



COMMITTEE FOR FINANCE AND PERSONNEL

Jocelyn Davis AM Chair
Senedd Finance
National Assembly for Wales
Cardiff Bay
Cardiff
CF99 1NA

23 June 2015

Dear *Jocelyn*

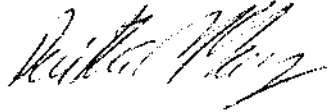
The Northern Ireland Assembly Finance Committee has been conducting a review of the operation of the Barnett formula. This has now concluded and I am pleased to be able to send you a copy of the Committee's report, which is attached for information. It is also available at the following weblink: <http://nia1.me/2nf>

As you will see from the report, we see scope for the devolved governments to work collaboratively on some of the issues relating to the devolution funding arrangements which need to be addressed. This would be especially timely in the context of the debate around wider constitutional reform and fiscal devolution. As such, I believe that the Committee's report, which was debated by the Assembly on Tuesday 23 June, will provide a useful contribution in that regard.

On a separate issue, the Committee and Finance Minister here have recently discussed the potentially disproportionate impact on regional economies which the British Government's austerity policy may be having. In that regard, it would be helpful to know what consideration has been given to this issue within the Welsh Assembly or Welsh Government. I would be grateful for any advice you can offer on this matter.

I look forward to our two committees liaising on issues of shared interest in the future.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Daithí McKay', written in a cursive style.

Daithí McKay
Chairperson
Committee for Finance and Personnel



Committee for Finance and Personnel

Report on the Review of the Operation of the Barnett Formula

Ordered by the Committee for Finance and Personnel to be printed 17 June 2015

This report is privileged and is the property of the Northern Ireland Assembly Committee for Finance and Personnel ('the Committee').

Neither the Report nor its contents should be disclosed to any person unless such disclosure is authorised by the Committee.

Embargoed until the commencement of debate in plenary.

Committee Powers and Membership

Powers

The Committee for Finance and Personnel is a Statutory Departmental Committee established in accordance with paragraphs 8 and 9 of the Belfast Agreement, Section 29 of the Northern Ireland Act 1998 and under Assembly Standing Order 48. The Committee has a scrutiny, policy development and consultation role with respect to the Department of Finance and Personnel and has a role in the initiation of legislation.

The Committee has the power to;

- consider and advise on Departmental budgets and annual plans in the context of the overall budget allocation;
- approve relevant secondary legislation and take the Committee Stage of primary legislation;
- call for persons and papers;
- initiate inquiries and make reports; and
- consider and advise on matters brought to the Committee by the Minister of Finance and Personnel.

Membership

The Committee has eleven members, including a Chairperson and Deputy Chairperson, with a quorum of five members. The membership of the Committee during the current mandate has been as follows:

Mr Daithí McKay (Chairperson)¹

Mr Dominic Bradley (Deputy Chairperson)

Ms Michaela Boyle²

Mrs Judith Cochrane

Mr Leslie Cree MBE

Mr Paul Girvan

Mr John McCallister^{3 4}

Mr Ian McCrea^{5 6}

Mr Adrian McQuillan

Mr Máirtín Ó Muilleoir^{7 8}

Mr Jim Wells^{9 10}

¹ Mr Daithí McKay replaced Mr Conor Murphy MP with effect from 2 July 2012

² Ms Michaela Boyle replaced Ms Megan Fearon with effect from 2 December 2013

³ Mr Roy Beggs replaced Mr Ross Hussey with effect from 23 April 2012

⁴ Mr John McCallister replaced Mr Roy Beggs with effect from 15 October 2012

⁵ Mr Ian McCrea replaced Mr David McIlveen with effect from 16 September 2013

⁶ Mr David McIlveen replaced Mr David Hilditch with effect from 1 October 2012

⁷ Mr Raymond McCartney replaced Mr Mitchel McLaughlin with effect from 6 October 2014

⁸ Mr Máirtín Ó Muilleoir replaced Mr Raymond McCartney with effect from 10 November 2014

⁹ Mr Jim Wells replaced Mr Peter Weir with effect from 18 May 2015.

¹⁰ Mr Peter Weir was a member of the Committee from 1 October 2012 until 18 May 2015

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List of Abbreviations and Acronyms

AME	Annually Managed Expenditure	NHS	National Health Service
BIICL	British Institute of International and Comparative Law	NI	Northern Ireland
CFP	Committee for Finance and Personnel	OBR	Office for Budget Responsibility
CIPFA	Chartered Institute of Public Finance and Accountancy	ONS	Office for National Statistics
DFP	Department of Finance and Personnel	PESA	Public Expenditure Statistical Analyses
EVEL	'English votes for English laws'	UCL	University College London
GVA	Gross value added	UK	United Kingdom
HM	Her Majesty	VAT	Value added tax
MBE	Member of the British Empire		
MOU	Memorandum of Understanding		
MP	Member of Parliament		

Introduction

Background and Purpose

1. In February 2012 the Committee for Finance and Personnel (CFP) received preliminary evidence from a panel of expert witnesses which indicated that, while historically the Barnett formula has provided generous funding to Northern Ireland, due to various factors, it is 'no longer a safe haven' and the point has been reached when it appears Northern Ireland 'will not do particularly well out of the Barnett formula in future' in terms of relative need.¹¹ Members subsequently noted the commitment made by the Conservative, Labour and Liberal Democrat Party Leaders in advance of the Scottish Independence Referendum that there would be a continuation of the Barnett allocation for resources (a commitment which appears to have been reaffirmed in the Conservative and Labour party manifestos for the General Election 2015¹²).
2. It was in this context that, on 24 September 2014, the Committee agreed the terms of reference¹³ for a review into the scope for improving the operation and administration of the Barnett formula, with a view to ensuring that the future needs of Northern Ireland are adequately met.
3. This review has several key objectives including:
 - examining how the formula has operated in allocating resources to Northern Ireland, including the extent to which public spending per head in Northern Ireland has converged with the average level of public spending per head in the UK;
 - considering the factors which could influence this convergence now and in the future;
 - exploring whether the formula should be supplemented with an additional mechanism to take account of relative need and economic circumstances in Northern Ireland;
 - examining concerns relating to the administration of the formula; and
 - specifying the issues which, if addressed, would support devolution in Northern Ireland by improving the future operation and administration of the formula.

¹¹ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/8-feb-2012-evidence-from-profs-trench-holtham-and-mclean.pdf>

¹² The Labour Party committed to maintaining the Barnett formula in Scotland and committed to ensuring that Wales must not be unfairly disadvantaged by the Barnett formula. <http://www.labour.org.uk/page/-/BritainCanBeBetter-TheLabourPartyManifesto2015.pdf>

The Conservative Party committed in its manifesto to retain the Barnett Formula as the basis for determining the grant to cover that part of the Scottish Parliament's budget not funded by tax revenues raised in Scotland as well as 'making the Welsh Government responsible for raising more of the money it spends so the Welsh people can hold their politicians to account.'

<http://docs.google.com/viewerng/viewer?url=http://static.guim.co.uk/ni/1429010009028/Conservative-Manifesto-2015.pdf>

¹³ <http://www.niassembly.gov.uk/assembly-business/committees/finance-and-personnel/review-of-the-operation-of-the-barnett-formula/>

4. To inform the Committee's deliberations, [written and/or oral evidence](#) was received from the following expert witnesses and stakeholder representatives between November 2014 and April 2015:
 - Professor Derek Birrell – Professor of Social Administration and Social Policy, Ulster University;
 - Alan Bermingham – Policy and Technical Manager, Chartered Institute of Public Finance and Accountancy (CIPFA);
 - Professor Paul Cairney – Professor of Politics and Public Policy, Department of History and Politics, University of Sterling;
 - Dr Graham Gudgin – Centre For Business Research, Judge Business School, University of Cambridge; Chairperson of the Ulster University Economic Policy Centre Advisory Board;
 - Professor David Heald – Professor of Accountancy, University of Aberdeen Business School, University of Aberdeen;
 - Professor Gerald Holtham – Academic, Cardiff Business School, University of Cardiff; Chairperson of the Independent Commission on Funding & Finance for Wales (also known as 'the Holtham Commission');
 - Professor Iain McLean – Professor of Politics, School of Politics, Oxford University;
 - Professor Colin Thain – Professor of Political Science, University of Birmingham; and
 - Professor Alan Trench – Hon. Fellow of Edinburgh University & UCL Constitution Unit, London.
5. In addition, the Committee commissioned research, which included a review of relevant literature¹⁴ and several members of the Committee visited Edinburgh in May 2015 to discuss issues of mutual interest with senior officials from the Scottish Government and with members of the Scottish Parliament's Finance Committee.
6. This summary review paper, which outlines the key issues arising from the expert evidence and signposts the reader to the source documents, is intended to inform a plenary debate by the Northern Ireland Assembly in June 2015. It is also anticipated that the evidence gathered, the review paper and the subsequent Assembly debate will inform the Department of Finance and Personnel (DFP) and the wider Executive in terms of any future developments in relation to the devolution funding arrangements for Northern Ireland and will also contribute to the wider UK debate in this regard.

