barnett squeeze by increasing the block grant to Wales by the same *percentage* as the corresponding increase in expenditure in England. In the absence of evidence to the contrary there is no justification for arbitrarily reducing relative identifiable public expenditure per capita on devolved services in Wales. Such a change would be a trivial modification to the current Barnett formula and would not increase total managed expenditure.
- 23. A fourth step would be to apply the principle that relative funding of services in the four countries of the UK should be related to relative need as is the case for intra-country distribution of funding. Need in this context would encompass remediation of disadvantage as set out in paragraph 11. Determination of relative need is of course a complex and potentially contentious subject. Given that expenditure on devolved public services is concentrated on health and education (approximately 70 per cent of the total) it is possible to formulate an acceptable needs model. Assessment of need is a challenge not unique to the UK and the Funding Commission should consider models employed in other countries with varying degrees of devolution. The additional funding needed to address remediation would be over and above the needs requirement.
- 24. An independent standing commission should be established which would either determine or advise on the allocation of funds to the four countries of the UK. Such a commission should be at arms length from the UK

Government in a similar way to the Monetary Policy Committee (MPC) of the Bank of England. The commission would:

- be given terms of reference unanimously agreed between the UK Prime Minister and the First Ministers of Wales, Scotland and Northern Ireland;
 - be advised by experts;
 - have an equal number of representatives drawn from each of the member countries of the UK;
 - have a suitably qualified secretariat to support the work of the commission together with an appropriate budget;
 - receive representations from interested parties;
 - commission appropriate external work to support the commission in its task;
 - as in the case of the MPC publish minutes of its meetings together with the evidence on which its recommendations are based; and
 - schedule its deliberations to fit in with the Spending Review cycle of the UK Government.
25. Some may object that the allocation of public funds is a political matter that is too important to delegate to a commission. A similar view was taken by many when the MPC was established ten years ago. At a minimum publication of the evidence gathered and considered by the commission, minutes of its deliberations and its recommendations would bring considerable pressure to bear on those charged with the allocation of funds to the four countries of the UK particularly if the recommendations of the commission were rejected.

Devolution of fiscal powers.

26. Another important step is for some fiscal powers to be devolved to Wales. A first stage would be to allocate all or some of the yield of certain taxes to Wales and then for the Assembly Government to have the power to set, in whole or in part, the rate of those taxes. This would be a desirable change because for the first time the Assembly Government would start to concern itself with income as well as expenditure: a vital connection if the Assembly Government is to be more accountable for the country's economic success and overall well-being. An important principle is that the block grant to the National Assembly should be unaffected by any variation to tax made by the Assembly Government.
27. In principle it is important that the Assembly Government has a measure of control over a number of different taxes rather than being reliant on one or two only. This is to ensure that the tax base is sufficiently wide and that action taken by the UK Government with respect to any one tax does not have too adverse an effect on the position in Wales. For example if Wales were to receive funds arising from income tax only then a decision made by the UK Government to reduce dependency on income tax and move the tax burden to indirect taxes could have an immediate and deleterious impact on revenues assigned to Wales. This would argue in favour of Wales being assigned some or all of the income arising from a number of the most widely based taxes such as income tax and value added tax. This would mirror to some extent the arrangements in Germany for example.
28. In 2006-07 identifiable public expenditure in Wales by the Assembly Government and local authorities totalled £15.2bn. Oxford Economics [1] has

estimated that in the same year total tax receipts that can be allocated to Wales were £19.3bn including £4.7bn from income tax, £3.6bn from National Insurance Contributions and £3.2bn from VAT. Thus taxes that can be allocated to Wales more than cover the total current budget of the Assembly Government.

29. Furthermore mechanisms for allocating these taxes should be fairly straightforward (the annual Budget Red Book published by the Treasury now includes an estimate of the yield to Scotland if income tax were varied by 3p). In the case of taxes such as corporation tax the position is more complex but nevertheless worthy of further consideration for economic development reasons.
30. An important principle is that if tax varying powers are employed by the Assembly Government in the shorter term the block grant should not suffer a corresponding increase or decrease otherwise the devolution of fiscal powers would be self-defeating.
31. In the short to medium term Social Protection should continue to be a UK wide programme with citizens being treated according to need in all parts of the UK. This reflects the common practice in many other unitary and federal states which have devolved government.

