Welsh Government response to recommendations from the Finance Committee's Report: Post-EU funding arrangements

The Welsh Government welcomes the Finance Committee's report on Post-EU funding arrangements. It is an important and timely contribution to the debate on this crucial issue as we believe the UK Government's approach is costing Wales jobs and growth and is a deliberate and unacceptable encroachment into a devolved policy area using the Internal Market Act (IMA) financial assistance powers.

Despite the UK Shared Prosperity Fund (SPF) first being announced in 2017, not a penny of replacement EU funding has reached Wales whereas new EU funding programmes would have started almost two years ago in January 2021.

In contrast, the Welsh Government had a framework for replacement EU funds already in place, the *Framework for Regional Investment in Wales*, which was co-developed over two years with the OECD and Welsh partners from local government, higher education, further education, businesses, other public and third sectors. The Framework was also subject to a full public consultation.

We accept all of the Committee's recommendations directed towards the Welsh Government. In regard to the Committee's recommendations 1, 2, 6, 8, 9, and 12-14, which are directed solely towards the UK Government, we are grateful for the Committee's ongoing support and for raising these. The Welsh Government will be very keen to see the UK Government's response to these recommendations and its future intentions, including the long-term replacement of EU funds beyond the end of March 2025.

Since the Minister for Economy and Minister for Finance and Local Government gave evidence in June, the Welsh Government has continued to raise its concerns, particularly in regard to the £1.1 billion loss of replacement EU funding, devolution not being respected and the allocation methodology applied, with a succession of Secretaries of State for Levelling Up, Housing and Communities, Chancellors of the Exchequer and Chief Secretaries to the Treasury.

The SPF was already underfunded, but the UK Government's Autumn Statement on 17 November means the overall value of the SPF for the UK has been reduced by £400m to £2.2 billion by the end of 2024/25. This again demonstrates a clear failure of the UK Government to deliver its Manifesto pledge to replace EU funds in full and is creating huge challenges for the Welsh economy.

The Welsh Government remains open to further dialogue with the UK Government which includes a discussion on SPF funding levels and allocations, together with the establishment of a genuine co-decision-making function for Ministers in order to improve the impact and value for money of the Fund in Wales.

In particular, the context has now changed and in light of the economic crisis and the hole in the public finances, consideration needs to be given to the future direction of the SPF, including the Multiply scheme, in order to achieve better economic outcomes. In Wales, EU funds previously supported critical pan-Wales programmes which are essential for productivity and growth such as Business Wales, apprenticeships, the Development Bank and our innovation programmes; yet under SPF arrangements the Welsh Government is being denied access to support these critical schemes.

We were able to work together more successfully on Freeports. We believe it is not too late for the UK Government to replicate this approach in the delivery of other UK funds and investments, including the SPF, so we can address long-term structural challenges and create a stronger, fairer and greener Wales.

Recommendation 1. The Committee recommends that, for future funds, the UK Government gives further consideration:

- to the time and resources required by local authorities to prepare bids;
- similar funding should be provided on the basis of need; and
- avoid a situation where time pressures influence the types of projects put forward.

Response: N/A for the Welsh Government

Recommendation 2. The Committee urges the UK Government to ensure the mechanisms around the Shared Prosperity Fund facilitate meaningful discussions with the Welsh and other devolved governments, in order to maximise the investment in Wales.

Response: N/A for the Welsh Government

Recommendation 3. The Committee recommends the Welsh Government clarify whether/how it will support the delivery of the Shared Prosperity Fund and what mechanisms it will use to ensure, as far as possible, funding is complimentary to other funding streams and policy in Wales.

Response: Accept

The Welsh Government’s position is clear that funding for devolved functions should come to the Welsh Government for Welsh Ministers to set priorities and strategic direction and be responsible and accountable for its administration and management. This will help avoid duplication of services, blurred accountability, poor value for money, sector funding gaps and an incoherent funding landscape where small amounts of money are spread thinly on short-term, localised projects.