How does the Barnett formula work?

7. In short, the Barnett formula is the mechanism used by the UK Government to allocate more than half of total public expenditure in Northern Ireland, Scotland and Wales. The formula has been used for the last thirty years to determine the annual increase (or decrease) in allocation. Each year, in the case of increases, the increments are added on to the previous year's allocation (the baseline) to create what is now a significant block grant of funds.¹⁵ The

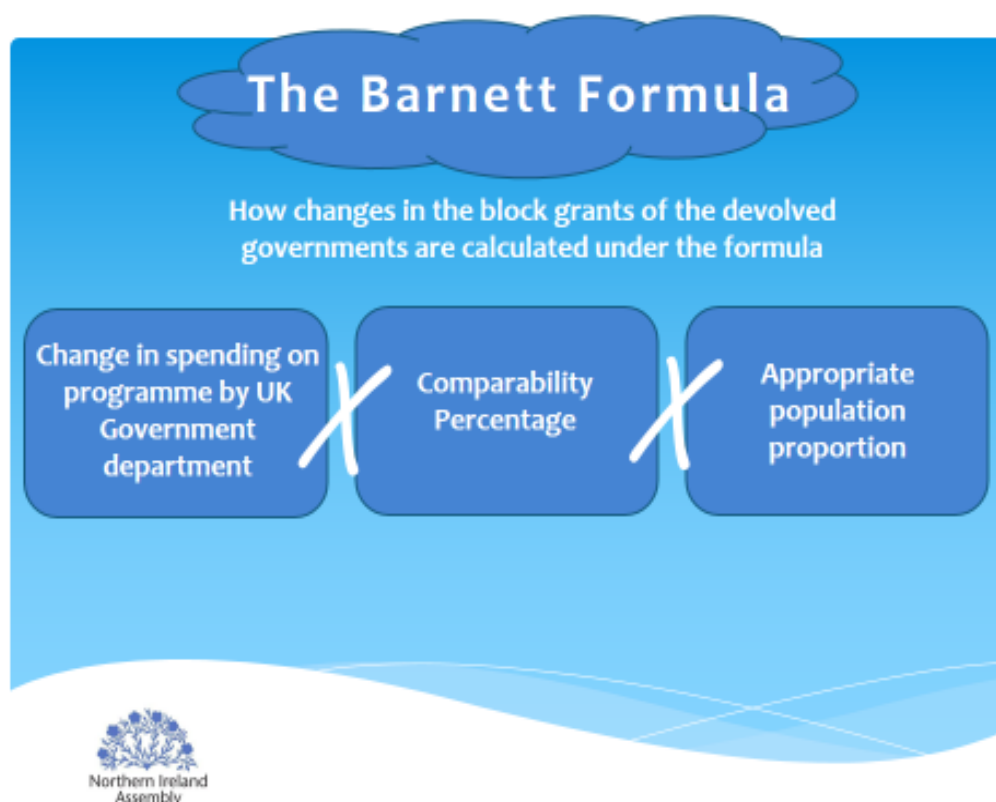
¹⁴ <http://www.niassembly.gov.uk/globalassets/documents/raise/publications/2014/general/11614.pdf> & <http://www.niassembly.gov.uk/globalassets/documents/raise/publications/2009/ofmdfm/4909.pdf>

¹⁵ <http://www.publications.parliament.uk/pa/ld200809/ldselect/ldbarnett/139/139.pdf>

baseline budgets of the devolved regions are historic, having rolled forward over the years, with the formula applying only in relation to changes and not the overall baseline expenditure.

8. The Barnett formula works on the basis of the calculation in Figure 1 and essentially provides the devolved governments with a population-based share of the change in planned spending by UK Government departments on comparable services in England, England and Wales or Great Britain (depending on the coverage of the expenditure considered). The comparability percentage relates to the extent to which services delivered by UK Government departments correspond to services delivered by the devolved governments. The product of the formula is known as the 'Barnett consequential' and determines the change to the block grant.

Figure 1



9. The Committee was reminded that, outside of the Barnett formula allocations, around 40% of Total Managed Expenditure is Annually Managed Expenditure (AME), which is agreed annually with the Treasury as it consists of demand-led programmes, mainly social security, including tax credits.¹⁶ In addition, there have been separate funding allocations, agreed as 'special packages', outside the Barnett formula, which are discussed at paragraphs 23 and 27.

¹⁶ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/d-birrell---review-into-the-operation-of-the-barnett-formula---march-2015.pdf>

10. More detailed information on how the formula works is available [here](#) and [here](#). More generally, the funding arrangements for the devolved governments, including the Barnett formula, are set out in HM Treasury's [Statement of Funding Policy](#).

Consideration of the Evidence

What are the pros and cons?

11. From the research and evidence considered as part of the review, it is clear to the Committee that strong arguments can be made both in favour of and in opposition to the Barnett formula. While not exhaustive, Figure 2 summarises the main points in this regard.

Figure 2



12. In his evidence, Professor Birrell pointed out that Treasury has had a long-standing commitment to the continuation of the Barnett formula for the following reasons:
- It can be applied simply and largely automatically;
 - It avoids direct annual negotiations over public expenditure between Treasury and the devolved administrations;
 - Its robustness as a mechanism for public expenditure allocation has been proven;
 - It is applied equally to each devolved jurisdiction;
 - It has minimised conflict between the four jurisdictions of the UK over spending levels;
 - It provides stable and largely predictable allocations without large fluctuations; and
 - It prevents the devolved governments from having to face many of the problems of revenue raising.¹⁷

¹⁷ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/d-birrell---review-into-the-operation-of-the-barnett-formula---march-2015.pdf>

13. In addition, when explaining the benefits of the Barnett formula in his evidence, Professor Heald highlighted the unhypothecated characteristic in terms of allowing devolved jurisdictions the discretion to make local decisions on the mix of spending and which ‘keeps Treasury off your patch’.¹⁸
14. Whilst acknowledging these benefits, the evidence indicated that the developing debate has also identified drawbacks of the Barnett formula. For example, the following concerns have been raised:
- It is not delivering an equitable share of funding between the devolved governments;
 - It does not take account of the relative spending needs across the UK and, while Northern Ireland has fared comparatively well under the formula to date, its needs may not be met in the longer term given the operation of the formula;
 - As devolution increases the calculations become more complicated, with the block grant needing to be amended to reflect the implications of any newly devolved fiscal powers;
 - There is a lack of transparency with the data used for calculations and with the basis for decision-making surrounding the formula;
 - Decisions can be taken arbitrarily by Treasury;
 - The formula is based on policy changes in England and, despite its unhypothecated nature, there can be a ‘tie-in’ to the model of public services in England;
 - Whilst the UK Government’s policy on protecting spending on Education and Health in England has provided some shelter to the Northern Ireland block grant from the impact of the more general austerity measures, this situation could change as UK Government spending priorities change, given the formula is based on English policy changes;
 - A ‘Barnett Flaw’¹⁹ can lead to anomalous outcomes, whereby the formula may not work in the way it was originally intended; and
 - It does not promote fiscal responsibility by the devolved governments in that a block grant in some amount is guaranteed under the formula regardless of what devolved government does and, for this reason, it is attracting political criticism from within England.
15. More information on the advantages and disadvantages of the formula is available [here](#).