Borrowing powers.

32. As part of a move to fiscal devolution the Assembly Government should have borrowing powers within a prudential borrowing framework: after all local authorities already have such borrowing powers although their revenue raising powers are extremely limited. The Assembly Government should be able to raise money in the capital markets in a similar way to devolved administrations in other parts of the world. The rating agencies would take a view as to the credit worthiness of any such issuance of debt and this, in turn, would constrain the Assembly Government to prudent borrowing. In practice it is probable that the UK Government would wish to set further constraints or limits and this should be on the basis of the Assembly Government being able to have borrowing limits in line with its proportion of total UK public expenditure.
33. There is also potential for the Assembly Government to use its ability to assume contingent liabilities up to the value of the block grant. This enables the Assembly Government to provide guarantees to third parties under certain circumstances and could be used for funding of capital investment in the public sector.
34. In the case of borrowing powers and contingent liabilities it would greatly facilitate matters if the funding of the Assembly Government were placed on a statutory basis: this should be done.

Conclusion.

35. Plaid Cymru believes that the current funding arrangements for Wales are both unsatisfactory and unsustainable and should be replaced. Wales has suffered for far too long in terms of inadequate and unfair funding. The funding, borrowing and fiscal measures advocated in this paper would both lead to a fairer allocation of funds and ensure that the Welsh Assembly Government assumes increasing responsibility and accountability for the economic and social success of Wales.

[1] Winners and losers in UK public finances. Oxford Economics July 2008.

Appendix.

THE STRENGTHS AND WEAKNESSES OF THE BARNETT FORMULA.

- 1) It is in the context of the principles set out in paragraph 11 of our evidence that we will comment on the Barnett formula.
- 2) The Barnett formula suffers from a number of significant weaknesses as a mechanism for allocating resources to Wales and should be replaced. The origins of the Barnett formula are well understood: the formula was intended as a short term expedient introduced in the late 1970s as a means of allocating certain monies related to expenditure on functions devolved to Scotland, Northern Ireland and Wales. Lord Barnett himself has on numerous occasions in the House of Lords drawn attention to the fact that the formula was intended to be a short term, stop-gap measure. In practice it has remained in place with little alteration for over thirty years.

Weaknesses of the Barnett formula.

- 3) The Barnett formula has a number of weaknesses as well as one or two possible advantages. The first three weaknesses noted in this appendix (paragraphs 4 to 6) arise from faulty implementation whilst the remainder (paragraphs 7 to 14) are fundamental criticisms of the formula.

Arbitrary setting of base line expenditures in 1978.

- 4) Base line expenditures to which consequential increases were cumulatively added were themselves based on the expenditure patterns in existence prior to 1978: indeed in the case of Scotland allocations were partly related to the Goschen formula established in the late nineteenth century. Furthermore although the Treasury undertook a needs assessment exercise in the late 1970s the outcome was not used to alter the base line allocations used in the Barnett formula. This is in spite of the fact that the Treasury's assessment indicating that Wales was receiving less than its needs based share of funds and Scotland was receiving more [1]. An attempt was made by the Treasury in the early 1980s to resurrect the idea of a needs assessment in the case of Scotland and Northern Ireland but was abandoned.

Inaccurate population ratios used from 1978 to 1997.

- 5) The population ratios used in the application of the Barnett formula did not accurately reflect the respective populations of the four countries of the UK and in practice favoured Scotland and disadvantaged Wales. Thus the initial distribution of funding when the Barnett formula was implemented and the population basis for allocating increases were flawed from the outset. Until 1997 the population ratios were not, with one exception, adjusted to reflect changes in actual populations and this arguably further favoured Scotland, where the population was declining, and penalised Wales where the population was increasing broadly in line with that of England. Population ratios have been adjusted annually since 1997 but the way that Wales lost out in the intervening period of almost twenty years has been locked into the baseline to which subsequent Barnett formula increases have been added.

Application of the formula is not subject to independent audit.