If the UK Government is unwilling to support our position and agree a co-decision making role for the responsible Welsh Minister, then Welsh Government resources will not be used to help the UK Government implement its UK schemes operating in devolved areas.

The Welsh Government remains committed, however, to our partners in Wales who are under immense pressure due to sector funding gaps and unfeasible timescales for developing plans and projects and putting in place administrative and governance procedures.

This includes us continuing to hold regular meetings of the Strategic Forum for Regional Investment in Wales, chaired by Huw Irranca-Davies MS, to share information and lessons learned among Welsh partners across the public, private and third sectors. Meeting papers and minutes of this Forum are published here.

Recommendation 4. The Committee recommends that further information is provided by the Welsh and UK governments regarding the deprivation element of the distribution formula and how this was agreed.

Response: This recommendation is directed towards the UK Government and Welsh Government. The Welsh Government accepts its part in the recommendation.

The Welsh Government did not agree the Shared Prosperity Fund (SPF) distribution formula used by the UK Government.

The Welsh Government suggested a formula with a 70% weighting for need, based on the Welsh Index of Multiple Deprivation (WIMD), and a 30% weighting for population. The WIMD is a recognised, broad-based composite index covering a wide range of need indicators. The inclusion of an additional simple population element tends to even out allocations across areas and was intended to meet the UK Government’s expectation for a formula providing wide-spread allocations.

The UK Government’s published formula has a 40% population weighting, a 30% weighting for the WIMD, and a 30% weighting for its own Community Renewal Fund (CRF) index (the pilot fund to the SPF). Both the WIMD and the CRF index are composite indices underpinned by a wide range of underlying indicators, so this is a highly complex approach. The CRF index has a much greater weighting than the WIMD for indicators that tend to favour more rural areas.

The WIMD was included in the published formula in a way that does not weight for differences in population size between local authorities in Wales. As the Institute for Fiscal Studies has pointed out, this means that more populous areas receive less funding per person than areas with the same socio-economic profile but with smaller populations. There is no clear rationale for this approach. The UK Government has applied different methodologies in each country. Its own methodology note recognises the issue with the way WIMD has been included in the formula for Wales but says: “However, WIMD is only being used in Wales, where there are a smaller number of Local Authorities with smaller variations in populations”. In fact, Cardiff, the most populous local authority, has over six times as many residents as the local authority with the smallest population, Merthyr Tydfil.

The Welsh Government remains concerned about the published SPF allocation formula. For allocations in Wales, it is not clear why the UK Government’s CRF index should be given equal weighting to the widely used and accepted WIMD.

Recommendation 5. The Committee recommends that increased engagement takes place between the UK Government, Welsh Government and local authorities to clarify how the Multiply programme will operate in Wales.

Response: This recommendation is directed towards the UK Government, Welsh Government and local authorities. The Welsh Government accepts its part in the recommendation.

The Welsh Government, along with our partners in local government, remain concerned that the Multiply adult numeracy programme is too narrow in focus and will lead to duplication of provision. Under current UK Government proposals, it is not realistic to spend the Multiply allocation within the limited Shared Prosperity Fund (SPF) time period. Greater flexibility, including widening the scope of Multiply to cover digital and literacy skills and a guarantee that any Multiply underspend could support other SPF activities – including other national growth schemes like Business Wales and apprenticeships – is needed to help mitigate against waste, poor value for money and poor outcomes for individuals.

Welsh Ministers will continue to raise these concerns with the Secretary of State for Levelling Up, Housing and Communities and the Secretary of State for Education. We are also very keen for meetings around Multiply, involving relevant Welsh Government and local government officials, to be reinstated in Wales so we can work together to address the problems associated with the delivery of Multiply in its current form.

Recommendation 6. Given that education is a devolved area, the Committee is disappointed with the method of allocating funding through the Multiply programme and recommends that the UK Government provides flexibility to spend funds from the Multiply programme in other areas.