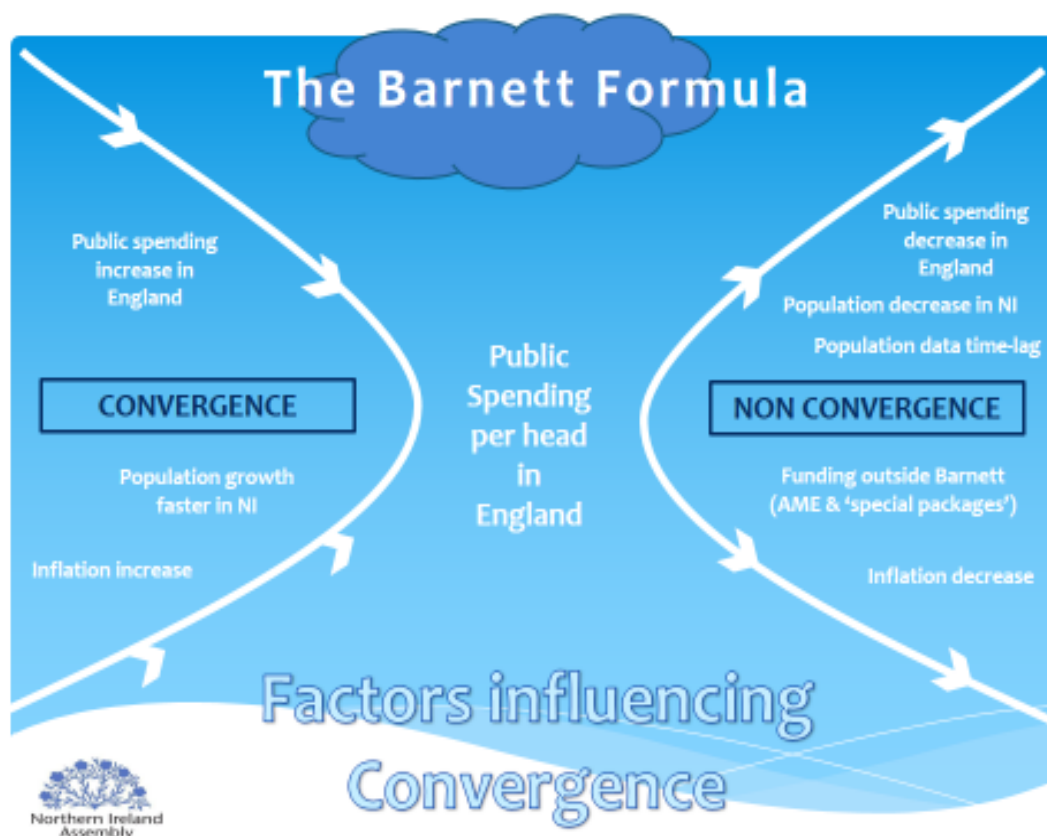
¹⁸ http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/150211_reviewofbarnettformula-prof-heald.pdf

¹⁹ <http://www.ifs.org.uk/publications/7444>
<http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/12-november-2014---further-evidence-from-professor-gerald-holtham.pdf>

What about convergence with public spending per head in England?

16. As part of the review, the Committee explored how convergence works, any evidence on the extent to which it has occurred for Northern Ireland to date and the factors influencing convergence. ‘Convergence’ refers to the coming together of per capita spending on comparable services in the devolved jurisdictions with that in England. As outlined in Figure 3, this can be influenced by various factors and the complexities in this regard were discussed in the evidence to the Committee.

Figure 3



17. In terms of how convergence works, the Committee noted research pointing out that the ‘logical conclusion of such a system is that relative public spending per head will converge on the English spending level’. This is sometimes referred to as ‘the Barnett Squeeze’ because the incremental spending change per head is the same and the effect of different per head starting levels in each of the devolved administrations will be eroded over time. It has been further argued that Barnett convergence ‘hastens during periods when public expenditure is growing above long term trend rates’.²⁰

²⁰ <http://www.niassembly.gov.uk/globalassets/documents/raise/publications/2009/ofmdfm/4909.pdf>

18. Professor Trench described convergence as ‘an arithmetical property of the Barnett formula’ and explained that:

*The Barnett formula allocates a version of spending changes that are made for England to a devolved Government, but it can never allocate to them more than 100% of what the changes are for England, even though the relative needs of all three devolved Governments are pretty clearly, as we know thanks to the Holtham commission's work, greater than those of England. So, convergence is something built into the system and ought to happen’.*²¹

19. While some of the evidence to the Committee indicated that convergence appears to have occurred in Northern Ireland to a certain degree, there was no clear consensus on the extent to which it has occurred. In terms of the general picture, Professor Heald indicated that convergence ‘unquestionably, seems to be happening in Northern Ireland’ and Professor Holtham suggested that this could lead to Northern Ireland ‘going below the level that needs-based formulae would give it once public funding starts to grow’²². Similarly, Professor Trench advised that convergence ‘appears to have bitten already to a material degree in Northern Ireland’ and Professor Thain agreed that ‘given long enough’ Northern Ireland will suffer as a result of convergence.²³
20. In his evidence in November 2014, Professor McLean highlighted that, in the last two years for which data is available, relative public spending per head in Northern Ireland has increased slightly. He concluded that there has not been a consistent trend towards convergence for various reasons, including: a reduction in comparable expenditure in England; a different population structure in Northern Ireland; time-lags in updating population data; and, a difference in social protection expenditure (most of which is outside the Barnett arrangements).²⁴
21. In addition, Professor McLean stated that: *the following make convergence more likely:*
- a. a large increase in spending in England on comparable services, e.g., the NHS;
 - b. an increase in inflation (because the Barnett mechanism works on nominal public expenditure, not adjusted for inflation);

²¹ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/12-november-2014---hansard-evidence-from-professor-trench-and-professor-holtham.pdf>

²² http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/150211_reviewofbarnettformula-prof-heald.pdf

<http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/12-november-2014---amended-submission---evidence-from-professor-alan-trench-and-preofessor-gerald-holtham.pdf>

²³ http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/150218_operationofthebarnettformulaprofthain.pdf
<http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/12-november-2014---hansard-evidence-from-professor-trench-and-professor-holtham.pdf>

²⁴ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/20-november-2014---written-submission-from-iain-mcclean.pdf>

c. *faster population growth in NI in any period before population numbers are re-calculated in the funding formula.*²⁵

22. In accepting that, in general terms, there has been a squeeze in Northern Ireland per capita spending over the last twenty years, Dr Gudgin pointed out that the factors influencing convergence can also work in reverse, whereby:

*If public spending is falling nationally then NI's share of that spending will tend to rise. This is what has been happening recently and it is why NI's share of UK Barnett "identifiable" spending per head has risen over the last 4 years*²⁶.

23. Moreover, Dr Gudgin also noted that convergence may be slowed due to special or 'top up' payments for Northern Ireland, such as the special package made by the then Chancellor Gordon Brown in 1999 and, more recently, under the Stormont House Agreement.

24. The Committee noted, in particular, the advice from Dr Gudgin that:

*The worst situation for NI would be if real spending was stagnant or falling while prices were rising. NI would then be hit twice, once by the real fall which would affect all regions and secondly by a falling share of national spending due to inflation.*²⁷

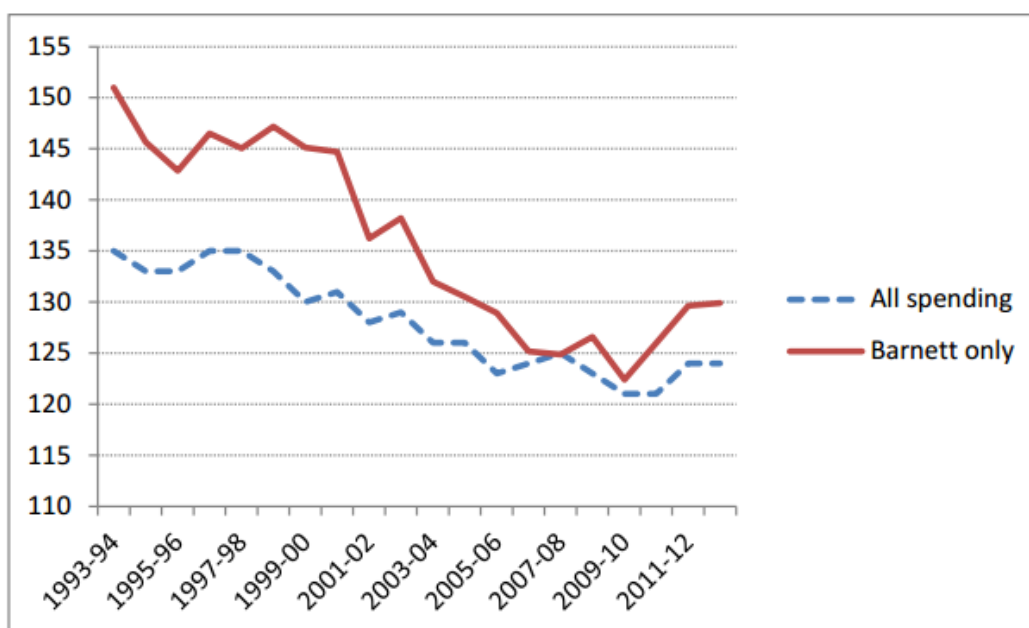
25. As illustrated in Figure 4 from Dr Gudgin's written submission, the Committee also noted the following pattern of public expenditure per capita in Northern Ireland, as compared to the UK average, since 1993:

