House of Commons

Public Accounts Committee

Oral evidence: Funding for Scotland, Wales and Northern Ireland, HC 1751

Monday 10 June 2019

Ordered by the House of Commons to be published on 10 June 2019.

Watch the meeting

Members present: Meg Hillier (Chair); Douglas Chapman; Sir Geoffrey Clifton-Brown; Chris Evans; Anne Marie Morris; Gareth Snell.

Gareth Davies, Comptroller and Auditor General, Linda Mills, Parliamentary Relations Manager, National Audit Office, Lee Summerfield, Director, NAO, and Marius Gallaher, Alternate Treasury Officer of Accounts, HM Treasury, were in attendance.

Questions 1-104

Witnesses

I: Sir Tom Scholar, Permanent Secretary, HM Treasury, and Jean-Christophe Gray, Director Devolved Funding, HM Treasury.

Report by the Comptroller and Auditor General

Investigation into devolved funding (HC 1990)

Examination of witnesses

Witnesses: Sir Tom Scholar and Jean-Christophe Gray.

Q1 **Chair:** Welcome to the Public Accounts Committee on Monday 10 June 2019. We are here today to look at the knotty issue of what is known as the Barnett formula, which is the calculation the Treasury uses to make sure that each nation of the UK receives its fair share of Exchequer spending. It was set by a predecessor of mine as Chair of this Committee, Joel Barnett, when he was a Treasury Minister, but it is not actually a clear written rule, so we want to talk a little bit about how it is being used now and how fair it is. One of the key things that we think is an issue is the lack of transparency. I don't think the average citizen in Scotland or Wales—or, indeed, in England—would really know how it is working, so we want to probe that a bit.

We are going to ask you some, hopefully, pithy questions. We have obviously got our national representatives here, so do expect some detailed questions about aspects of spending in Wales and Scotland. I am sure you are fully prepared with your map in front of you. I am going to ask Gareth Snell to kick off, once I have introduced our witnesses. We have, from my left to right, Jean Christophe-Gray, who is the director for devolved funding at Her Majesty's Treasury, and Sir Tom Scholar, who is the permanent secretary at the Treasury. Welcome to you both. I think, Mr Gray, it is your first time in front of us.

Jean-Christophe Gray: It is. Thank you for the welcome.

Chair: A warm welcome to you. You are going to have a great fun time.

Jean-Christophe Gray: That is what they told me.

Chair: I am sure they did. If we do our job properly, you will know you have mastered your brief. Actually, if you are director for devolved funding it should be easy material for you, I am sure. We are setting you up nicely. I am now going to bring in our friendly member, Gareth Snell.

Q2 **Gareth Snell:** Yes, you are being set up, Mr Gray. If I can start with you, Sir Tom, we all know what the Barnett formula is, so we don't need to go into too much detail about what it is, but can I just ask you, given that we now have a varying set of devolved settlements for each of the nations outside of England, all of whom now retain different levels of tax bases domestically, how fit for purpose you think the Barnett formula is for funding adequately the nations of the UK outside of England?

Sir Tom Scholar: As you say, the Barnett formula is an important part of the mechanism for allocating funding across the nations of the UK, but it is by no means the only part of that mechanism, not least reflecting the changes to the devolution landscape over the years, particularly in recent years. It is important, I think, to understand.

I would like to say two things about the Barnett formula right at the beginning. First of all, it is only part of the allocation mechanism. Secondly, it is a mechanism—it is a guide. You sometimes hear people talk about it and ask whether it is fair or not. I think what I would say is that it is a mechanism that gets you some of the way there, and there is a further set of arrangements that apply differently in Wales, Scotland and Northern Ireland.

You ask whether it is still fit for purpose. Famously, when it was proposed in 1978 by Joel Barnett, who was then Chief Secretary to the Treasury, he anticipated—as he often said in later life—that it was a proposal for one year, I think for Scotland only, and he certainly never expected to see how long-lived it would prove to be. Although over the years many people, inside government and outside, have from time to time questioned whether it is still the right way of doing it, nevertheless successive Governments and most of the time the major political parties in their manifestos have continued to support it—as I say, not as the only way but as part of the way of addressing funding questions.

Furthermore, I would add, a couple of important independent commissions of recent years—the Holtham commission in the case of Wales and the Smith commission in the case of Scotland—have looked at these things. Again, their proposals have been to add things on to the framework in various ways, but the basic principle of allocating changes to funding in England—or England and Wales, as the case may be—to other parts of the country reflecting population shares has been supported over time. In the Treasury, it is not for us as officials to decide the framework—that is one that has built up over time—but it is our job to operate it correctly.

The Chair mentioned transparency; that is something we have put a lot into in the past few years, and we are keen to build on that, including in this spending review. I should say that I very much welcome the NAO Report that we are looking at today, because it is a complicated system, and it is not straightforward for the citizen to understand. I think the NAO Report does a really good job in setting out how it has worked.

Chair: We were reflecting that it is the first time that the NAO can remember looking at this, and the first time that the Public Accounts Committee can remember looking at it. Depending on how it goes today, we might be looking at it in a lot more detail, to warn you there.

Q3 **Gareth Snell:** I suppose that doesn't really get to the nub of my question, though. I appreciate that it is the policy of the Treasury, and I'm not seeking your opinion on whether the policy is correct, but in terms of the formula or the mechanism itself, what you have described and what the NAO Report described is a very complex and often subjective series of funding streams that can—or could not—be activated. In terms of the degrees of devolution—not just in Wales, Scotland and Northern Ireland, but also within our city regions as well, coming on stream—what longevity do you think there is for a system that is as complex, interwoven and arguably opaque as the Barnett formula?

Sir Tom Scholar: If the past is a guide to the future, it has been with us for 40 years. Let me say a couple of things: I agree it is complicated, and it is partly our job and partly the NAO's job to explain it, and this Committee can play an important part in that. The formula itself, I would say, is not subjective; the formula itself is largely mechanical.

Gareth Snell: But the application of the formula—

Sir Tom Scholar: Well, the application is also mechanical. When we are applying it, which we do in complete openness with our colleagues in the Scottish and Welsh Governments and the Northern Ireland Executive, we look at whether Parliament has decided that a particular activity is reserved or devolved—the Report explains this—and depending on whether it is reserved or devolved, we then allocate consequential funding to the other three nations as a consequence. That element of it, the Barnett formula itself, is mechanical.

