

# Quick guide

## First Report of the Independent Commission on Funding and Finance for Wales. (Holtham Commission)

August 2009

### 1. Introduction

The *One Wales* agreement<sup>1</sup> set out the commitment to establish a Commission to review how the devolved Wales is funded. In July 2008, the Office of the First Minister issued a press release announcing that Gerald Holtham is to Chair the Commission on Funding and Finance.<sup>2</sup>

#### Remit of the Independent Commission on Funding and Finance for Wales

The Commission was set the following terms of reference:

- Look at the pros and cons of the present formula-based approach to the distribution of public expenditure resources to the Welsh Assembly Government; and
- Identify possible alternative funding mechanisms including the scope for the Welsh Government to have tax varying powers as well as greater powers to borrow.

### 2. First Report of the Commission

The Commission published its first report, *Funding devolved government in Wales: Barnett and beyond* in July 2009.<sup>3</sup> This initial report assesses the Barnett formula, as it has been applied to Wales, and considers the case for change. It **concludes** that the Barnett formula:

...has no stated purpose other than getting a distribution done. In this it unquestionably succeeds. The purpose that can be inferred from its operation is to achieve the distribution with a minimum of public political conflict.

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<sup>1</sup> *One Wales: A progressive agenda for the government of Wales. An agreement between the Labour and Plaid Cymru Groups in the National Assembly. June 2007.* [on 31 July 2009]

<sup>2</sup> *Welsh Assembly Government Press Release, Chair of Commission on Funding and Finance announced, 8 July 2008.* [on 31 July 2009]

<sup>3</sup> *Independent Commission on Funding and Finance for Wales, First Report, Funding devolved government in Wales: Barnett and beyond (July 2009)* [on 31 July 2009]

It goes on to state that the fundamental flaw in the current system is that it **takes no account of relative needs** and that there is scope for significant improvement, and thus **the Commission has proposed**:

...a number of specific changes that would recalibrate the fiscal relationship between the Welsh and UK tiers of government, in a way that is appropriate to the post-devolution constitutional status of Wales. If implemented, our recommendations would improve the transparency and robustness of the current system, and would also enhance the ability of Welsh Ministers to allocate resources in line with Welsh priorities.

### 3. Principal report recommendations

#### 1. Ensuring funding is aligned with needs

The Commission recommend that funding arrangements for Wales should be based on relative needs. They recognise that the implementation of a needs-based system would '*face formidable political and practical hurdles*' and suggest that a conference of politicians and experts from across the UK would be required to settle the political issues. They go on to state that it is:

...essential that both the assessment of relative needs, and the mechanism by which funding would be aligned with needs, should be developed through mutual agreement and not through unilateral imposition of a Treasury decision.

The Commission recognise that developing and implementing a new system will take time. However, they recommend that immediate changes should be made, as the report calculates that Wales currently receives less than it would if it were funded using the formula as it applies to England. In order to avoid further convergence in Wales, they suggest a simple adjustment to the existing formula.<sup>4</sup>

#### 2. Enhancing the funding flexibility available to the Welsh Government

The Commission have made a number of recommendations aimed at improving the financial flexibility of the Welsh Government, specifically in relation to capital spending within their allocations

- **Managing capital budgets** - The Commission recommend that the Welsh Government should be allowed the flexibility to draw forward capital allocations over the course of a spending review period. This would help to 'smooth' capital budgets<sup>5</sup> and permit investment in a manner appropriate to Welsh circumstances.

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<sup>4</sup> Analysis within the report suggests that Wales would receive £114 (rather than the current £112) for every £100 spent in England, if it were determined by the English funding formula. A simple adjustment to avoid further convergence would be to multiply any positive increments allocated to Wales by 114 per cent; thus placing a floor under funding for Wales and preventing further convergence.

<sup>5</sup> Capital allocation via the Barnett formula tends to be variable from year-to-year as spending varies depending on the initiation or completion of large-scale projects in England from which Wales gets a consequential.