²⁵ *ibid*

²⁶ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/28-january-2015---evidence-from-dr-graham-grudgin.pdf>

²⁷ *Ibid.* &

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/390673/Stormont_House_Agreement_Financial_Annex.pdf

Figure 4 - Public Expenditure per head in Northern Ireland (UK =100)²⁸

26. Similarly, in his written evidence to the review, Professor Holtham explained that:

The Barnett Formula causes convergence automatically whenever there is nominal growth in public spending. By the same token it generates divergence when spending falls in nominal terms.....The reason is simple. If spending in England goes up or down....where policy is devolved, the grant and hence spending in Northern Ireland also goes up or down.....This is not a problem when spending is falling so convergence has been less of a problem in the austerity era since 2010.....It becomes a problem when growth of public spending resumes.²⁹

27. In his evidence, Professor Birrell emphasised the importance of two forms of funding outside the Barnett formula having an influence over the expected move towards convergence specifically in the Northern Ireland context. Firstly, AME, which makes up some 40% of total managed expenditure and is demand-led and not subject to firm multi-year limits, includes social security which is not yet devolved in Scotland and Wales. Secondly, there have been instances of significant amounts of funding being provided outside of the formula, often associated with the unique post-conflict situation in Northern Ireland (e.g. funding for devolving Policing and Justice).³⁰ Similarly, the evidence from Professor Holtham and Dr Gudgin highlighted that changes in devolved responsibilities will affect convergence, depending on the logistics of the 'bargain struck'; while Dr Gudgin also concluded that any

²⁸ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/28-january-2015---evidence-from-dr-graham-grudgin.pdf>

²⁹ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/12-november-2014---evidence-from-professor-gerald-holtham.pdf>

³⁰ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/d-birrell---review-into-the-operation-of-the-barnett-formula---march-2015.pdf>

future reform of the system for allocating funding to the devolved governments ‘is likely to have to include “demand-led” spending within its remit’.³¹

28. Most of the expert witnesses advised that population changes will also have an impact on how the formula works and in turn affects spending and thus convergence. In his oral evidence, for example, Professor Holtham commented that *‘Barnett only works on the change: if your population is falling, your expenditure per head is being buffered and you are not subject to the Barnett squeeze’*³². In terms of the converse effect, Professor Trench, for example, stated that *‘population changes – an increase – may help explain the rapid decline in per capita spending in Northern Ireland in the 2000s, as well as an economic ‘peace dividend’ following the end of the Troubles.’*³³
29. The Committee noted a further consideration highlighted by Professor Cairney who pointed out that difficulties in understanding convergence arise because ‘it can only refer to an overall position but we can see some convergence in some policy areas, such as health, arising from a combination of the financial settlement and devolved government policy choices’.³⁴ Also, CIPFA highlighted the challenges which the shortcomings and inaccessibility of the data present when attempting to examine convergence.³⁵
30. More detailed information on the issue of convergence is available [here](#).

³¹ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/28-january-2015---evidence-from-dr-graham-grudgin.pdf>

³² <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/8-feb-2012-evidence-from-profs-trench-holtham-and-mclean.pdf>

³³ http://www.niassembly.gov.uk/globalassets/documents/raise/knowledge_exchange/briefing_papers/series3/alan_trench031013.pdf

³⁴ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/prof-paul-cairney-barnett-formula-sub-04032015.pdf>

³⁵ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/11-march-2015-written-submission-from-the-chartered-institute-of-public-finance-and-accountancy-cipfa.pdf>

What might influence future devolution funding arrangements?

31. The evidence to the Committee highlighted the potential for significant constitutional reform across the UK to have a bearing on the future operation of the Barnett formula and the wider arrangements for devolution funding and finance. The debate over UK constitutional reform is taking place against the backdrop of a growing number of studies calling for the Barnett formula to be replaced or supplemented.³⁶ The most recent of these, [A Constitutional Crossroads: Ways Forward for the United Kingdom](#) from the British Institute of International and Comparative Law (BIICL) has concluded that:

*The present Barnett formula governing funding arrangements for the devolved governments does not deliver equity between the various parts of the UK. It is not appropriate for the Union's decentralised constitution. The way forward is a grant mechanism based on clear criteria such as relative need with a discount for devolved tax raising powers and subject to periodic reviews.*³⁷

32. The Committee is also mindful that, while the three main UK-wide party leaders made a commitment that the Barnett formula will continue, it is unclear what this will mean going forward. This point has been highlighted by Professor Heald who previously questioned whether this might mean one or more of: the Barnett name being kept; the population-based adjustment mechanism continuing, whether or not in combination with needs assessment; and/or Scotland's level of per capita public spending being maintained.³⁸
33. Relating to the debate over constitutional reform, the Committee has noted several issues, as discussed below, which may lead to increased complexity and contention, and ultimately influence the future of the Barnett formula and devolution funding generally.

Fiscal devolution and block grant adjustment

34. The BIICL report has highlighted how 'fiscal devolution has been approached on a piecemeal and ad hoc basis' and that 'the difficulties that the Barnett formula poses at present will be aggravated by the way that further devolution will be implemented', in particular the calculation of associated block grant deductions.³⁹ This latter point was evident in the expert evidence to the Committee.
35. In their evidence, Professors Trench and Thain pointed to the implications of the further devolution of fiscal powers, potentially leading to diminished funds allocated through the

³⁶ <http://www.publications.parliament.uk/pa/ld200809/ldselect/ldbarnett/139/13902.htm>
<http://www.publications.parliament.uk/pa/cm200809/cmselect/cmjust/529/52902.htm>
<http://www.commissionsscottishdevolution.org.uk/>
<http://gov.wales/docs/icffw/report/100705fundingsettlementfullen.pdf>

³⁷ http://www.biicl.org/documents/593_bingham_report_constitutional_crossroads.pdf

p.xiii

³⁸ <http://www.scottish.parliament.uk/parliamentarybusiness/CurrentCommittees/87349.aspx> p. 5

³⁹ http://www.biicl.org/documents/593_bingham_report_constitutional_crossroads.pdf

p.43

Barnett formula and to increasingly notional deductions from the block grant.⁴⁰ On this latter point, Professor Trench argued that:

*it will become increasingly hard to identify what the growth of the devolved tax base would have been absent tax devolution, not least because there will be behavioural changes.*⁴¹

36. In terms of the impact of corporation tax devolution on the Northern Ireland block grant, Professor Trench also pointed out that the cut would need to be adjusted in subsequent years.⁴² In his evidence, Professor Heald urged caution over how the regional adjustment will be calculated and how that abatement will be revalued as the years pass, with the possibility of a large transfer of risk to the devolved jurisdiction.⁴³
37. For its part, CIPFA held that the debate is ‘potentially coming to a head’ because the Barnett formula and further devolution of fiscal powers do not sit well with each other, including in terms of the inequity of devolved jurisdictions retaining their own tax revenues whilst at the same time receiving a disproportionate amount of tax revenues from taxpayers in the rest of the UK. It was the view of CIPFA that ‘the more you move towards fiscal autonomy, the more you need a needs-based approach’ and that ‘increasing pressure on further devolved powers as a result of the Scottish referendum will probably make the Barnett formula even more irrelevant and archaic in its operation.’⁴⁴
38. Other evidence, including the briefings from Professors Holtham and Cairney, also recognised the impact of fiscal devolution on the Barnett formula, though its continued role in determining the block grant was acknowledged. In his evidence, Professor Birrell pointed to the possibility of pressure being placed on Northern Ireland to consider income tax powers given moves to devolve powers in this area to Scotland and Wales.
39. From previous DFP evidence to the Committee, it had been noted how the detail of the Treasury calculations over corporation tax devolution had not been shared with the

⁴⁰ http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/150218_operationofthebarnettformulaprofthain.pdf
<http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/12-november-2014---hansard-evidence-from-professor-trench-and-professor-holtham.pdf>

⁴¹ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/12-november-2014---hansard-evidence-from-professor-trench-and-professor-holtham.pdf>

⁴² <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/12-november-2014---hansard-evidence-from-professor-trench-and-professor-holtham.pdf>

⁴³ http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/150211_reviewofbarnettformula-prof-heald.pdf

⁴⁴ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/cipfa---operation-of-the-barnett-formula-29.04.15.pdf>

