POST-EU REGIONAL DEVELOPMENT FUNDING

Submission to the Inquiry by the Welsh Parliament's Economy, Trade and Rural Affairs Committee

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Basis of the submission

The present note is submitted in a personal capacity in my role as an academic who has worked on many aspects of UK regional and local development. However, it is also informed by my other roles as National Director of the Industrial Communities Alliance – the all-party association of local authorities in the industrial areas of England, Scotland and Wales – and as Secretary to the Westminster All-Party Parliamentary Group on the UK Shared Prosperity Fund.

Overview

Under the banner of the UK Shared Prosperity Fund (UKSPF), the post-EU funding for regional development through until March 2025 is now in place. UKSPF funds have been allocated to local areas across the UK, including within Wales, and all the Investment Plans have been signed off. To all intents, what happens over the next couple of years is already fixed.

It is important therefore to focus on what might come next. The decisions on this would normally be revealed in the UK Government's next Spending Review, anticipated in the autumn of 2024. If there were to be a change in government at or around the end of that year, the new government would have a very narrow window to revise plans that would normally come into effect in April 2025.

The thinking about funding beyond March 2025 has already begun. In March this year the Industrial Communities Alliance, which represents local authorities in many of the areas targeted by EU funding and now by the UKSPF, adopted a number of recommendations. These are based on extensive discussion, including among local authority officers from around Britain, and form the core of the present submission. They apply to Wales as much as any other part of the UK. It would be especially helpful if the Welsh Parliament, and the Welsh Government, felt able to rally round this 'ask' of Westminster.

Controversies

It is appropriate, however, to begin by commenting on three controversial aspects of the transition to date in Wales from EU funding to the UKSPF.

The first concerns the **quantum of funding**. The UK Government say it is fully replacing EU funding to the regions. The Welsh Government, on the other hand, says that Wales has been seriously short-changed, to the tune of £1.1bn according to a written statement in December 2022 by the Minister for Economy. The Welsh Parliament's Finance Committee, in a report published in October 2022, argued that an independent body needs to assess these conflicting claims.

The truth is that both governments are right. The UK Government's figures refer to *spending in each financial year*, and it is correct that by 2024-25, when the still substantial legacy EU spending finally drops out of the picture, UKSPF funding of £1.5bn for the UK as a whole will broad match in real terms the annual average EU funding (ERDF and ESF) over the last spending round.

Where the Welsh Government is correct is that if the UK has remained within the EU we would at this stage have had a *financial commitment* to a much larger sum. Using the UK Government's figure of £1.5bn a year as a guide, this might have been worth £10.5bn over seven years to the UK as whole, compared to the actual allocation to the UKSPF of just £2.6bn over three years through to March 2025.

The second controversy concerns the **role of Welsh Government**. There has been a major change here. Under EU funding, the Welsh Government was centrally involved in decision-making, though within the tightly defined framework of EU priorities and the UK-wide plan agreed between London and Brussels. As the Welsh Government has repeatedly complained, the involvement of the devolved administrations in the development of the UKSPF has been minimal and the UK Government has allocated funding right down to local authorities.

Whether this greater involvement for local authorities is entirely a bad thing is something the Committee will wish to assess. However, it has not been without problems. No least, the fragmentation of UKSPF funding between so many authorities makes it difficult for organisations that operate across boundaries, or at the level of Wales as a whole, to find a meaningful way to engage. Welsh universities, for example, who previously received substantial funding for research and business development, appear to be among those losing out.

The third controversy concerns the **local allocation of funding**. As the Committee will be aware, a note produced by the Institute for Fiscal Studies (IFS) argued that the way in which the UK Government used the Indices of Deprivation in allocating UKSPF funding to local authorities within Wales was flawed. The UK Government used the *ranking* of each authority; IFS argued that this took no account of the *population* of each authority and therefore favoured some over others. The IFS argument is correct. The effect of this blunder has been to divert several millions to smaller Welsh authorities at the expense of larger Welsh authorities.

Looking ahead: context

In any discussion of the future of the UKSPF, a key factor the Welsh Parliament and Government need to bear in mind is that the UK Government says it intends to streamline levelling up funding. The UKSPF is of course an integral part of the wider package of levelling up funds.

This intention was flagged up in the February 2022 *Levelling Up White Paper*, repeated in the September 2022 *Growth Plan*, and again in the November 2022 *Autumn Statement*. Now that some of the levelling up funds, including the UKSPF, apply across the whole of the UK there is no reason to suppose that the commitment to streamlining does not apply to Wales.

Streamlining is welcomed by local authorities, especially in England where the multiplicity of funds has created overlapping objectives and a substantial administrative burden. In Wales, fewer UK Government funds apply – principally the UKSPF and the Levelling Up Fund – and the Welsh Government receives Barnett consequentials as a result of other levelling up spending, so there are fewer potential benefits.