- **End year flexibility (EYF)** <sup>6</sup> - The Commission recommends that the Welsh Government should be able to access EYF funds without the need for discussion with and agreement from HM Treasury. This would further ease the problem of managing capital expenditure, and give Wales the freedom to ‘save’ consequential from large projects in England, without the need for negotiation with HM Treasury.
- **Moving funds from capital to resource budgets** - The Welsh Government (similar to UK Government departments) can move funds from resource to capital budgets. However, the reverse cannot be achieved other than in exceptional circumstances and requires the consent of HM Treasury. The Commission recommends that the Welsh Government should have the freedom to move funds from capital to resource budgets, providing that such transfers would not breach the UK Government’s fiscal rules.

If this were implemented, together with the ability to draw forward capital from future years, then the ability to move capital to resource budgets would apply only in years where no capital was drawn forward; thus ensuring that capital drawn forward is only used to fund additional capital investment over that provided via the Barnett formula. In effect, the Welsh Government could either draw capital from future years, or move resource into capital in order to fund investment, but not both.

### 3. Reducing the likelihood of future disputes

The Commission have recommended that the technical aspects of the Barnett formula’s operation should be administered by an independent advisory body that is at arms length from both the UK Government and the Welsh Government. This would ensure that the rules of the settlement were implemented fairly and reduce the likelihood of disputes arising.

The key reference document for the current arrangements is the Statement of Funding Policy.<sup>7</sup> The Welsh Ministers are consulted on the content of this Policy, but are not signatories to the document. The Commission concludes that this is inconsistent with the principle of mutual agreement between the devolved administrations and the UK Government, which should underlie the operation of devolution processes. Thus, the Commission recommend that the topics covered in the Statement of Funding Policy should be contained within a new Ministerial concordat that should be subject to joint approval of the UK and Welsh governments.

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<sup>6</sup> End year flexibility (EYF) – mechanism to carry over unspent provision from one year to later years. Ensures any underspend remains available rather than being returned to HM Treasury. Is subject to HM Treasury approval. For more information see the Members’ Research Service Quick Guide [End Year Flexibility](#).

<sup>7</sup> [HM Treasury. \*Funding the Scottish Parliament, National Assembly for Wales and Northern Ireland Assembly: Statement of Funding Policy \(October 2007\)\*. \[on 31 July 2009\]](#)

#### 4. Improving transparency

The Commission concluded that there is a lack of detailed and robust statistics making it difficult to analyse the impact of the Barnett formula. They recommend that the UK Government should produce an annual publication that would enable direct comparisons between Welsh Government expenditure covered by the Barnett formula and similar expenditure in England, thus enhancing the transparency of the process by which the Welsh Government is funded.

In addition to this, the Commission recommend that a Treasury Minister should be invited to attend the National Assembly's Finance Committee to discuss the funding made available to Wales, at least once in each spending review period.

Many of the conclusions and recommendations are in broad agreement with those of other reviews of the funding arrangements which have been recently conducted (see [Further Information](#)).

#### 4. Further work of the Commission

The Commission are now undertaking phase two of their review, which will concentrate on alternative funding mechanisms, including tax-varying and borrowing powers. To this end, the Commission has launched a second call for evidence.<sup>8</sup>

The Commission is due to report to the Assembly Government on the second part of its work in summer 2010.

#### 5. Further information

For further information on the Independent Commission on Funding and Finance for Wales, please contact Eleanor Roy, Members' Research Service ([Eleanor.Roy@Wales.GSI.Gov.UK](mailto:Eleanor.Roy@Wales.GSI.Gov.UK))

##### Useful Links

- Members' Research Service Quick Guide: [Barnett Formula](#)
- Members' Research Service: [The Barnett formula: funding the devolved administrations](#)
- Independent Commission on Funding and Finance for Wales: [First Report Funding devolved government in Wales: Barnett and beyond](#) (July 2009)
- Independent Commission on Funding and Finance for Wales: [Commissioned Research](#)

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<sup>8</sup> [Independent funding commission issues call for evidence on tax and borrowing powers for Wales](#) (on 31 July 2009)

- [Commission on Scottish Devolution](#) (Calman Commission) published their final report: [Serving Scotland Better: Scotland and the United Kingdom in the 21st Century](#) in June 2009
- [House of Lords, Barnett Formula Select Committee](#) published their final report [The Barnett Formula](#) in July 2009.
- Full list of [Quick Guides](#)

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