Department.⁴⁵ Similarly, arising from its visit to Edinburgh, the Committee noted that concerns about a lack of transparency in relation to block grant adjustments have also been raised in the context of further fiscal devolution in Scotland. This was highlighted, for example, in a recent [report](#) by the Scottish Parliament's Finance Committee which has also recommended that 'sufficient time is made available to allow effective parliamentary scrutiny of adjustments to the block grant prior to implementation'.⁴⁶

40. The Committee noted that it is still unclear what implications might flow from the 'no detriment' principle contained in the [Report of the Smith Commission for further devolution of powers to the Scottish Parliament](#), which was published in November 2014 and which the Scotland Bill 2015 aims to implement. The lack of clarity includes whether the 'no detriment' principle will be applied across the devolved jurisdictions. According to the principle:

*Where either the UK or the Scottish Governments makes policy decisions that affect the tax receipts or expenditure of the other, the decision-making government will either reimburse the other if there is an additional cost, or receive a transfer from the other if there is a saving.*⁴⁷

41. The practical outworking of this on block grant adjustments could undoubtedly become complex and contentious, and the question arises as to whether it will apply in respect of corporation tax devolution in Northern Ireland. On this latter point, the Committee has previously raised concern that Treasury has not yet agreed to mitigate the costs to the Northern Ireland block grant from reducing the corporation tax rate against associated benefits accruing to the UK Government from increases in other tax yields, including income tax and VAT. This concern was also highlighted in the evidence from Dr Gudgin.⁴⁸
42. A related issue noted during the Committee visit to Edinburgh was the suggestion raised in evidence to the Scottish Parliament's Finance Committee that the UK Government was seeking to include a 'constraining factor' within the block grant adjustment, which would forecast the yield from devolved taxes up to about 2030 and adjust the block grant accordingly so that neither the UK Government or the Scottish Government would be better or worse off. This was criticised as defeating the point of devolving the taxes.⁴⁹

⁴⁵ <http://www.niassembly.gov.uk/assembly-business/official-report/committee-minutes-of-evidence/session-2011-2012/march-2012/corporation-tax--departmental-briefing/>

<http://www.niassembly.gov.uk/assembly-business/official-report/committee-minutes-of-evidence/session-2011-2012/june-2011/committee-for-finance-and-personnel---devolution-of-corporation-tax/>

⁴⁶ <http://www.scottish.parliament.uk/parliamentarybusiness/CurrentCommittees/87349.aspx> p. 7

⁴⁷ http://www.smith-commission.scot/wp-content/uploads/2014/11/The_Smith_Commission_Report-1.pdf
para 95(4)(a)

⁴⁸ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/28-january-2015---evidence-from-dr-graham-grudgin.pdf>

⁴⁹ <http://www.scottish.parliament.uk/parliamentarybusiness/CurrentCommittees/87349.aspx> pp. 8 – 9

‘English Votes for English Laws’

43. As part of its evidence gathering, the Committee also explored the potential implications for the Barnett formula from the proposals in relation to ‘English votes for English laws’ (EVEL) in the Westminster Parliament – essentially giving English MPs the opportunity for enhanced scrutiny and a veto over new legislation applying to England.⁵⁰ Discussion included the potential for this reform to have a bearing on spending allocations to the devolved regions, as any law which includes either increased or decreased spending in England would have a direct knock-on effect on Northern Ireland, Scotland and Wales under the Barnett formula. As such, it was considered that this could potentially lead to some controversial decisions about what constitutes ‘England-only’ laws.
44. Various of the expert witnesses expressed concern with the implications of this potential reform, which was reflected in the following comments by Professor Heald:

*there is a very serious danger that the English-votes-for-English-laws issue is going to disrupt the system quite seriously. When one country is 84% of the whole, there is not such a thing as an English law. Anything that is subsequently going to affect the funding of Scotland, Wales and Northern Ireland is not solely an English matter.*⁵¹

45. The BIICL report has outlined the complexities around this issue and has suggested potential solutions, including changes in the way legislation is framed and ‘separating decisions about policy from those about finance’ at Westminster.⁵² However, uncertainty remains as regards what, if any, implications EVEL might have for devolved funding arrangements.

Devolution within England

46. A further consideration around constitutional reform identified in the evidence was what, if any, implications there might be for the Barnett formula and wider funding arrangements from devolution within England. While some of the expert witnesses questioned whether there is significant demand for devolution in England, the precise nature and timing of any such reform was still unclear when the Committee was taking its evidence.
47. Members noted from Assembly research, however, that, in May 2013, the London Finance Commission had called for greater fiscal autonomy for the UK capital city and, in October 2014, the City Growth Commission made a case for decentralisation to cities of a range of

⁵⁰ <http://webarchive.nationalarchives.gov.uk/20130403030652/http://tmc.independent.gov.uk/report-of-the-commission-on-the-consequences-of-devolution-for-the-house-of-commons/>
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/387598/implications_of_devolution_for_england_accessible.pdf

⁵¹ http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/150211_reviewofbarnettformula-prof-heald.pdf

⁵² http://www.biicl.org/documents/593_bingham_report_constitutional_crossroads.pdf
pp. 26-31, 45

policy remits.⁵³ More recently, the Committee noted the new UK Conservative Government's announcement of a '[Cities and Local Government Devolution Bill](#)' to provide enhanced devolved powers to large English cities which choose to have elected mayors, in areas such as economic development, transport and social care.⁵⁴ This has led the English Local Government Association to call for the decentralisation of powers to be extended to non-urban areas.⁵⁵

48. It is still too early to say what, if any, impact devolution within England may have on the wider devolution funding arrangements. However, the Committee has noted, in particular, the question over whether devolving such policy remits within England (which are already devolved to Northern Ireland, Wales and Scotland) could impact on Barnett consequentials as a result of associated reductions in the expenditure of the applicable Whitehall departments. The question also arises as to what further complexities could result from significant fiscal powers being devolved in England in the future.

'Tie-in' to English model

49. In his evidence, Professor Trench argued that, with the Barnett formula calculation and the basis for the attribution of funding, there was an implicit tie between the devolved regions and public services in England. He illustrated this point during oral evidence with an example in respect of higher education and the university fees in England, and stated that:

The Barnett formula, because it delivers changes in spending according to decisions that are made about spending in England, contains within it an implicit assumption that devolved Governments will, broadly speaking, be happy with the overall pattern of public services in England. If you dramatically alter the pattern of spending in England, that feeds through the block grant.⁵⁶

50. While it was accepted that the devolved governments are not tied into the same expenditure pattern as England as they have discretion over how they spend the grant allocated through the formula, the point was specifically about the funding ramifications from decisions about spending in England.⁵⁷ A further illustration which the Committee noted was the scenario of a Westminster Bill to remove NHS funding from general tax

⁵³ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/research-papers/research-paper-658-14---the-barnett-review-update-2014.pdf>

⁵⁴ <https://www.gov.uk/government/speeches/chancellor-on-building-a-northern-powerhouse>

⁵⁵ http://www.local.gov.uk/web/guest/media-releases/-/journal_content/56/10180/7295886/NEWS

⁵⁶ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/12-november-2014---amended-submission---evidence-from-professor-alan-trench-and-preofessor-gerald-holtham.pdf>

⁵⁷ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/12-november-2014---hansard-evidence-from-professor-trench-and-professor-holtham.pdf>

revenues, which would have far-reaching financial implications for the devolved governments; a consideration which is all the more pertinent in the context of EVEL.⁵⁸

51. In his evidence, Professor Thain similarly highlighted the funding risks for Northern Ireland (and Wales) from trends in policy-making in England, including in terms of increased privatisation and contracting out of services. He stated:

*Convergence to England means convergence to England; by the back door or by the front door, it means that all decisions taken in England will eventually seep through to the constituent parts of the United Kingdom. I do not think that that is consistent with the spirit of devolution...*⁵⁹

52. **In summary, the Committee believes that the aforementioned issues have the potential to further complicate the existing devolution funding arrangements and lead to disputes between the devolved governments and the UK Government, which could act as a further impetus for more thorough-going reform of the fiscal framework governing devolution across the UK.**