Given the UK Government's intention to streamline levelling up funding, should the UKSPF simply be merged into a much bigger levelling up funding pot? Or should it be retained as a separate funding stream? For Wales, which has received approaching a quarter of all the UK's EU and SPF funding, it would certainly be a serious mistake to allocate the UKSPF via the Barnett formula.

The way forward

RECOMMENDATION 1: *The UK Shared Prosperity Fund needs to be maintained as a separate funding stream*.

Despite the substantial attractions of streamlining, in the context of the UKSPF there are serious drawbacks. The attractions of a separate UKSPF Tranche 2 are:

- It would visibly honour the political commitment to replace EU funding. If the UK had remained within the EU, the nations and regions of the UK would at this point have had guaranteed EU funding through until the end of 2027.

- In purpose and allocation, the UKSPF more closely aligns with the aim of regional and local economic development than any of the UK Government's other levelling up funds. The EU funds themselves were always intended to narrow the gaps in prosperity between local economies – arguably the core of levelling up.

- Unlike all the UK Government's other levelling up funds, which have been allocated by competitive bidding (or in the case of England's Towns Fund by invitation only) the UKSPF has been wholly allocated by formula.

- The allocation to date of the UKSPF strongly targets less prosperous local economies. The per capita allocation to Wales is almost twenty times greater than the per capita allocation to South East England. None of the other levelling up funds match this strong skew.

- It's difficult to see how a merger of the UKSPF into other levelling up funding streams would work in the devolved nations, where several of the present funds do not apply and where the devolved administrations also run their own programmes.

RECOMMENDATION 2: *Tranche 1 of the UKSPF is nevertheless imperfect, so there is a case for reform.*

- Local and regional economic development needs to be reaffirmed as the aim. The purpose of the Fund has been somewhat diluted – indeed the UK government now argues that the UKSPF "is not a direct replacement for the EU structural funds". It need not be a direct replacement in detail but promoting jobs, productivity and growth in less prosperous local economies should remain the key objective.

- The financial allocations in Tranche 1 are driven by out-of-date statistics. The UK government essentially replicated the 2014-20 allocation of EU funding to sub-regions, which means that by 2025 the underpinning data will be fifteen years old. To command confidence and support, the updating of statistics and associated formulas should be open to consultation and scrutiny prior to deployment.

- The duration of funding is too short. It is impossible to deliver transformational projects, especially capital spending, within just two or three years. Local players need early notification of financial allocations for planning purposes and longer timeframes for delivery.

- Funding should not be pre-emptively allocated to specific initiatives, as has been the case with the Multiply adult numeracy programme within UKSPF Tranche 1. It should be for local partners to identify local priorities. Nor should there be a specific requirement for matching finance.

- The devolved administrations should be fully involved in setting the strategic priorities and in the allocation and management of UKSPF funding. In contrast to previous practice, this has not been an integral element of Tranche 1 even though the devolved administrations are major players in their own economies.

As noted earlier, UKSPF funding presently builds up to £1.5bn a year in 2024-25, when legacy EU spending drops out of the picture. Beyond March 2025, to maintain the same level of spending would require an on-going UKSPF budget of £1.5bn a year, uprated for inflation. If the inflation adjustment were to be 20 per cent (not unreasonable perhaps), UKSPF spending from 2025 onwards would need to average at least £1.8bn a year, or £5.4bn over a three-year spending round.

This would still not be a full replacement for EU funding. Adding £5.4bn to the existing three-year allocation of £2.6bn would bring the cumulative UKSPF total to £8bn by 2027-28. As noted earlier, a seven-year EU funding cycle through to the end of 2027 would have been worth £10.5bn, plus a further adjustment for recent inflation of perhaps £1bn bringing the total to around £11.5bn.

The main reason for the gap (some £3.5bn) is that some of the EU funding would have been carried forward to pay for spending in the following years. Rolling forward spending in this way is hugely advantageous because it allows commitments to be made to major schemes that take time to deliver. It is an approach that should be adopted with the UKSPF. To match previous EU funding, an additional £3.5bn should therefore be earmarked in Tranche 2 for spending commitments running on beyond the end of the next spending round.

RECOMMENDATION 3: *If as part of streamlining it proves impossible to maintain a separate identity for the UKSPF, the way to carry forward as many benefits as possible would be to establish a 'minimum guarantee'*.

Under a 'minimum guarantee', all parts of the country would be guaranteed to receive not less from the UKSPF funding rolled into the levelling up pot than they would have received if the UKSPF had continued to operate as a separate funding stream.

In effect, this would be a 'fund within a fund' with its own allocation formula but all areas would be reassured that they would not be disadvantaged by the changeover to a streamlined funding system. In terms of spending, however, as part of a new streamlined pot there would presumably be local flexibility to move funding from one project to another within a broad framework of goals.

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