Where the judgment comes in is on—well, that element is mechanical. There are then other elements of the fiscal settlement, in particular tax devolution, which are the product of negotiations between the UK Government and the other three Administrations. If I may just add one final thought, there is then the ability for UK Ministers to make judgments about the allocation of resources across the whole country, and I would agree that that element is, to a degree, subjective.

Q4 **Gareth Snell:** You have situations in which devolved Administrations believe they have, in some way, been short-changed or that they have not quite received the allocation that they were anticipating through the Barnett formula or other ways in which the Treasury may reallocate resources, where you have projects for which—we will get on to the calculations later—it becomes, "Is it local or is it national?". If it is as mechanical as you suggest, why is it that there are occasions where the devolved Administrations feel as though they have not been given exactly what they want, when presumably they can make the same computations that you have made and come to the same answer?

Sir Tom Scholar: In our experience, it is not normally the case that there is any dispute about the application of the formula; the question is normally whether the formula is able to capture sufficiently all of the different elements that would go into a judgment of relative need or fairness. Ultimately, a judgment of relative need or fairness, when you are talking about allocating resources, is a political judgment rather than a mechanical one.

As I said, the Barnett formula gets you to the starting point and is a hugely important part of the decision, but the cases you were alluding to are cases where, for example, the Government of Wales perceives an additional need that the formula does not cater for, and makes its case. In a settlement of national resources going to different areas, or different nations within the overall country, that is always going to be a possible source of contention.

Q5 **Gareth Snell:** If we accept for one second that the mincer in the middle is always the same mincer, but the input and the output are different depending on the type of meat that you are using—that is a really flawed analogy; I'm sorry, Chair—what do you believe could be done to make those input decisions more transparent and less subjective? Also, what do you think could be done to make the application more understandable, not just to the devolved Administrations but to my constituents in Stoke-on-Trent, for instance? They will not necessarily know what the Barnett formula is, but ultimately it is money that they have paid into the system being redistributed around the country in one way or another.

Sir Tom Scholar: As I said earlier, the Report in front of us today is a very important part of that. We will publish further information around the spending review about how we approach these decisions, and how we operate the system. I should say that those will be quite technical, because it is a technical system. I would add that in the whole of Government accounts, which we will discuss here next week, we have a chapter with a breakdown by nation and by region that gives information on spending per head.

We are constantly trying—I know this is a great theme of this Committee too—to explain all this so that the informed citizen can understand and make choices accordingly, but in the end, particularly given tax devolution now in Scotland, and an element of welfare devolution, it is inevitably a complicated system that takes a little bit of time to explain.

Q6 **Gareth Snell:** I will come to you Mr Gray, but going back to my previous point, given the expanded range of devolution settlements—the more systems that are being devolved to the nations—do you believe that the Barnett formula, as the chunk in the middle of that system, will still be fit for purpose in five or 10 years' time to properly ensure that there is a fair allocation of funding around the United Kingdom?

Sir Tom Scholar: What the Barnett formula does and has always done is allocate changes to funding from a baseline going back 40 years, in which there was a difference in funding per head across the nations of the country. As I said earlier, people have looked at that from time to time. I recall that in the 1990s, when I was first working in the Treasury, there was some question about whether the Government would try to change it in favour of a different formula. In the end, people have always stuck with it because for the core of the process of allocating changes to funding it is readily explicable in terms of looking at the degree to which changes in English funding require changes in devolved funding, then looking at a population base.

An important thing that has changed in recent years is, in particular, the changes to tax and, alongside that, some changes to the borrowing powers to accompany the greater legislative and political devolution, in particular in Scotland and Wales. We have new fiscal frameworks for Scotland and for Wales, both of which were agreed in 2016. We have said that we will review those in the years ahead—in the case of Scotland, based on the advice of an independent commission that needs to report by the end of 2021.

That will give everybody—the Government in Scotland, the Government in Westminster, and this Committee and everyone looking at it—an opportunity to look at five years of this new framework. That will again be a time to ask these questions of fitness for purpose, fairness and so on, which can be addressed only through a political process, because the allocation of resources is a political decision.

Q7 **Gareth Snell:** I will put the same question to you, Mr Gray, in a second. Briefly, Sir Tom, when you are looking at those parts of the input—whether it is the Barnett formula per se, direct funding, or some other Government decision on spending and what should then be given to Wales, Scotland and Northern Ireland—how much of those decisions by officials in your Department are based on the precedent of previous decisions around similar allocations, and how much of it is overseen politically depending on what sort of decision outcome you wish to achieve, as opposed to what the actual position might be?

Sir Tom Scholar: The principal determinant of changes to the block grant—the allocation of funding from Westminster to the devolved Administrations—is the formula, which, as I said earlier, is mechanical rather than discretionary. It is not the choice of officials. It is actually not the choice of Ministers, other than to continue with it.

Q8 **Gareth Snell:** No, but the allocation, through categorisation and things like that, has become a subjective input, based on decisions that are made—I appreciate not necessarily by civil servants, but by politicians. If you are categorising and making decisions, or giving advice on those matters, how much of what you are advising is based on the precedent, which will have an impact either on the block grant or consequential Barnett funding, as opposed to looking at an amount of money and trying to cut the cake to fit a prescribed budget?

Sir Tom Scholar: I will come in a moment to things outside the formula, but when you look at the formula and whether a particular item of expenditure has consequentials or not, what we look at is the statutory functions of the devolved Administrations and whether they have responsibility for providing the particular service.

That is different in different countries. Sometimes the Westminster Government—the UK Government—are responsible for providing the service. For example, the administration of justice in Wales is provided by the UK Government. Therefore, if we are allocating additional resources at a UK level to justice, that already covers Wales but it does not cover Scotland, so when we look at the operation of the formula we just look at what Parliament has decided.

Outside the formula, we come to the things that you are talking about—areas of spending such as city deals. This is a relatively new area of devolution, and devolution within England as well as across the nations of the UK. What we do as officials there is advise Ministers on the possibility for successful city deal arrangements. That is partly based on the local economy, partly based on local support, including the provision of match funding at a local level, and partly based on the business plan and the ability of a particular set of proposals to generate jobs and incomes in the particular cities.

There, when we are looking at how we would advise the allocation of resources, I would agree that that is much more based on trying to assess relative merits and make trade-offs between them. That is the particular area where that does happen.

