

LOCAL GROWTH FUNDS: THE CAPITAL/REVENUE SPLIT

Submission to the Economy, Trade and Rural Affairs Committee

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The new Local Growth Funds

The UK Government's new Local Growth Funds, due to come into operation in April, are to all intents the replacement for the UK Shared Prosperity Fund (UKSPF), which in turn replaced EU funding to the regions. The activities to be funded – infrastructure investment, business support and skills development – are the same, the new funds kick in as the UKSPF comes to an end and, like the UKSPF, the new funds are managed outside the Barnett formula.

The new funds' predecessors were cornerstones of UK regional development and strongly targeted at less prosperous parts of the country.

In the forthcoming three-year spending round (2026-29), £675m has been allocated to the new Local Growth Fund in England, £140m to the fund in Scotland and £547m to the fund in Wales. Compared to the UKSPF in 2025-26 these are all reductions – a 60% cut in England, 39% in Scotland and 13% in Wales – because the former UKSPF budget line is also being used to pay for the UK Government's Pride in Place neighbourhood initiative. In England, the reduced funding goes exclusively to eleven mayoral authorities in the North and Midlands, so their cut is less severe, but the flipside is that the rest of England faces a 100% cut.

The capital/revenue split

Cutting the budget is a political choice, but the truly inept proposal is to radically shift the capital/revenue split.

In Scotland, Wales and Northern Ireland, capital spending presently accounts for 26% of UKSPF expenditure. In the new Local Growth Funds the UK Government is imposing a 70/30 capital/revenue split from April 2026 onwards.

In England, capital spending presently accounts for 15-30% of UKSPF expenditure, depending on the authority. For the new Local Growth Fund, the government is imposing a capital spending share that rises through time to 58% in 2028-29. Unlike in the rest of the UK, the government also adds a fourth year's funding for 2029-30 that's 100% capital (though revenue spending isn't normally allocated that far ahead).

The consequences of the capital/revenue split

The revenue-funded activities supported by the UKSPF are mainly **business support, training, and employability schemes**, the latter intended to engage the economically inactive and bring down the benefits bill.

The proposed shift to capital spending takes a sledgehammer to these services, all of which match the UK government's mission to create growth and jobs and the vast majority of which take place in less prosperous parts of the country.

Thousands of jobs delivering these services are also put at risk. On the basis of data from a sample of authorities, it's estimated that in England 4,000 local authority jobs are presently directly supported by UKSPF funding, a further 1,500 in Wales and more than 500 in Scotland. Probably at least as many jobs are supported in Third Sector organisation delivering revenue-funded UKSPF services.

In addition, it's nigh-on impossible to deliver meaningful capital projects within the short timescale set by the new Local Growth Funds. It takes time to secure permissions and then to issue contracts, let alone to deliver on the ground. This was one of the painful lessons of the Johnson-era levelling up initiatives. It had been thought that the Treasury had taken on board this lesson because the 2025 Spending review said the government would establish *"a new local growth fund, including a 10-year capital settlement from 2026-27 to 2035-36"*. This commitment has clearly been overlooked.

The root of the problem

The absurd capital/revenue split now being imposed is rooted in an administrative adjustment.

In the 2021 Spending Review, when the UKSPF was first established, it was included as an independent budget line, separate from the mainstream budget for the then Department for Levelling Up, which managed the money. The capital/revenue split for the UKSPF was set at 12/88 for the three years through to 2024-25.

In the 2025 Spending Review, the former UKSPF monies were fully absorbed into the budget of the Ministry for Housing, Communities and Local Government (MHCLG), which was given a 70/30 capital/revenue split for the sum of its spending beyond England's Local Government Financial Settlement. This capital/revenue split has then been applied mechanically to the new Local Growth Funds in the devolved nations.

In England it's a little different because alongside the new Local Growth Fund the UK Government created a recyclable Mayoral Growth Fund worth £500m, which is wholly capital and partially offsets the larger percentage cut in funding that England would otherwise be facing. Add the two new English funds together however and over the three-years 2026-29 the capital/revenue split becomes 66/34, little different to in Scotland, Wales and Northern Ireland.

In the same way, a 70/30 capital/revenue split has been mechanically applied to the Pride in Place initiative, but unlike the new Local Growth Funds the Pride in Place initiative does not inherit a substantial body of existing services and jobs in need of financial support.

Who's to blame?

The proposed capital/revenue split for the new Local Growth Funds reeks of bureaucratic ineptitude and inertia.

MHCLG and the Treasury should have been aware of the activities currently supported by UKSPF monies and how they would be put at risk by the proposed capital/revenue split. Officials in both departments should also have been aware that prior to the 2025 Spending Review UKSPF monies were, quite sensibly, accounted for separately to the mainstream MHCLG budget and with a quite different capital/revenue split.

One of the problems here is that institutional memories within the civil service are exceedingly short. In the Treasury, for instance, the staff presently overseeing this area of MHCLG spending are two generations on from those involved in the 2021 Spending Review.

Ministers can't escape some of the blame – they should have spotted the consequences of the mechanical application of MHCLG's capital/revenue split. On the other hand, they would have had to be on top of the details and the key players (MHCLG Secretary of State, Communities Minister, Chief Secretary to the Treasury, Scottish Secretary) were all new in the September reshuffle.

The way out of the mess

The solution requires commonsense rather than additional spending.

In the context of the Local Growth Funds, the distinction between capital and revenue spending is meaningless. Training, for example, creates an asset for the labour market that might deliver benefits to the economy for forty years or more, longer than the lifespan of some bricks-and-mortar investments. Business support – advice, consultancy, marketing etc. – can be as invaluable as investment in machinery. It's all an investment in local economies and in growth and jobs.

The obvious way forward is to abolish the distinction between capital and revenue spending in local growth funding, or at the very least to return to the capital/revenue split that previously applied to the UKSPF. This may not be the way accountants in the Treasury see things but it's the sensible way their political masters need to proceed.

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