Response: N/A for the Welsh Government

Recommendation 7. The Committee recommends that the Welsh Government assess the Multiply programme and consider its existing funding commitments in this area, with the aim of avoiding duplication of other existing approaches and schemes.

Response: Accept

Skills is a devolved matter in Wales, but the UK Government has not given the Welsh Government any role in relation to Multiply. Instead, the UK Government has been clear that Shared Prosperity Fund Regional Investment Plans developed by local authorities should indicate how this ring-fenced funding will be used to implement Multiply in each local area.

The Welsh Government provides funding to the Regional Skills Partnerships (RSPs) to drive investment in skills by developing responses based upon local and regional need. The RSPs also have a key role in analysing and influencing provision to support regional growth. RSP board membership includes representatives from relevant economic sectors, education providers, local authorities, third-sector, employers, and industry representative bodies and so forth. As the RSPs are non-statutory, Welsh Government funding is paid to the Welsh Local Government Association (WLGA) which in turn issues contracts and funding to an accountable body on behalf of each RSP.

As the main vehicle in Wales to consider skills and employability delivery issues in their region the Welsh Government will ask RSPs to assess the implementation arrangements for the Multiply programme in each of their regional areas to help avoid duplication with existing schemes.

Recommendation 8. The Committee recommends that the UK Government provides further information on the team being established in Wales to operate the Funds, including the resources and staff to be deployed by the UK Government in Wales.

Response: N/A for the Welsh Government

Recommendation 9. The Committee recommends that the UK Government provide further information on the role and responsibilities of UK-wide ministerial forum that will support delivery of the Fund, as well as any other relevant engagement and responsibilities of the Welsh Government.

Response: N/A for the Welsh Government

Recommendation 10. The Committee recommends that the Welsh Government provides information as to how its officials will be involved in regional partnership groups and what role they will play in investment plan development.

Response: Accept

Four regional investment plans for the first year of the Shared Prosperity Fund (SPF) were submitted by Welsh local authorities by 1 August, and the UK Government was expected to approve these plans and make the funding available from October. While the Welsh Government has no decision-making role in the SPF, we are encouraged by the references local authorities have made in these investment plans to alignment with our *Framework for Regional Investment in Wales*, the Regional Economic Frameworks, and other Welsh Government strategies. The work and collaboration undertaken by local authorities during the summer has taken place against the backdrop of enormous pressure due to unfeasible timescales and reduced funding allocations imposed by the UK Government.

We have always been clear that we support the opportunity for national and regional approaches to allow for a more strategic consideration of where investment can best be targeted. In our *Framework for Regional Investment* a consensus was reached for Corporate Joint Committees (CJCs) to be the accountable decision-making body at the regional level to help deliver replacement EU funds. Four CJCs are now operational across Wales, and we would support the use of these existing structures as the governance vehicle for the delivery of the SPF. These could be supported by new, cross-sector advisory panels or partnerships whose governance are focussed just on the SPF and whose role would be to advise and support the CJCs in the agreement of SPF investment plans and interventions. We strongly believe that any SPF advisory panel or other SPF supporting partnership invitations should be extended to Members of the Senedd, and not limited to the UK Government's preference for Members of Parliament to be represented.

While we have made clear that we will not use our resources to implement UK Government policies that directly bypass the Welsh Government and Senedd, we are committed to our partners in Wales. We understand that local authorities are using different partnership approaches; for example, the South West Wales region is working through existing regeneration partnerships/boards in each LA area, as well as through monthly regional collaboration meetings. We will continue to maintain close working relationships with these and other partnerships including, for example, the CJCs and the regional skills partnerships.

As noted in our response to recommendation 3, we will also continue to hold regular meetings of the Strategic Forum for Regional Investment in Wales to share information and lessons learned, including on the SPF, among Welsh partners.