Q9 **Gareth Snell:** Mr Gray, is there anything you want to add?

Chair: You are the one who is responsible day to day for deciding what's in and what's out, on the subjective elements of it.

Jean-Christophe Gray: Well, I hope it's not a shock to say that I agree with—

Chair: I have to say, as you are newcomer to this Committee, that we always urge witnesses if you agree just to say that you agree; don't repeat it.

Jean-Christophe Gray: I very much agree with that characterisation.

Q10 **Chair:** Can I ask you what it's like in the hot seat? How hard is it for you as a civil servant to make a judgment, and what pushback do you get? I am not asking for a specific example. If you want to give a specific example that would be great, but is it tricky? Is it tricky territory to be in, because it is not clear cut and you have to make judgments? You then make recommendations to Ministers on those judgments, and there might be an overriding political thing, such as the northern powerhouse, for example, that would perhaps have an impact.

Jean-Christophe Gray: Going back to what Tom was saying about the application of the formula, although it can take a bit of unpicking it is a mechanical process. One of the advantages of the formula is its replicability. At official level, we are on the phone or over email with our devolved counterparts on a daily basis, and I would say that that transparent arrangement works very well. They are able to replicate the calculations very straightforwardly.

At official level, I will not go as far as saying that it is easy, but we are able, for example, if a Minister is interested in policy area X, to go to the statement of funding policy, which has the comparability factors for each budget line per Department, and set out what the Barnett consequential, if any, would be of a particular policy area if it involves a change to spending in England or in England and Wales.

Q11 **Sir Geoffrey Clifton-Brown:** Can I take you to page 28 and paragraphs 2.14 and 2.15? Paragraph 2.14 is to be welcomed, in that you now publish the total amount of block grant and the consequential amounts, but the first sentence in paragraph 2.15 is: "Unlike UK government departments, the devolved administrations are not involved in direct negotiations with HM Treasury on their funding settlements." Why not, Sir Tom?

Sir Tom Scholar: I will, in a moment, turn to Mr Gray, who has, unlike me, directly taken part in settling spending reviews, but the principal reason is the one that I have described: in a spending review, we are allocating changes to the funding of Governments Departments—typically additional funding. We have a formula that calculates what the consequences of that are for the block grant, and then the changes to the Scottish, Welsh and Northern Ireland budgets drop out of that.

That is, if you like, the classic spending review. It does happen that there are additional decisions outside the formula, whether it is city deals or, for example, an allocation for policing in Northern Ireland or Scotland reflecting a particular need there that is not reflected elsewhere in the country. Typically, on those things decisions tend not to be taken at spending reviews but at other times, at other fiscal events.

The main allocation decisions in respect of the devolved Administrations are mechanical, and derive from the correct application of the system. That, if you like, is not a negotiation. As Mr Gray said, we are closely in touch with our colleagues in the devolved Administrations.

Q12 **Chair:** But they are not bidding.

Sir Tom Scholar: In the run-up to a spending review, we will make sure that they know what comparability factors we are using, and that there is agreement that they are the correct ones. We will also want to make sure that they are confident that we have correctly recorded and reflected changes to funding baselines. There is a large technical exercise, but it is not exactly a negotiation.

Q13 **Sir Geoffrey Clifton-Brown:** I understand that the Barnett formula, as Mr Gray has already made clear, needs to be replicated, and that it is a formula and it is just that. That is what happens at the spending review, but at other times of the year, when these consequentials are announced, inevitably there is an element of subjectivity and judgment in those. Why cannot the devolved Administrations be involved in that subjectivity and judgment?

Sir Tom Scholar: If we make a new allocation outside a spending review in a fiscal event, clearly the decision about where to allocate new resources, whether it is to skills, housing, education, health or whatever, is a ministerial decision and a political judgment. However, once the decision has been made, the application of that funding to the devolved Administrations is, again, a technical and mechanical matter, because either the policy area in question is reserved at the UK level or it is devolved, and Parliament has decided that. Depending on whether it is reserved or devolved, the funding flows from that.

Let me give an example of something that was a little more complicated than that—decisions on NHS funding last year. As you know, about a year ago the UK Government—

Q14 **Chair:** We know the background. Do you want to go to the point of what you are saying?

Sir Tom Scholar: The point is that at the time the announcement was made in July it was not clear precisely how it would be funded. At the time, we said to our colleagues in the devolved Administrations, and indeed publicly, "If the entirety of this funding were new money allocated to NHS England, then these would be the consequences for Scotland, Wales and Northern Ireland." In the Budget several months later, a small part of the funding was reprioritisation from existing budgets. That was not new money, and therefore did not give rise to new devolved consequentials.

Chair: Yes, it was within the envelope of existing expenditure.

Sir Tom Scholar: In respect of the NHS money, the devolved Administrations got slightly less than we had first estimated. I should say, at the same time we also allocated new money to social care that did have consequentials, so actually overall they got a little bit more than the first estimate. That is just an illustration that sometimes the precise funding may come a little bit later from the initial announcement. We always err on the side of more information and trying to give people a better idea earlier, but it sometimes means that corrections need to be made later.

Q15 **Sir Geoffrey Clifton-Brown:** In terms of Government mechanics, when a Department is bidding for money, if it is a devolved subject—say, health or education—does the Treasury advise that Department, "If you want another £1 billion, that will cost the Treasury £1.1 billion or £1.2 billion because that is the additional settlement to the devolved Administrations."?

Sir Tom Scholar: Yes, we do. We factor that fully into our advice.

Q16 **Sir Geoffrey Clifton-Brown:** You do, but do you tell the Departments that?

Sir Tom Scholar: Yes, it is part of the discussion.

Q17 **Chair:** Okay. Lesley Laird MP raised with me the stronger towns fund. She has been pressing to ask whether it is Barnettised, and she has been asking the Minister questions about this. It seems that, if it is, it was not very clear from the beginning, because no answer has been forthcoming. It raises for me the question of whether the Departments and Ministers really understand Barnettisation and the consequentials when they make an announcement.

The NHS one is a very good case in point. The cynic in us could say, "Aha—advertised as new money one day, but when it came to the nitty gritty the Barnett formula showed us that actually it wasn't all new money." If there was more transparency around that, we would have known more about it. Do you think that Departments really understand it, and that when Ministers make announcements they have actually taken into account the guidance that you have to live by?