- 6) The application of the formula is not subject to independent audit despite there appearing to be instances of incorrect and inconsistent application of the

[1] HM Treasury Needs Assessment 1979.

formula. Examples of this range from relatively small areas of expenditure such to more material ones. Expenditure on the Royal Botanic Gardens, Kew had a comparability factor was 100 per cent in 2004-05 but 0 per cent in 2007-08. The 2007-08 treatment implies that expenditure on Kew is for the benefit of the UK as a whole and this could well be the case but it ignores the fact that the Royal Botanic Gardens in Edinburgh and the National Botanic Gardens of Wales have a similar role but public funding for them has to be found from other programmes within the block grants. At a more material level is spending on the London Olympics; Crossrail, which has a comparability factor of 100 per cent; the Channel Tunnel Rail Link, which has a comparability factor of 0 per cent; and London & Continental Railways which has a comparability factor of 0 per cent. It appears that some of these decisions are either inconsistent or arbitrary.

A mechanistic rather than needs based formula.

- 7) A central weakness of the formula is that it is a mechanistic formula that does not take account of relative need except to the extent that such needs were reflected in the baseline expenditures in existence thirty years ago. For example there is significant evidence that relative needs have changed during the intervening period if measures such as relative GDP per capita or relative expenditure per capita on social protection are used as proxies for relative need. In the case of relative GDP per capita this has, in the case of Wales, declined from 88 per cent of the UK average in the late 1970s to 77 per cent in 2007 but this has had no influence on the Barnett formula determined increases to the block grant.

An arbitrary convergence formula.

- 8) Another objection to the formula is that it is a convergence formula: it is not passive. If the formula is applied rigorously, as it has been since 1997-8, then devolved, identifiable expenditure per capita will converge to the same level across the four countries of the UK. Expenditure *within* the four countries of the UK would not converge to a uniform level because different needs based formulae, are used to allocate such intra-country monies. Changes to other identifiable public expenditure programmes and in particular social protection is not subject to the Barnett formula and does not therefore suffer such convergence.
- 9) In the absence of needs assessment there is no cogent case for converging per capita public expenditure across the four countries of the UK. In the case of Wales the deterioration over the last thirty years in relative GVA per capita would suggest that identifiable expenditure should have increased in relative terms. Estimates have been published of the effects of the Barnett squeeze on Wales between 1999-00 and 2004-05 and show that the cumulative loss to Wales for that period was £1 billion [1]. To put this in perspective this is equivalent to a cumulative squeeze of 0.6 per cent per year of the block grant.

Lack of transparency

- 10) The absence of convergence in practice in the first eighteen years of the formula is a perverse example of the lack of transparency in the operation of the formula. Students of the formula have found it extremely difficult to explain why the convergence inherent in the formula has not been manifested in practice. This is particularly striking because for most of the period during which the formula has been in operation the changes in public expenditure used to determine changes in the block grant have been *nominal* changes

which should have accelerated convergence. It is assumed that there have been many examples of the so-called by-passing of Barnett in the period 1979 to 1997 although academics and others struggle to provide definitive evidence. It may be fair to surmise that the Barnett formula did not receive much government or public attention between 1979 and 1997 although recently released papers from the then Scottish Office show that the Treasury attempted unsuccessfully in the early 1980s to reduce the block grant to Scotland and Northern Ireland but not, significantly, to Wales. It was thus possible for governments of the day to deviate from the formula without much public attention being paid to such practices.

- 11) This lack of convergence was, of course, prior to the establishment of the Scottish Parliament and the National Assembly for Wales in 1999. It is also the case that in 1997 the incoming UK Government stated that it would apply the Barnett formula rigorously and this appears to be the case with a few, well documented exceptions. These include the provision of most of the EU sourced Objective 1 and Convergence funds to Wales being allocated over and above changes to the block grant determined by the Barnett formula. The UK Government also publishes a Statement of Funding Policy to coincide with each spending review and this casts additional light on the operation of the formula. However there appears to be no adequate means for challenging what appear often to be arbitrary decisions regarding comparability factors used in the formula.
- 12) It is inevitable that many adjustments will be made to planned and actual expenditure over the life of the Spending Review cycle. These changes will have an impact on the Barnett consequential but such changes are made by the Treasury and it appears that there are cases where that department is in practice 'judge and jury' without reference to the Assembly Government (see paragraph 18 of this appendix for a material example).

A formula driven by the public expenditure priorities of England.