Recommendation 11. With the transition from EU funds to the Shared Prosperity Fund, the Committee recommends that the Welsh Government works with local authorities and stakeholders to identify any potential gaps and requests further information on the criteria and circumstances where the Welsh Government might intervene.

Response: Accept

We understand that the disruption, inflexibility and funding reduction is creating an extremely challenging situation for many organisations in Wales that have previously benefited from EU funds. Many sectors of the Welsh economy are now reporting redundancies and the closure of vital programmes in areas such as research and innovation, skills and support for vulnerable people.

This already unacceptable situation is exacerbated by the UK Government's ongoing delays to approving SPF investment plans and, as per the Autumn Statement, the decrease in the overall value of the SPF and local authorities being denied any spend of their SPF allocations in 2022/23.

The Welsh Government cannot plug financial gaps from the loss of more than £1.1 billion of replacement EU structural and rural funding. The Welsh Government has been denied access to the Shared Prosperity Fund (SPF), and we are already using funds from the last Welsh Budget to support pan-Wales schemes like Apprenticeships and Business Wales which are critical for productivity and growth.

We will continue to raise these concerns with UK Government Ministers, and we urge the UK Government to reconsider its approach especially in light of the economic crisis so value for money and economic impact is achieved. We are also in regular contact with the WLGA and local authorities to try and minimise as much of the disruption as possible caused by a SPF which is vastly reduced compared to EU funds and has no regard to devolution in Wales.

Recommendation 12. The Committee recommends that the UK Government increases flexibility to move Shared Prosperity Funds between financial years and between projects, similar to that offered through EU Structural Funds programmes. The Committee further calls for increased flexibility on how underspends will be treated.

Response: N/A for the Welsh Government

Recommendation 13. The Committee recommends that the UK Government provides clarity on its long-term plans for replacement EU funding and the status of the Shared Prosperity Fund beyond 2025. If it is to be replaced by a successor fund, the Committee recommends that relevant engagement needs to be taking place with stakeholders immediately.

Response: N/A for the Welsh Government

Recommendation 14. The Committee recommends that any successor to the current Shared Prosperity Fund:

- takes a longer term approach and is closer to the length of EU structural funding programmes than the current Shared Prosperity Fund; and,
- is aimed at creating growth and increasing GVA in Wales.

Response: N/A for the Welsh Government

Recommendation 15. The Committee recommends that an independent body assesses both the Welsh and UK government's claims around the levels of future funding and how this compares to previous EU funding.

Response: This recommendation is directed towards the UK Government and Welsh Government. The Welsh Government accepts its part in the recommendation.

We would be happy for an independent body to assess the Welsh Government claims around the levels of funding and how this compares to previous EU funding.

The Minister for Finance and Local Government issued a Written Statement on 4 May 2022, setting out the Welsh Government position and the loss of funding to

Wales as a result of the UK Government's arrangements for replacement EU funding.

Financial Implications: None

Recommendation 16. The Committee recommends that the Minister for Finance and Local Government reports back to the Committee on the funding issues discussed at the meeting of the Finance: Inter-ministerial Standing Committee.

Response: Accept

As set out in the inter-institutional relations agreement between Senedd Cymru and the Welsh Government, the Finance Committee and the Legislation, Justice and Constitution (LJCC) Committee are kept informed of all discussions at the Finance Inter-ministerial Standing Committee. This includes notifying the Committees of when meetings are due to take place, the agenda for discussion and a summary of the key points the Finance Minister intends to raise, as well as providing a readout from those discussions following the meeting. A joint four nations communique is also published after each meeting.

Recommendation 17. The Committee recommends that the Welsh Government provides further information on the dispute resolution position with the UK Government and when/how it might be used to resolve funding disputes.

Response: Accept

The joint Review of Intergovernmental Relations was published in January 2022. We have agreed to use the package of reforms which has emerged from the Review as the basis for the conduct of intergovernmental relations.