Sir Tom Scholar: Clearly, it is the Treasury that is responsible for the formula and has the understanding of the whole picture and the operation of it.

Q18 **Chair:** But a shadow Front Bencher cannot get an answer on something quite basic. It is £160 million for Scotland potentially; £1.6 billion across English towns. It is big money, but not mega-bucks in a sense for the overall Budget.

Sir Tom Scholar: In the case of the stronger towns fund, which is intended to be a multi-year programme, the funding for future years needs to be decided in the spending review. If there are new allocations there for the fund in areas where policy is devolved, which you would expect there to be—

Q19 **Chair:** Are you saying that that is complicated because it deals with different policy areas, because stronger towns is not just one pot of money?

Sir Tom Scholar: The funding for this year was a reprioritisation of existing budgets, so that does not give rise to new Barnett consequentials. In terms of future years, that gets decided in the spending review, and when the money is allocated that will have consequentials.

Q20 **Chair:** That is quite an interesting answer, because that has not been forthcoming so far, which is an interesting indication that perhaps the system is unable to give that answer. That is a slight worry.

You have raised the spending review. We understand that it is likely to be delayed—perhaps you can tell us more. What are the consequences of a delay to the spending review on Barnett allocations?

Sir Tom Scholar: We will need to set new spending plans this autumn for the year 2020-21 at least. In the normal course of events, as the Chancellor said, we would be setting plans for three years, but we have to set plans for next year as a minimum, because we do not have plans for next year.

Q21 **Chair:** So how are you going to do that? Will you just roll it over from last year?

Sir Tom Scholar: That is a decision that will need to be taken by the Chancellor and the Prime Minister in due course.

Q22 **Chair:** But what are the options? To roll it over? There will be special pleading all over the place, won't there? What are the options, other than rolling over this year?

Sir Tom Scholar: The work we are doing at the moment with spending Departments, which we have been engaged in for several months, is the usual preparatory process for a spending review, where we go through baselines, reconcile the data, and make sure that we all start from the same starting point. The next step beyond that is to allocate the overall envelope, and then the next step beyond that is to allocate the additional resources within the envelope.

We are not able to do the second or third of those things until we actually start the spending review, and the Chancellor is on the record as saying that that is a decision that will be taken in July. Clearly, the timing of UK decisions is critical for the devolved Administrations because of their own budgeting. We totally understand that, and we will make sure that those decisions are taken in a timely way, so that they can take into account—

Chair: We will probably come back to this a little later.

Q23 **Gareth Snell:** That was the point I was going to raise. In terms of managing the expectations of the devolved nations in their budget-setting process, what does the Treasury do to give some sort of understanding of the total sorts of figures that the devolved nations may get? Also, with in-year changes that might lead to Barnett consequentials, what does the Treasury do to make sure that those devolved Administrations have some understanding of what might be coming down the line so that they can prioritise?

One of the things that this Committee looks at is value for money, and one of the things that we have been critical of in all Departments is in-year funding changes that lead to very quick spending of money, because you have been given it in-year and need to get rid of it by the end of the year. My concern is that where we have significant changes in-year that lead to an in-year Barnett consequential, which is obviously an issue for the audit committees of the devolved nations, are we getting good taxpayer value for money with the money that is being moved to the devolved nations on the back of decisions in Westminster?

Sir Tom Scholar: I will turn to Mr Gray in a moment, if I may, on how this actually happens in practice, but typically—not always—a decision to allocate a new sum of money to a particular area of spending would be taken in a Budget or a spring statement, if we are outside a spending review cycle. We would typically make sure in the run-up to announcement, and often only quite close to the announcement because of the need to make sure that everything is actually properly decided, that the devolved Administrations had an understanding of what we were doing on the day, so that they would know on the day what the consequences for them would be.

Q24 **Gareth Snell:** The financial consequences?

Sir Tom Scholar: Yes. For example, if extra money is being made available for housing, that will have consequences in Scotland, Wales and Northern Ireland. Of course, it does not mean that the money has to be spent on those things, and it does not mean that the Administrations have to follow the same policy decision that the UK Government have made.

Q25 **Gareth Snell:** I am thinking about things like Crossrail versus HS2. HS2 has been designated a national project while Crossrail is a local transport infrastructure project, so has different impacts and different consequentials. Wales gets nothing for HS2, perversely, but gets something as a result of Crossrail. Obviously those characterisations are important.

Mr Gray, in a minute I would like you to talk me through how you make some of those decisions, but say the Government have to put some more money through the DFT into Crossrail. When would the devolved nations expect to get their Barnett consequentials, and given the relatively large figures that are involved in that project, and therefore the consequentials, what do you do to make sure that they know that that money is coming in good time, so that they can plan for it properly and make use of it in a more focused way? However they choose to use it, how do you give them good notice that that money is coming?

Sir Tom Scholar: Again, I will defer to Mr Gray if I get this wrong. The way I think we operate the system is that at the moment the announcement is made, or immediately beforehand, we will discuss with the devolved Administrations how much additional money is being announced for an England or an England and Wales programme, over what years and what the budgetary consequences for them will be—how much additional money they can expect as a consequence, and over which years. Of course, all money has to be voted by Parliament—either at main estimates or at supplementary estimates. If it is an in-year change, that will be incorporated into the supplementary estimates that Parliament will consider in January or February. The important thing is that the devolved Administrations will know to expect that money and to expect Parliament to vote that money, so that they can start to allocate it immediately, in-year. Similarly, if it is a multi-year funding thing, they will expect the additional money to come the following year and the year after.

Q26 **Chair:** Does Mr Gray want to explain how you decided between Crossrail and HS2?

Jean-Christophe Gray: On Crossrail and HS2.

Q27 **Gareth Snell:** Just as examples of two, multibillion-pound rail infrastructure projects. One triggers something for Wales, and one does not. How do you come to those sorts of conclusions about when you should apply consequentials, and how subjective is it?

Chair: And how much discretion is there?

Jean-Christophe Gray: It comes back to what Sir Tom said earlier about the Barnett formula being applied in a mechanical way that follows the administrative arrangements, which vary from one devolved Administration to another. In the case of HS2 and Crossrail, and in terms of so-called heavy infrastructure, the distinction is that the Scottish Government makes a grant via its transport Departments to Network Rail.