- 13) The Treasury remains the driving force and key influencer in all cases of budgets including public expenditure plans. The allocation of funds to the devolved administrations is a *consequence* of spending decisions agreed between the Treasury and the various departments of state in London. In particular changes to expenditure on education and health *in England* represent approximately 70 per cent of the change to the block grant but in the case of Wales these programmes enjoy a high degree of devolution (100 per cent and 99.3 per cent, respectively). Thus spending decisions for England made by the Department of Children, Schools and Families and the Department of Health have a major influence on changes to the block grant to Wales despite the fact that policy-making in these portfolios is wholly devolved. The Assembly Government has minimal influence on policy making and, in particular, budgeting, by these Whitehall departments. Thus changes to the block grant are determined by departments of state which have little or no financial remit in the territories of the devolved parliaments and assemblies. Indeed with the exception of spending on social protection, there is a surprisingly small proportion of expenditure by UK government departments in Wales which have some responsibility for expenditure in Wales on non-

[1] Agenda. Institute of Welsh Affairs. Spring 2006.

devolved, identifiable expenditure. With the exception of social protection, £1.5bn only out of total identifiable expenditure of £24.2bn in 2007-08 corresponded to identifiable, non-devolved expenditure. To a large extent a number of UK departments of state are, from a financial viewpoint, departments for England only and yet changes to their budgets have a major impact on changes to the block grant directly impacting Wales and its citizens with little democratic input. Such a 'rough and ready' approach may have made sense as a short term expedient but it is not a satisfactory basis for the longer term which in the case of the Barnett formula has now been in force for thirty years.

A formula that takes no account of the massive structural changes in Wales since 1979.

14) Since the Barnett formula was introduced there have been massive structural changes in the Welsh economy such as the closure of the coal mining industry which have had a devastating knock-on social effect. These changes have proportionately been far greater in Wales than in England but the formula takes no account of this.

An outdated formula whose operation does not reflect devolution and the existence of the National Assembly.

15) The Barnett formula pre-dates the establishment of the National Assembly by twenty years but the approach remains the same and does not reflect the changes constitutional position of Wales. The Assembly Government has minimal influence on the funding of its activities and on the operation of the formula. The Joint Ministerial Committee has no formal role in the resolution of any disputes and the Secretary of State for Wales is in a weak negotiating position as a member of the UK cabinet which is dominated by the interests of England.

Advantages of the Barnett formula.

16) There are a number of arguments advanced in favour of the Barnett formula:
The formula reduces the need for negotiation with the Wales Office and the Assembly Government.

17) It is true that the formula reduces the need for the Treasury to negotiate with departments representing the devolved administrations. The counter argument is that there is a corresponding democratic deficit under the current arrangements. The Treasury is 'judge and jury' in its own case with little scope in reality for challenge. If the Assembly Government and its members are to be empowered to represent the electorate of Wales they must be able to negotiate with the UK Government in such a crucial area as funding.

The block grant permits the Assembly Government to have a high level of spending discretion.

18) An advantage of the block grant (as distinct from the Barnett formula per se) is that once the size of the block grant is determined it is to a significant extent a matter for the Assembly Government as to how the money is spent. It is possible that a detailed needs assessment approach to determining the block grant could undermine that freedom.

The formula leads to predictable outcomes.

19) Defenders of the formula argue that outcomes on a year to year basis are predictable which facilitates the annual budget planning of the Assembly Government. Recent evidence tends to undermine this claim. In the run up to the 2007 Comprehensive Spending Review (CSR) the UK Government made

a number of forward spending commitments in England including health and education. From those commitments it was possible to estimate the Barnett consequential for Wales for the three year CSR period: this indicated an average annual increase in real terms of approximately 2.6 per cent. When the CSR was published this gave an annual increase of 2.4 per cent. However the baseline expenditure on which the growth was based had been reduced due to postponement of certain health expenditures in England during the prior spending period. As a result the year on year real increase in the block grant was 1.8 per cent. It was clear from the comments of the Assembly's Finance Minister that this was unexpected as well as unwelcome.

Operation of the formula offsets Wales's weak negotiating position

20) Past evidence suggests that Wales has suffered compared with Scotland in the allocation of funds due to its weak negotiating position. One advantage of the current arrangement is that the Department of Children, Schools and Families and the Department of Health are powerful departments within Whitehall and Wales may indirectly benefit from such strength given the correlation between increases in spending in those departments and changes to the block grant. This may be true but it is hardly satisfactory that a democratically elected Assembly Government is not in a position to negotiate the funding settlement for Wales.

End.