⁵⁸ http://www.biicl.org/documents/593_bingham_report_constitutional_crossroads.pdf

p.31

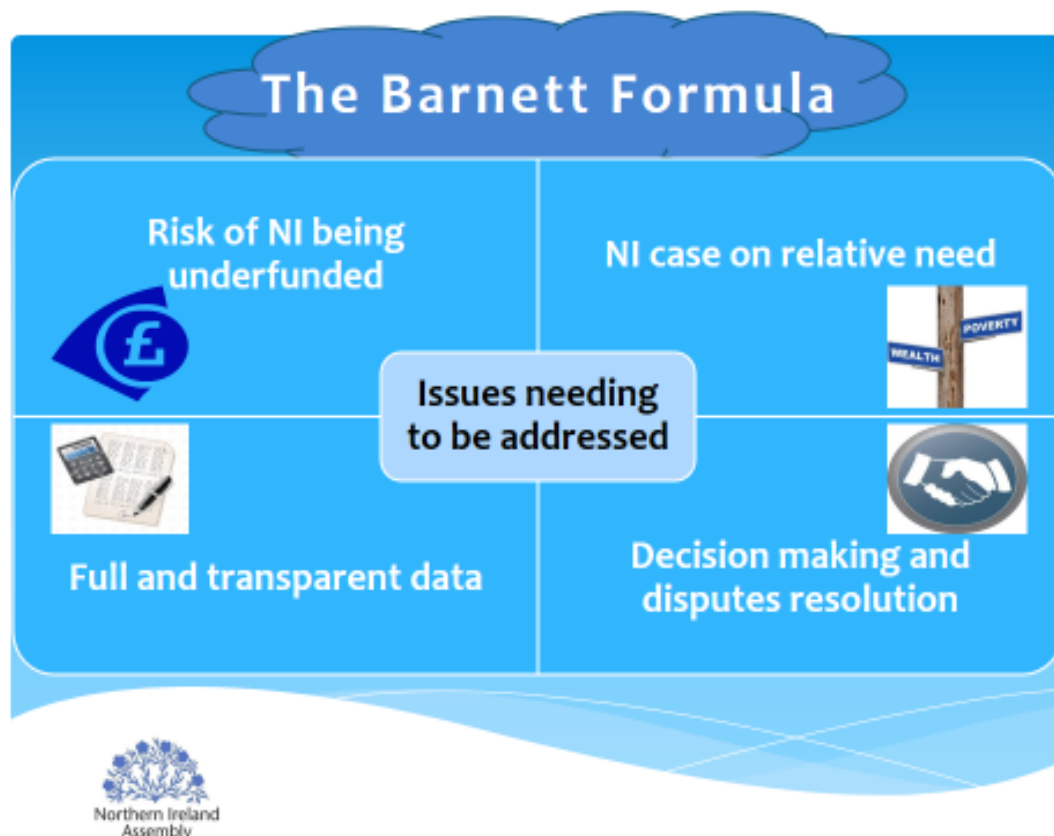
⁵⁹ http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/150218_operationofthebarnettformulaprofthain.pdf

p.8

What issues need to be addressed?

53. Arising from the review, as outlined in Figure 5, the Committee has identified four key areas which will need to be addressed, whether the Barnett formula is retained in some form or completely new devolution funding arrangements are introduced.

Figure 5



The risk of Northern Ireland being underfunded

54. In the original expert evidence received by the Committee in 2012, it was noted that the work of the [Holtham Commission](#) had indicated that the relative need of each of the three devolved administrations was greater than that of England and that the Barnett squeeze has taken Wales⁶⁰ below the point it would be at if there were a needs-based formula. Moreover, the updated evidence from Professor Holtham in 2014 suggested that there has been a Barnett squeeze in Northern Ireland, but starting from a higher level. In this regard, Professor Holtham advised that:

⁶⁰ The Committee has noted efforts to put in place arrangements for a 'Barnett floor' to prevent future convergence in respect of Wales.

http://www.biicl.org/documents/593_bingham_report_constitutional_crossroads.pdf

p.43

*We are maybe only a few years away from Northern Ireland being in the same position as Wales, i.e. going below the level that needs-based formulae would give it, once public funding starts to grow.*⁶¹

55. This conclusion was shared by Professor Trench who cautioned that:

*the point at which spending matches a reasonable estimate of relative need may not be far away. At that point, life could get very tough indeed for a Northern Ireland finance minister.*⁶²

56. This is illustrated in Table 1, which Assembly Research prepared using the Holtham estimates of relative need and Treasury's latest expenditure data to calculate an index of relative expenditure levels for each country, with England as the base. However, in considering this analysis, it should be noted both that the Holtham estimate of Northern Ireland's relative need was a 'rough-and-ready' calculation and that some potential question marks exist over the data in Treasury's annual [Public Expenditure Statistical Analyses](#) (PESA).⁶³

Table 1: Identifiable Total Expenditure on Services per head in 2013-14, by country, and Holtham's estimate of relative need⁶⁴

<i>£ per head</i>	England	Scotland	Wales	N. Ireland
Total 2013-14 expenditure	8677	10275	9923	10961
2013-14 expenditure indexed to England	100	118	114	126
Holtham relative need indexed to England	100	105	115	121

57. Also, in terms of the estimate of relative need in Northern Ireland at 121%, the Committee noted that the Holtham Commission pointed out that this would increase to 124% if adjusted for variations in taxable capacity relative to house prices and concluded that:

⁶¹ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/8-feb-2012-evidence-from-profs-trench-holtham-and-mclean.pdf> & <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/12-november-2014---hansard-evidence-from-professor-trench-and-professor-holtham.pdf>

⁶²

http://www.niassembly.gov.uk/globalassets/documents/raise/knowledge_exchange/briefing_papers/series3/alan_trench031013.pdf &

http://www.niassembly.gov.uk/globalassets/documents/raise/knowledge_exchange/presentations/series3/alan_trenchppt031013.pdf

⁶³ <http://www.niassembly.gov.uk/assembly-business/committees/finance-and-personnel/barnett-formula/research-papers/> http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/150211_reviewofbarnettformula-prof-heald.pdf

⁶⁴ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/research-papers/research-paper-291-15---relative-need-and-public-expenditure-data-in-the-united-kingdom.pdf>

*a strong case could be made that such an adjustment gives a purer estimate of relative need than is obtained by basing the analysis on unadjusted expenditure data.*⁶⁵

58. Professor McLean offered an additional perspective on whether the relative level of public spending in Northern Ireland is 'fair' by focusing on the proposition: *What if the only purpose of public expenditure were to relieve poverty?* By comparing relative public spending with relative GVA per head, this 'crude measure' found that Scotland receives consistently more public spending per head than would be expected, Wales receives consistently less than would be expected and Northern Ireland receives 'roughly what the model would predict'; though, as illustrated in Table 2, there was no clear trend in terms of whether the position in Northern Ireland is becoming more or less 'fair'.⁶⁶

Table 2: Comparison of relative public spending with relative GVA per capita

McLean's Relative Index					
	2008	2009	2010	2011	2012
England	0.99	0.99	0.99	0.99	1.00
Scotland	1.12	1.12	1.12	1.13	1.09
Wales	0.82	0.81	0.81	0.85	0.80
N. Ireland	0.97	0.96	0.92	0.98	0.94
UK	1.00	1.00	1.00	1.00	1.00

A Northern Ireland case on relative need

59. The Committee noted a range of views on both the merits and the practicability of moving to a needs-based assessment. In 2009 the inquiry by the [House of Lords Select Committee on the Barnett Formula](#) proposed that any needs assessment should take account of population age structure, low income, ill health and disability and economic weakness. Similarly, in his evidence, Professor Holtham pointed out that adding a needs-based element to a public spending formula need not be complicated and could be easily explained by the following key factors, data for which is readily available and could be factored into any calculation: demographics; poverty or deprivation; incidence of chronic health complaints; and the sparsity of the population.⁶⁷ While also supporting a needs-based assessment for Northern Ireland, Professor McLean pointed to the importance of ensuring that the data used to assess needs is not distorted in anyway at the expense of one region for another. He

⁶⁵ [Independent Commission on Funding & Finance for Wales](#), Fairness and accountability: a new funding settlement for Wales, page 137.

⁶⁶ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/20-november-2014---written-submission-from-iain-mcclean.pdf>

⁶⁷ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/12-november-2014---evidence-from-professor-gerald-holtham.pdf>

also took that view that, in light of the level of fiscal autonomy promised to Scotland, the move to a needs-based arrangements for Northern Ireland and Wales is now easier.⁶⁸

60. In discussing how a needs-based alternative could take account of socio-economic indicators, the resource base and special territorial factors, Professor Birrell pointed out that 'disputes could arise over finding agreement on definitions of need', including in terms of taking into account different structures and circumstances in Northern Ireland when assessing need. As such, he concluded that 'it is likely that a mechanism for negotiations would be necessary to resolve disputes on an annual basis'.⁶⁹

61. In his written submission, Professor Cairney advised that replacing the Barnett formula with a needs-based assessment:

*is (in many ways) far more controversial than Barnett. A needs based formula involves many value choices about what people need and what services we should all deliver. Further, for many, a UK-wide needs based formula seems increasingly distant from the idea of devolved discretion.*⁷⁰

62. [Assembly research](#) highlighted a similar point being raised in a paper on [Scotland's fiscal future in the UK](#) by Bell and Eiser, in terms of a needs-based system being potentially inconsistent with the notion of 'Scotland evolving into a semi-autonomous state within a fiscally federal UK' (though it was also acknowledged that there is a strong argument that the Barnett formula is not suited in this regard either).