Network Rail has a de facto subsidiary, Network Rail Scotland, for those types of heavy projects. That is not the case in Wales; there isn't a Network Rail Wales. Heavy infrastructure rail projects in this case are done on an England and Wales basis, and the Welsh Government therefore does not make a grant to Network Rail in the way the Scottish Government does. There is a different administrative arrangement for that element of the railway.

It is a bit akin to the example of justice that Sir Tom gave earlier. Crossrail, which is administered by Transport for London, is therefore a local transport scheme, and Scotland, Wales and Northern Ireland receive the Barnett consequentials of it. In a sense, the distinction follows the comparability factors that are set out in the statement of funding formula, which explains there is a distinction between the administrative arrangements for heavy rail infrastructure in Wales and Scotland. As I say, that follows through. The way I tend to think about it—slightly crudely, perhaps—is that the Scottish Government is making a payment to Network Rail for those types of projects in a way that the Welsh Government does not, because that element comes from the Department for Transport budget. That is why there is a distinction between the two in that case.

Q28 **Chris Evans:** Say a new Prime Minister comes in now and decides to cut the budget for Crossrail. Will it have Barnett consequentials for Wales? Will it be reduced?

Sir Tom Scholar: Under the operation of the formula, the answer is yes.

Q29 **Chris Evans:** So the nation would be at a disadvantage because of the cut in their budget. Is that right?

Sir Tom Scholar: That is the answer that the formula would give, yes. As I said, you cannot describe the formula as giving the right answer or a fair answer—you have to apply a different judgment to that. What it does is give the answer. It says that if you are spending this much less on a programme in England that is devolved, the consequence is that you would spend that much less in the devolved Administration, too.

Chris Evans: Talk me through this. How would you claw that money back? Would you take that out of the block grant, or would it have to be a one-off payment?

Sir Tom Scholar: Let us imagine, in your example, that this is a decision taken in the autumn, alongside other spending decisions for the year ahead. It would be part of many decisions on different programmes, some with increased funding and some with decreased funding. As we were describing earlier, you would go through each line of that, and that would give a consequence for the block grant for next year. Whether it would be more or less overall would depend on whether there were increases elsewhere to offset the cut in that area. It would not be a case of taking back money out of the budget this year; it would be a question of what the allocation of the block grant would be the following year.

Q30 **Chris Evans:** So there could be a cut to the block grant next year in that case.

Sir Tom Scholar: I can't speculate on the outcome of the spending review and what decisions will be taken, but if spending is increased in England, or England and Wales, there will be increases elsewhere, and if it is decreased, there will be decreases elsewhere.

Q31 **Chris Evans:** The point that I am trying to get to is this: what if the Welsh Government had already allocated that funding? What would you do then?

Sir Tom Scholar: As its name implies, the block grant is a block grant—a sum of money transferred in its entirety to the Welsh or Scottish Government, or the Northern Ireland Executive, as the case may be. Those Administrations make their own decisions about allocating it. Like any Government, at any point in time, they will have multi-year spending commitments that need respecting, and discretion elsewhere. Changes to the block grant would need to be dealt with through a process of prioritisation and allocation by, in your example, the Welsh Government.

Q32 **Chris Evans:** If the Chair will indulge me, I will mention a case that I think you know of. The M4 relief road has now been turned down by the Welsh Government. What if money had been allocated, on the back of the Barnett formula consequentials, to build that road? What would you have done? I know that comes out of the block grant, but how would the Treasury develop that?

Jean-Christophe Gray: Please correct me if I have misunderstood the question. The M4 levels road is a discretionary project for the Welsh Government, so in a sense, the Welsh Government was deciding whether to go ahead based on how it wanted to prioritise and allocate its resources. The moneys that it was going to spend will, I assume, now be available for other projects, but—this is where I may have misunderstood—I am not quite sure that there would be a direct read-across to Barnett consequentials, because in a sense—

Q33 **Chair:** You are saying it is just funded out of the block grant.

Jean-Christophe Gray: Yes. Once the block grant has been transferred to the Welsh Government, it is entirely the decision of the Welsh Government, through the Welsh Assembly, how it allocates that money.

Q34 **Chris Evans:** But if you have allocated the money through Barnett consequentials, and the block grant has reduced or become bigger, and then you've said, "Crossrail"—or some other project—"has been cut; we'll take the money back," and that has to be absorbed by the block grant, would a project like that be able to go ahead? If the Welsh Assembly had committed to it, but it could not go ahead, what would you have done in that situation?

Chair: I think Mr Evans is asking whether there would have been discretion for a ministerial decision to allow enough funding to keep the M4 relief road, or whatever the major project, going. Would there be any easing or smoothing of a cut? Is there a formula?

Jean-Christophe Gray: Again, it is a hypothetical, so it is quite hard to—

Chris Evans: I mean, the Welsh Assembly have said no; we know that.

Jean-Christophe Gray: I think perhaps the most helpful answer I can give is that there are financial smoothing arrangements in place; it is a feature of the Scottish devolution settlement as well as the Welsh one. Both Governments are able to borrow for capital projects. They also have a reserve. I don't know the other decisions that Welsh Ministers will be taking alongside that, but they may well be able to access those types of arrangements, should they choose to do so. As I say, there is a capital borrowing and a capital reserve facility open to them, so they might be able to use that.

Q35 **Chris Evans:** One last question before the Chair moves on. Is there a committee that you know of in any of the devolved institutions that is specifically looking at the Barnett consequentials of ministerial announcements?

Jean-Christophe Gray: I am not sure that I will necessarily get the names of the committees right. I know that the Scottish Parliament, because some of my colleagues have been in front of it relatively recently, alongside the Chief Secretary, takes a great deal of interest in all the fiscal devolution arrangements, including the operation of the Barnett formula. As I say, the Chief Secretary and one of my colleagues were giving evidence only a few months ago on all these types of issues.

Q36 **Sir Geoffrey Clifton-Brown:** Jean-Christophe, maybe I have misunderstood the mechanism—please tell me if I have—but I want to take two specific categories of spending. First, on city deals, when the 23 or whatever it was city deals for England were announced, a proportion of that funding was in the devolved settlement under the Barnett formula, yet all the city deals in Scotland were funded in full under the settlement. Can you explain how that works? Likewise, when Leeds was granted city of culture in 2017, a portion of that was given to the devolved Administrations under the Barnett formula, but for example—I know it was a little while ago—the Cardiff city of sport in 2014 was presumably funded in full under the Welsh devolution settlement. How is it fair that the devolved Administrations get that funding in full, but when England gets them, a proportion of the expenditure is given in a Barnett formula allocation to the devolved countries?