The reforms offer structures and processes to enable meaningful engagement, and a mechanism that affirms each government's right to refer and escalate a dispute.

It introduces more robust machinery, including a Council for heads of government, chaired by the UK Prime Minister, with an impartial secretariat, Inter-Ministerial Standing Committees – one covering intergovernmental relations as a whole and one focused on finance – to consider strategic or cross-cutting issues, and brings Ministerial engagement (quadrilaterals) within a robust framework, badged as Inter-Ministerial Groups (IMGs).

The proposed mechanism around dispute avoidance and resolution outlines each government's right to refer and escalate a dispute, including removal of barriers to raising disputes and requires independent chairing and independent secretariat arrangements. It includes a presumption of independent input, through either advice or mediation, and increased transparency to aid legislatures' scrutiny and stakeholder engagement.

As set out in the inter-institutional relations agreement between Senedd Cymru and the Welsh Government, the Committee will be kept informed of all discussions at F:ISC. This will include any intentions to formally invoke the dispute resolution process as set out in the Intergovernmental Relations review.

Financial implications: None.

Recommendation 18. The Committee recommends that the Welsh Government provides further information on the progress in resolving the issues that have been identified with other funding streams, including; Erasmus+, Horizon Europe and European Territorial Co-operation.

Response: Accept

The UK's association to the Horizon Europe programme is yet to be formally signed off by the EU. Since the Welsh Government's response to the Finance Committee in June, the UK Government has issued a statement covering the UK-EU Specialised Committee on Participation in Union Programmes consultations meeting held in September 2022.

With the ongoing delays to formalise UK association, the UK Government has also announced (1 September) an extension to its safety net for UK applicants applying to Horizon Europe. The guarantee only provides assurance for this year, covering Horizon Europe calls that close on or before 31 December 2022. The announcement included details published on 20 July on how the UK will transition to a new R&D programme if unable to associate to Horizon Europe, Copernicus and Euratom. This includes assessment by UKRI of Horizon applications that become ineligible and funding for participation as a third country to March 2025. The Welsh Government continues to engage with the UK Government on the association discussions.

The UK Government has decided not to participate in 2021-2027 European Territorial Co-operation programmes (other than PEACE Plus). Despite this, we are continuing to work closely with Devolved Governments to explore alternative ways in which our stakeholders might continue to engage in co-operation programmes through Third Country provisions in the EU Regulations, at the very least on a 'project-by-project' basis.

Our understanding is that, in principle, the European Commission (EC) has no objection to partners from the UK participating in 2021-2027 ETC programmes, on the basis that they bring their own finance; however, agreement from the UK Government would need to be secured to unlock participation. The EC has communicated its position to EU Member States and we are pressing UK Government to clarify its position on this matter.

The UK Government's decision means that it has not been possible to develop a successor Ireland Wales cross-border programme through the EU Framework; however, work is taking place to progress discussions and consider options to preserve gains made by the programme.

On Erasmus+, the Welsh Government will continue its delivery of *Taith*, Wales' international exchange programme. This £65m investment provides for all sectors and participants previously supported through the Erasmus+ programme. *Taith* is also helping to repair relationships across Europe that have been damaged by the UK Government's decision not to participate in Erasmus+. The Minister for Education and Welsh Language discussed *Taith* and Wales' exchanges with Europe at the European Parliament on 25 October 2022.

We also strongly believe it is crucial the UK Government does not reduce or remove their commitment to the Turing Scheme, the UK's global programme for studying, working and living abroad, which replaces some elements of Erasmus+.

Recommendation 19. The Committee recommends that the Welsh Government provides the financial projections relating to the remaining £795 million funding from the European Social Fund and European Regional Development Fund.

Response: Accept

This is a critical time for stakeholders in Wales as the EU funding programmes 2014–2020 draw to a close. The Welsh Government has fully committed all of the funding for the European Regional Development Fund (ERDF) and (European Social Fund) ESF programmes, and there are several projects which can deliver activities until the summer of 2023 and can claim expenditure for activities until the end of December 2023.