63. Dr Gudgin's evidence cautioned against the assumption that a needs-based assessment would lead to Northern Ireland maintaining its higher level of public expenditure and also argued that, if Barnett was to be replaced by a needs-based allocation of UK public expenditure, the pressures as a result of public sector reform would be likely to increase.⁷¹ Professor Heald also urged caution over any move to a needs-based assessment, pointing out that any resultant reduction in funding would have to be phased in and advising that any needs assessment is done by an independent body.⁷²

64. From a further standpoint, the Committee noted that Northern Ireland is ranked highest of the three devolved jurisdictions on the Holtham calculation of relative need and that there

⁶⁸ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/20-november-2014---written-submission-from-iain-mcclean.pdf>

⁶⁹ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/d-birrell---review-into-the-operation-of-the-barnett-formula---march-2015.pdf>

⁷⁰ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/prof-paul-cairney-barnett-formula-sub-04032015.pdf>

⁷¹ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/28-january-2015---evidence-from-dr-graham-grudgin.pdf>

⁷² http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/150211_reviewofbarnettformula-prof-heald.pdf

may be particular considerations requiring to be covered by any agreed UK-wide approach to needs assessment. This latter point was recognised by several of the witnesses, including that ‘there was significant infrastructure neglect in Northern Ireland because of its political history’.⁷³ While reflecting on the benefit of the unhypothecated aspect to the Barnett consequentials, Professor Thain pointed out that:

*that is maybe at the cost of having a proper discussion about Northern Ireland's particular needs, including its social deprivation needs in particular, which need to be addressed through a separate allocation of resources.*⁷⁴

65. In its evidence, CIPFA recommended a complete removal of the Barnett formula in favour of a ‘principles based approach’ which would take account of need, equity, accountability and transparency; though it also accepted that a supplementary or ‘top-up’ mechanism could be introduced to take account of relative need. Moreover, in countering the argument that Northern Ireland should not be raising issues because of the perception that it benefits from the Barnett formula, CIPFA advised that:

*if you want to get to a fair and equitable position funding-wise, there is an opportunity to be at the forefront of that debate, rather than putting your head in the sand ... if you are going to influence policy, keeping your head down and saying nothing is probably not the best way to go about it. You are then going to leave it in the hands of Treasury and others to make those decisions for you.*⁷⁵

66. Members recall that the predecessor Committee for Finance and Personnel, as far back as 2007, highlighted its concern that the then debate on the options for funding devolution in Scotland had the potential to open up the issue of the future of the Barnett formula for Northern Ireland. As such, the Committee recommended that the Executive should ‘assess the implications of this scenario and prepare accordingly’. Moreover, the [DFP response](#) confirmed that this would be ‘kept under consideration’.

67. **It is clear from the evidence that any UK Government move toward complementing or replacing the Barnett formula with a needs-based assessment could generate controversy in terms of the approach taken, the definitions applied and the data used. Also, the Committee is aware that, while the Holtham Commission examined relative need from the Welsh standpoint, the Northern Ireland Executive has not completed a comparable exercise (a Needs Assessment was initiated by the Executive in 2001 but this was abandoned when Direct Rule returned). In view of this, the Committee considers that it is now timely for an initiative by the Executive to examine an appropriate methodology from a Northern Ireland perspective, including an agreed definition of need, and to begin to fully assess local spending needs using current, robust and reliable data. Such work would help to inform the Executive’s position,**

⁷³ http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/150211_reviewofbarnettformula-prof-heald.pdf

⁷⁴ http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/150218_operationofthebarnettformulaprofthain.pdf

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⁷⁵ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/cipfa---operation-of-the-barnett-formula-29.04.15.pdf>

both in determining the longer-term interests of Northern Ireland and in the event that proposals for a needs-based mechanism arise from the ongoing debate on constitutional reform in the UK (which is reasonably foreseeable given the current context).

Provision of full and transparent data

68. The Committee noted concerns amongst the expert witnesses generally about the quality and availability of the public finance data underpinning the Barnett decisions and a recognition that greater openness and transparency was required, even in the event of a move toward needs assessment.

69. Professor Trench pointed out that there is no audit requirement and ‘scant information about what changes in spending for England trigger changes in devolved grants or how the amounts of those changes are calculated’ in terms of the Barnett consequential.⁷⁶ Professor Holtham saw a case for the initial calculations of the consequential being carried out by an independent agency, stating that:

*the size of the grant would still be subject to political decision but those decisions should not be able to hide behind manipulation of technical factors.*⁷⁷

70. Similarly, in his evidence, Professor Thain called for the publication of the Barnett consequentials at a sub-programme level and suggested a strengthened role for the Office for Budget Responsibility (OBR) in the oversight on public spending data.⁷⁸ Dr Gudgin concurred that key decisions about consequentials should be made in a transparent manner by an independent regulator or a committee on which devolved authorities sit. He also pointed out that there was potential for much more openness and transparency in the negotiations between Treasury and DFP about how much the block grant would be affected as a result of corporation tax devolution, including in terms of the associated data.⁷⁹ Professor Heald shared a similar sentiment in stating that:

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http://www.niassembly.gov.uk/globalassets/documents/raise/knowledge_exchange/briefing_papers/series3/alan_trench031013.pdf & http://www.niassembly.gov.uk/globalassets/documents/raise/knowledge_exchange/presentations/series3/alan_trenchppt031013.pdf

⁷⁷ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/12-november-2014---evidence-from-professor-gerald-holtham.pdf>

⁷⁸ http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/150218_operationofthebarnettformulaprofthain.pdf

⁷⁹ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/28-january-2015---evidence-from-dr-graham-grudgin.pdf> or http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/150128_barnettformuladrgrahamgudginnicep.pdf

*Because of the past lack of transparency on how the system operates and the lack of trust in how it operates, we definitely need a body ... separate from the Treasury that actually collects and publishes the data.*⁸⁰

71. In terms of some positive developments noted in relation to data, CIPFA highlighted the improved data collection capacity of Treasury as a result of initiatives such as Whole of Government Accounts and Professor McLean pointed to improvements in the main data series, PESA. However, CIPFA also highlighted the shortcomings in data for the purpose of examining convergence and Professor McLean also cautioned that, with further devolution, the operation of the Statement of Funding Policy increases in complexity in terms of attributing tax revenues, as well as spending, to the appropriate territory and within that appropriate department.⁸¹
72. There was, therefore, a broad consensus amongst the expert witnesses on the need for full and transparent data. Similarly, arising from its visit to Edinburgh, the Committee noted that concerns about the lack of transparency and accountability in relation to how the Barnett formula operates and the block grant is calculated were identified in a recent [report](#) by the Scottish Parliament's Finance Committee.

Equitable arrangements for decision-making and dispute resolution

73. Related to the issue of the need for full and transparent data, the Committee also noted various suggestions for improvements to the arrangements for making decisions and resolving associated disputes in relation to devolution funding and finance. The potential reforms identified in the research and evidence included:
- placing the Barnett formula on a statutory footing with reporting requirements;
 - requiring the Statement of Funding Policy to be approved by the devolved Finance Ministers;
 - providing for an independent advisory or decision-making function, comparable to the Australian Commonwealth Grants Commission, to oversee funding allocations; and
 - providing for independent review and dispute resolution functions.
74. The evidence from several of the expert witnesses highlighted how the Barnett formula has no statutory underpinning and is wholly under the control and discretion of a single UK Government department (i.e. HM Treasury) which operates the Statement of Funding Policy in a non-statutory way and which does not require agreement from the devolved governments. In this regard, Professor Holtham concluded that Northern Ireland would

⁸⁰ http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/150211_reviewofbarnettformula-prof-heald.pdf

⁸¹ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/20-november-2014---written-submission-from-iain-mcclean.pdf>
<http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/11-march-2015-written-submission-from-the-chartered-institute-of-public-finance-and-accountancy-cipfa.pdf>

benefit from the Barnett formula ‘being put on a proper statutory basis with an element of independence from Treasury introduced into technical calculations’.⁸²