Jean-Christophe Gray: Again, it comes back to the operation of the formula following the statement of funding policy. The formula allocates funding to the devolved Administrations through a percentage of changes in funding in England—or England and Wales in some instances, such as the justice system. Where there is a change in spending in England, such as in city deals, if there is additional moneys as opposed to reprioritisation, the formula triggers Barnett consequentials. Where the UK Government chooses to allocate funds directly to a devolved Administration—in parentheses, I think all the city deals involve match funding, so it is not just the UK Government—that is obviously not changing the levels of spend in England, so the formula does not come through. Again, the hopefully straightforward answer to your question is that it is the operation of the formula, as has been consistently set out.

Q37 **Chair:** So there could be a change, but with a political decision. The only way to change it would be to have a political decision to change the formula.

Jean-Christophe Gray: Well, the short answer to that question is that there is a political ability to change. Perhaps the best answer is that the formula sits on the bedrock of spending in England, or England and Wales. It deals not with stock, but with the flow—that is, the changes in that spending, and it then allocates them proportionately to the population shares.

Chair: That is very good. One day that will be clipped as the "How to understand the Barnett formula" guide, so well done.

Q38 **Sir Geoffrey Clifton-Brown:** Obviously, the devolved countries get quite a lot of money from the EU structural funds. Has there been any commitment to replace those if and when we leave the EU?

Jean-Christophe Gray: There are two things there. In terms of what I might call the current EU financial period, and the funds that are associated with that, which, because of the way the EU budget works, can go through to 2023, the UK Government has set out a guarantee on those funds. In terms of the future, the UK Government has set out that it will introduce the UK shared prosperity fund, with regard to structural regional allocations. The Government is currently consulting—MHCLG is the lead Department—on how it will draw that up, including with the devolved Administrations.

Q39 **Douglas Chapman:** Good afternoon. What we have heard so far has underlined how complex this whole system is. In Scotland, there will be taxation changes, covering not just income tax but VAT, and social security changes. I think those will be very difficult to implement, because of some of the complexities. I am wondering what kind of discussions the Treasury could have with the devolved Administrations to make the process a bit more transparent and simpler. I think anyone outside this room will find it really difficult to get their head round where the funding comes from, where it goes and, above all, whether there is a fair allocation to all the constituent countries in the UK.

I wonder what your view is on how you could simplify the system, and how you would go about involving the devolved Administrations or Governments across the UK in that, so that they have more buy-in on what you are trying to achieve.

Sir Tom Scholar: Taking the question of Scotland, as you say, if anything, the arrangements are becoming more complicated, rather than less, with the devolution of new areas of tax and some areas of welfare policy. That was agreed between the UK and Scottish Governments in the 2016 fiscal framework, which came out of the recommendations of the Smith Commission through 2014 to '16.

Of course, that was an independent commission, but it brought together the main parties and made recommendations, and I think it is fair to say that it was a product of an extensive process of stakeholder engagement and an attempt at consensus-building. What came out of it was intended by the people proposing it to be responsive to the political debate at the time. That was then handed to the Scottish and UK Governments, for them to try to turn it into a set of workable arrangements, which we did through that fiscal framework. It is fair to say that that is in the fairly early stages of settling down. We have seen quite a bit of debate on that, including in the last few days.

I would be the first to agree that this is complicated. The Scottish Government are getting used to operating this, and we are getting used to working with them on that. As I said earlier, there is a requirement for the whole thing to be reviewed in a couple of years' time. As finance people, we like things to be simple, rather than complicated; this one is really rather complicated. The best that we can do is just keep on trying to explain. The Scottish Government also, of course, want to do that.

As I said earlier, the contribution of the NAO is significant here, and I am sure that the Committee can make a contribution too, but there is no getting away from it: it is a complicated relationship.

Q40 **Douglas Chapman:** On that relationship, the Report said: "The Scottish Government told us that it had little opportunity to scrutinise the list of programmes and comparability factors before the Spending Review 2015." To me, that does not drive us towards better government.

Some of my colleagues in the Scottish Government are of the opinion that some of their information comes through so late that it has severe knock-on effects, not just for their budget, but for the budget that they then have to allocate to local government, for example. Everyone is hanging by a thread, and although there might be discussions at your level, in terms of the Government's position, lots of decisions need to be made post-spending review and for subsequent Budget announcements. Do you feel that, across the whole of Government in the UK, each of the Departments that are responsible for their own budgets are sufficiently aware that their decisions, and maybe delays in decisions, cause problems further down the line for the devolved Administrations?

Sir Tom Scholar: The responsibility for that rests with us; we are the ones who lead the dialogue with—

Q41 **Chair:** To pick up on Mr Chapman's point—we touched on this earlier—do you think that they come to you early enough for guidance, or are announcements sometimes made without really understanding what it is that Mr Chapman is driving at—that we need to know the consequentials earlier than we sometimes do?

Sir Tom Scholar: Sorry, just to clarify, are we talking about new announcements of funding at the UK level?

Chair: Yes.

Douglas Chapman: Yes.

Sir Tom Scholar: Let us think first of spending reviews and then of announcements outside spending reviews. In the case of the spending review—

Q42 **Chair:** You kind of have a grip on that, so that is why that works quite well.

Sir Tom Scholar: But we are looking to make more progress there. We have heard, for example, the view of the devolved Administrations that in 2015, they saw the comparability factors quite late in the day and would have appreciated an earlier look at them. That is something that we have heard and are working on. We are trying to take that on board.

Q43 **Chair:** When you say earlier in the day, when are you aiming to hit it?

Sir Tom Scholar: We are working on that now. As I said, we are doing the preparatory work across the board for the spending review.

Q44 **Chair:** They are getting it late because they often set their budgets after the UK Budget—or before, in one case. How much earlier are you trying to draw that back? Do you have a long-term aim or an interim aim?

Sir Tom Scholar: I would distinguish slightly between two different things. The comparability factors, which will determine what the block grant will be in the spending review, are one thing, where we have a bit more control and will look to get them that information in good time.

The second thing, which you are also referring to, is the date of the spending review itself or, in previous years, the date of the Budget itself. Of course, ultimately that date is decided by the Chancellor, but we have a very good understanding of the need not to give the devolved Administrations nasty surprises.