The delivery profiles of projects inevitably change throughout the course of the ten-year multi-annual programmes in order to address multiple factors, including changing economic and labour market conditions. For example, some activities, especially those supported through the ERDF, had to be paused during the global Covid pandemic. Generally, the ERDF supports more infrastructure type developments which have longer spend profiles and the ESF supports more revenue type activities that will claim funds more quickly.

The remaining ERDF and ESF programme spend in Wales is £619 million (as at 31 October 2022), with spend being on an upward trajectory since the Welsh Government's evidence to the Committee in June this year. During the next three months, based on current project spend profiles, we expect another £170 million of spend (based on a planning rate of £1: €1.17) to be claimed by stakeholders. However, we know that these financial projections will change and fluctuate significantly over the coming months and during the course of 2023. This will be because of exchange rate fluctuations and stakeholders trying to tackle head on additional external challenges including those created by the cost-of-living crisis, inflationary pressures, and the financial and economic crisis.

The Programme Monitoring Committee for the EU Structural Funds and Investment programmes 2014–2020, chaired by Mike Hedges MS, continues to monitor the progress of the programmes, including commitment and spend. The meeting papers are available at https://gov.wales/wales-programme-monitoring-committee. Data on the progress of the programmes is also available at [Progress of programmes: EU Structural Funds 2014 to 2020 | GOV.WALES].

Recommendation 20. The Committee recommends that the Welsh and UK governments publish the detail of the amount and profile of legacy funding that Wales is due to receive from the European Social Fund and the European Regional Development Fund.

Response: This is a recommendation directed towards the UK Government and Welsh Government. The Welsh Government accepts its part in the recommendation.

Under EU arrangements, EU funding cycles are multi-annual, i.e. covering ten years, and existing and new programmes overlap by two years. This means that new EU programmes would have started from January 2021, with WEFO able to award / commit funding from an entirely new funding allocation to new long-term, multi-annual projects while still paying existing projects from the 2014-2020 programmes for activities up until end of December 2023. For example, in the first year of delivery of the ERDF and ESF programmes 2014–2020, the Welsh Government announced some £370m committed to strategic investments, such as entrepreneurship and SME support packages via Business Wales and Apprenticeships and other legacy programmes. In contrast, the SPF is over three financial years (2022/23 to 2024/25), and it is now the end of 2022 and local government are still yet to receive confirmation of approval of their UK Shared Prosperity Fund (SPF) investment plans and the release of their funding allocations.

The slow build-up of funding for the SPF means that the allocation for Wales only matches previous annual EU funds by 2024-25. It is important to remember that EU programmes provide planning certainty over a ten-year period. Many of the larger projects in the current funding round, such as support to the development of South Wales Metro, were always planned to be at the back end of the programme period.

In contrast, there is no firm promise of replacement funding beyond the initial round of SPF. There is no UK Government commitment for the funding gap in earlier years to be filled in future, and this is why Wales and other parts of the UK are losing out. The loss of £1.1 billion of funding to Wales through the SPF is explained in the Welsh Government's written statement available [here]. Furthermore, the UK Government's Autumn Statement reduces the overall value of the SPF which will create even more pressures on the Welsh economy.

As part of its preparation for the 2021 UK Spending Review, HM Treasury requested our estimate of the tails of EU receipts for EU structural funds and for EAFRD (farm funding). The information provided in October 2022 ahead of this Spending Review will inevitably be a snapshot of something dynamic and reflective of the position at that time – the position now will be quite different as project spend profiles do change and fluctuate significantly due to a range of external factors as noted in our response to recommendation 19 above. The information was provided to HM Treasury with the caveat that Welsh Ministers fundamentally disagreed with any replacement EU funding methodology which involved netting off tails of EU receipts.