75. Examples were cited of the arbitrariness in Treasury decisions on what does or does not attract Barnett consequentials. These included initial decisions that infrastructure spending on the 2012 London Olympics, Crossrail and Kew Gardens would not attract consequentials as they were classified as an activity in England having UK-wide benefits. It has also been pointed out that, in addition to deciding on consequentials and other key issues such as the ‘comparability percentages’ and how disagreements are resolved, Treasury controls decisions over the carry forward of unspent year-end money and access to the UK Reserve.⁸³
76. While examples such as the 2012 London Olympics have been used to highlight instances of unilateral decision making on the part of Treasury, [Assembly research](#) has noted recent academic work which also raises more fundamental and potentially controversial points about the relationship between the Barnett formula and political power, in particular the level of central Treasury control and influence over devolved funding and policy decisions.
77. In terms of improving the operation of the Barnett formula, Professor Trench pointed to the suggestion made by the Scottish Finance Secretary, John Swinney, that devolved Finance Ministers should be responsible for approving the Statement of Funding Policy which would ‘make a significant difference to how it is framed and the process of settling it and agreeing what goes into it’.⁸⁴ In his evidence, Professor McLean suggested that the responsibility for the Statement of Funding Policy and the assignment of spending programmes between reserved and devolved functions could be moved to a neutral regulator, such as the Office for National Statistics (ONS) or the OBR.
78. In terms of the suggestions for more thorough-going reform, Professor McLean highlighted the possibility of a neutral agency taking over the process, under arrangements similar to that pertaining to the [Australian Commonwealth Grants Commission](#).⁸⁵ Similarly, CIPFA recommended that ‘the resource allocation process should be depoliticised by being overseen by a commission which is independent of government’; this would comprise members independently appointed for a fixed period of time, and would take decisions on the basis for allocations out of the Treasury’s hands.⁸⁶

⁸² <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/12-november-2014---evidence-from-professor-gerald-holtham.pdf>

⁸³ http://www.biicl.org/documents/593_bingham_report_constitutional_crossroads.pdf
pp. 41.

⁸⁴ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/12-november-2014---hansard-evidence-from-professor-trench-and-professor-holtham.pdf>

⁸⁵ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/20-november-2014---written-submission-from-iain-mcclean.pdf>

⁸⁶ <http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/written-submissions/11-march-2015-written-submission-from-the-chartered-institute-of-public-finance-and-accountancy-cipfa.pdf>

79. On the issue of disputes resolution, Professor Trench pointed to the example of the 2012 London Olympics as highlighting the lack of success by the disputes panel of the Joint Ministerial Committee, which is chaired by a UK Government Minister and operates under the [Memorandum of Understanding](#) (MoU).⁸⁷ Also, in questioning whether ‘the gentlemen’s agreements – the concordats – can survive in an increasingly complex political and fiscal situation’, Professor Thain saw the potential for the Supreme Court to get involved ‘in some of the decisions about arbitration between Westminster and the devolved parts of the UK.’⁸⁸
80. Members noted other recent evidence underlining the weaknesses in the current arrangements for decision making and dispute resolution in relation to devolved funding. For example, in highlighting the informality of intergovernmental relations in the UK, the BIICL report concluded that the machinery for financing devolution ‘*can no longer be left to the sole discretion of HM Treasury*’ and included in its recommendations a call for an independent body to advise Treasury, an external review function in respect of block grant calculations and deductions and an independent disputes resolution function.⁸⁹ Also, members noted that the Scottish Parliament’s Finance Committee has recently highlighted weaknesses in the inter-governmental machinery in terms of transparency, scrutiny and accountability, with most business being conducted outside the formal mechanisms and on the basis of bilateral arrangements.⁹⁰

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http://www.niassembly.gov.uk/globalassets/documents/raise/knowledge_exchange/briefing_papers/series3/alan_trench031013.pdf &
http://www.niassembly.gov.uk/globalassets/documents/raise/knowledge_exchange/presentations/series3/alan_trenchppt031013.pdf

⁸⁸ http://www.niassembly.gov.uk/globalassets/documents/finance/barnett-formula/hansards/150218_operationofthebarnettformulaprofthain.pdf

p.5

⁸⁹ http://www.biicl.org/documents/593_bingham_report_constitutional_crossroads.pdf

p.47

⁹⁰ <http://www.scottish.parliament.uk/parliamentarybusiness/CurrentCommittees/87349.aspx> pp. 10 – 11

Conclusions and Recommendations

81. While noting the pledges made by the three main UK-wide party leaders to retain the Barnett formula, the Committee is mindful that, as yet, there is no clarity on what precisely this will mean in practice or, indeed, whether this commitment will be maintained in the medium to long term. In recognising that the Barnett formula has some undeniable benefits, the evidence has also highlighted drawbacks and growing criticism.
82. From the evidence received, the Committee has identified key factors which could influence how or whether the Barnett formula continues to operate as well as issues which need to be addressed in the event that it is retained for the foreseeable future. In light of these findings and given the ongoing debate on wider constitutional reforms and fiscal devolution, the Committee makes the following recommendations:
- that DFP examines in more detail the extent of convergence to date and the future trajectory to fully assess the risk of Northern Ireland being significantly underfunded in future;
 - that DFP and the wider Executive establishes how a needs-based assessment mechanism would best be designed to take account of the Northern Ireland context and that the chosen methodology is piloted using current data – by way of pre-emptive measures in the event that either the UK Government decides to dispense with or alter the Barnett formula or that the formula no longer meets Northern Ireland’s spending needs in future;
 - that the Minister of Finance and Personnel, on behalf of the Executive, engages with her counterparts in the Scottish Government and Welsh Government with a view to presenting jointly agreed proposals to the UK Government for initial improvements to the operation of the Barnett formula and related devolution funding arrangements. These could include, for example: undertakings by Treasury to publish the data upon which Barnett consequential and related decisions are based; a requirement that the Statement of Funding Policy is subject to approval by the devolved governments; clarity on the arrangements for block grant adjustments; and interim improvements to the inter-governmental machinery between the UK Government and the devolved governments. Such measures could be regarded as positive first steps pending any more substantive constitutional reforms to devolved funding arrangements; and
 - that DFP brings forward proposals on how the Committee and wider Assembly will be afforded the opportunity to undertake effective scrutiny of planned adjustments to the Northern Ireland block grant arising from the devolution of corporation tax and in terms of any further fiscal devolution.

83. **The Committee acknowledges that, leaving aside the resolution of the issues identified by this review in the immediate future, the dynamic of wider UK constitutional reform could result in a more significant re-engineering of the funding arrangements for devolution, whether that involves the Barnett formula being reshaped or ultimately replaced. With this in mind, the Committee recommends that DFP and the wider Executive takes a more proactive approach by developing a fully considered position on what will be in Northern Ireland's best interests as regards longer-term funding arrangements and by seeking to contribute to and shape the wider debate accordingly.**

Minutes of Evidence

Wednesday, 8 February 2012	Committee for Finance and Personnel Review of the Operation of the Barnett Formula: Professor Trench, Professor Holtham and Professor McLean	 View Online
Wednesday, 12 November 2014	Committee for Finance and Personnel Review of the Operation of the Barnett Formula: Professor Trench and Professor Holtham	 View Online
Wednesday, 28 January 2015	Committee for Finance and Personnel Review of the Operation of the Barnett Formula: Dr Gudgin	 View Online
Wednesday, 11 February 2015	Committee for Finance and Personnel Review of the Operation of the Barnett Formula: Professor Heald	 View Online
Wednesday, 18 February 2015	Committee for Finance and Personnel Review of the Operation of the Barnett Formula: Professor Colin Thain	 View Online
Wednesday, 11 March 2015	Committee for Finance and Personnel Review of the Operation of the Barnett Formula: Professor Derek Birrell	 View Online
Wednesday, 29 April 2015	Committee for Finance and Personnel Review of the Operation of the Barnett Formula: CIPFA	 View Online

Submissions

The following submissions have been received by the Committee in relation to the review:

- [Oral Evidence from Professors Trench and Holtham - Additional Information from Professor Holtham](#)
- [Preliminary Remarks from Professor Gerald Holtham](#)
- [Written Submission from Professor Iain McLean](#)
- [Follow-Up Submission from Professor Gerald Holtham](#)
- [Written Evidence from Dr Graham Gudgin](#)
- [Written Submission from Professor Paul Cairney](#)
- [Written Evidence from Professor Derek Birrell](#)
- [Written Submission from CIPFA](#)

Assembly Research Papers

The following research papers were considered by the Committee in relation to the review:

- [The Barnett Review Update 2014](#)
- [Relative need and public expenditure data in the United Kingdom \(Updated\)](#)

The information contained in this document is available online at:

www.niassembly.gov.uk

This document can be made available in a range of alternative formats including large print, Braille etc. For more information please contact:

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