Q45 **Chair:** On the comparability factors, how early do you think that you will be able to tell the Scottish and Welsh Governments and the Northern Ireland Executive?

Sir Tom Scholar: I don't think that we can make a commitment on that today but I can say that we are working—

Q46 **Chair:** You cannot make that commitment. Do you have a long-term target? In the long-term, are you hoping to do it three months earlier than you do currently? Is there an optimal time that you are aiming for?

Sir Tom Scholar: I do not think we have a particular target on that, but we are keen to get them to them in good time.

Q47 **Chair:** Okay, we will watch and see if it is earlier next year.

Sir Tom Scholar: Typically, it is at spending reviews that they get changed. They were last set out in 2015, so we are now going through the quite lengthy process of going right through what is a very large spreadsheet with lots of columns and lots of rows.

Q48 **Chair:** That is an interesting point. If the spending review does not happen as a three-year settlement and we have a sort of interim spending review, does that mean that there is a chance to look again at the comparability factors the year after this interim spending review? Would that open it all up again?

Sir Tom Scholar: It is not so much a question of opening it up, because, as I have said, we look at the legislation and ask, "Is the activity devolved or not?". It is mostly a question of making sure that it is completely accurate, up-to-date, and is also recognised as being accurate and up-to-date by the devolved Administrations.

Q49 **Chair:** So you are saying that that will happen again in a year's time?

Sir Tom Scholar: We would do that at least whenever there is a new spending review or a new set of major allocations.

Q50 **Douglas Chapman:** If Barnett worked in reverse, so the devolved Administrations kept all the taxation, made up their own spending plans and decided that they would hand money back to the Treasury to pay for foreign affairs and defence and so on, how happy would you be to not know how much you would get back from each devolved Administration? That is really the point. It is about building up that level of confidence to say that we know how much our spending will be. If you knew that you were not going to get x amount back from Northern Ireland or x amount back from Wales to pay for defence, for example, that would be a concern, would it not?

Sir Tom Scholar: We would always be very happy if anybody was giving us money back, which, I have to say, does not happen very often. In the case of the system as we currently operate it, yes, we do understand, but the Scottish or Welsh Governments need to set their budgets for the year ahead and, in order to do that properly, they need good information as to what the block grant will be.

This is a slightly different year because, as I said earlier, there are no plans for next year, so we are setting new ones. Most years the block grant is known two or three years in advance; only marginal changes ever come out of Budget announcements. This year is obviously different in that a set of quite major decisions are to be taken about funding next year. We entirely understand the need for the Scottish Government, for example, to have information on that in good time to make their own planning. I should add, that is an issue not just for the Administrations in Scotland, Wales and Northern Ireland, but for local authorities right across the country, which need to know what their own settlements for next year will be. We are very well aware of that, and keen to do everything we can to make sure that people have good time.

Q51 **Douglas Chapman:** Another layer of complexity levels will be added by whatever deal is eventually struck on leaving the EU—Brexit. What kind of plans are the Treasury making at the moment? For example, 80% of fish in the UK are landed in Scotland and we have got people who are absolutely dependent on hill farming subsidies in Wales, so each individual constituent part of the UK has its own issues with regard to what happens after Brexit. What kind of plans are in place, and how will that affect the Barnett formula, so that the money follows the area of responsibility that each of the devolved Administrations actually has?

Sir Tom Scholar: Public money that is allocated to, or spent in, Scotland, Wales and Northern Ireland from the European Union budget does not follow the Barnett formula or Barnett rules; it is determined according to whatever the EU rules are. Obviously, a very important thing that we will all need to do in developing new frameworks for after we have left the EU is to work out how to replicate or replace that funding in the future. That will be a long process of discussion and negotiation ahead.

More immediately, the policy of the Government is to have an implementation period this year and next year, in which we would still be participating in the EU budget—so structural funds, payments to farmers, research funding or science funding would continue to flow this year and next year as today, under the same system. As Mr Gray said earlier, the UK Government have also made a guarantee that, in the event that the UK leaves the EU without an agreement, the funding that people are currently expecting would still be paid. There is a parallel guarantee on agriculture payments. Obviously the situation is uncertain, and we don't know what is going to happen when, but we are doing everything we can to make sure that people understand what funding they can expect, including funding that they would until now have received from the EU.

Q52 **Chair:** If there was no deal, is there a guarantee to the devolved Administrations that they would get a relevant settlement?

Sir Tom Scholar: The guarantee on structural funds is solely and specifically in the event of no deal, yes.

Q53 **Douglas Chapman:** Does that apply to departmental funds as well, as they are released from Europe to the devolved Administrations?

Sir Tom Scholar: Yes. No matter where those payments are made to, whether to private or public sector entities, the same guarantee applies.

Q54 **Chris Evans:** I wonder whether you could explain something to me, Sir Tom. As we know, counter-terrorism has no borders whatever. Money has been allocated to counter-terrorism efforts nationally, so why are devolved Administrations benefiting from extra money when counter-terrorism happens in Edinburgh, Belfast, Cardiff or anywhere else you wish to name?

Sir Tom Scholar: Counter-terrorism funding is allocated to two different spending bodies: the police are a major recipient, as are the security services. The security services are UK-wide. It is a reserved function, so money that goes to the security services does not then lead to Barnett consequentials. But policing is devolved, so, where the money is allocated to policing, it does have consequentials. Whether there are consequentials or not depends on who the recipient of the funding is.

Q55 **Chris Evans:** It is my understanding that the consequentials amounted to

£19.8 million. Under the system at the moment, the devolved institutions decide where they want to spend their money through their budgets. Does that necessarily mean that that money has gone to the police? Do you know that?

Sir Tom Scholar: No.

Q56 **Chris Evans:** It is a weakness in the system, then. You allocated £19.8 million for counter-terrorism measures, but you are still not sure whether it has gone towards counter-terrorism measures in Scotland and Northern Ireland.

Sir Tom Scholar: That is the design of the system. It is designed to allocate changes in funding at the England or UK level to give consequential changes to the devolved Administrations, but to allow those Administrations to make their own decisions on how they allocate the money. That is true not just in counter-terrorism, but across all public services, except where there is a legal right to a particular level of spending such as in the welfare system. That is the design of the system.

Q57 **Chris Evans:** Prevent is the flagship Home Office scheme. Does that funding follow counter-terrorism police funding or is it reserved?

Sir Tom Scholar: On the precise question of Prevent funding, I don't know the answer to that.

Chair: Mr Gray?

Jean-Christophe Gray: Discretion is the better part of valour. I might double-check.

Q58 **Chris Evans:** Do you want to use the usual line, "We'll write to the Committee"?

Jean-Christophe Gray: I was desperately trying to avoid it—no.

Chair: Is "avoid promising to write" in the latest training?

Jean-Christophe Gray: Whatever you do, don't write. I will—

Chair: If you write to us and we're not happy, we'll come back to you.

Sir Tom Scholar: We will check that.

Chair: Some of that comes through MHCLG, I guess, so it depends. That is probably partly how it is allocated.

Q59 **Chris Evans:** Just one more question on the city of culture. As a Welshman, I tuned into "The One Show" and waited for the Minister to announce that Swansea was going to be the city of culture. Unfortunately, he said the wrong word and said "Coventry". Had he said Swansea, would the other nations, Northern Ireland and Scotland, have received—sorry, I don't know who the competitor was in Scotland—

Gareth Snell: Paisley.

Chris Evans: Paisley. Had they said Paisley or Swansea, would the other nations have had additional funding because of that?

Jean-Christophe Gray: I think that if the UK Government was making a direct payment to that Administration, then no, because it would not be a change in funding in England. I only paused because I do not know the ins and outs. If there was also some wider funding going through DCMS, it is possible that there might be some small amount.

Q60 **Chair:** Could you check what the consequentials are for that particular allocation?

Jean-Christophe Gray: If I understood the question, there has not been a consequential allocation for Swansea, so I cannot check it.

Q61 **Chris Evans:** He said Coventry when he should have said Swansea—somebody wrote the wrong name on the letter.

Jean-Christophe Gray: But there will be a Barnett consequential from money going to Coventry because it is in England.

Douglas Chapman: Given that the MSP for Paisley is also the Finance Minister in Scotland, I am not sure what would have happened there in terms of additional funding. Strange things happen sometimes.

Chair: It's cheaper. You don't have the competition next time; you've got two good runners-up.

Q62 **Douglas Chapman:** Overall, there seems to be quite a disparity in the perceived level of spending across Northern Ireland, Wales, Scotland and England. Northern Ireland is highest at just over £11,000 per head and England is just over £9,000 per head. What is the reasoning behind why that situation has developed? What is your understanding of how these disparities have taken place?

Sir Tom Scholar: As I said, by a long way the biggest determinant of funding levels is the Barnett formula. It allocates changes to spending according to the extent to which a policy is devolved or not, and population. It has been in operation for 40 years. The baseline from 40 years ago was one in which there was higher spending per head in Scotland, Wales and Northern Ireland than in England—that is a long-standing historical thing. What the origins are back in the mists of time I do not know. Since that has been baked in for at least 40 years and probably considerably longer, that is the main reason for the difference in spending per head that you observed.

Q63 **Douglas Chapman:** If you were presenting that to the public, I take it that does not include any additional spending that might happen through Government Departments—DFID, the Foreign and Commonwealth Office, MOD and so on. How would that figure look if all those other Departments' spending was taken into account? Can you break it down by constituent nation?

Sir Tom Scholar: I think it would be very difficult to do that, certainly in the case of the FCO or overseas development assistance. I do not know on what basis you would allocate that. That is the classic case of a reserved matter, because the country's foreign policy has a similar effect on all parts of the country.

Q64 **Douglas Chapman:** It does have an impact on the level of spend in each country. The example I have here is that the Defence agency based in Bristol employs 13,000 people. I can only imagine the kind of budget that it has, given the nature of its work—at the Defence Equipment & Support centre, I imagine that quite a lot of people would be on fairly robust salaries. I do not think that the figure you gave beforehand includes any of that kind of spend. It is easy to try to compare apples with pears, but it does not work like that. You are trying to say to the general public the levels of spending in each country, but they do not include a whole raft of spending that goes on in Government. Is that an accurate way of looking at it?

Sir Tom Scholar: I am thinking now of the general picture. If you look at Government Departments in general and their running costs, including the salaries that they pay out, most Departments have operations up and down the country. The Ministry of Defence would be one example that is nationwide, up and down the country; equally, HMRC, the DWP or the Department for Transport. We can readily think of different offices across different parts of the country. I am not aware that we or anyone has ever produced an assessment of what I think you are angling for—a regional breakdown of UK Government spending on salaries. I do not think I have ever seen such an analysis.

Douglas Chapman: That is one of the criticisms with Barnett, because it looks like some of the devolved Administrations are getting an unfair advantage when it could be argued that the absolute opposite is the true picture. If we do not have those figures, you can neither prove nor disprove where Government money is being spent. Would that be the case?

Sir Tom Scholar: The Barnett formula is used to calculate the block grant, which is money provided to purchase public services. That, I think, is a different question from the direct contribution to the local economy of Government procurement or Government wages and salaries.

Q65 **Chair:** Certainly that is true, but it is also true—if you think about investment, there is the campaign today about the northern powerhouse by the local papers up there wanting investment in the very broad north of England. I know when the Government were recently announcing a pot of money that could go to certain areas, partly around some of the Brexit issues, some MPs were saying, "We do not want one-off pots of money. We need proper investment, and that means jobs." That can mean devolving Government tasks and parts of Departments out to areas. I know it is not strictly the Barnett formula, but it is investment, but in kind. Is there anywhere in the Treasury that that is measured? It is not really a BEIS issue, is it? Where would that be measured in the

Government?

Sir Tom Scholar: I think it is the Cabinet Office that leads this. There is a cross-Government attempt to move more civil service jobs out of London and the south-east and across the rest of the country. That is a Cabinet Office policy area. What I do not know is what information is either available or published that tells you what the current distribution of Government wages and salaries is across the country. I do not know the answer to that, but I can certainly look into it.

Chair: I don't think Mr Chapman is suggesting that it should be included in the Barnett formula, are you?

Q66 **Douglas Chapman:** I am not suggesting for one minute that it should be included. We are looking at national variations. When people look at that, they make a value judgment on who is getting what from the national cake. It is perhaps misleading that there are other tranches of spend that the Government make where Wales, Northern Ireland and Scotland do not benefit, because the system of government in England is so interlinked with the existing Departments that they are treated as one. They are not UK Departments. Departments such as Housing are just for England. We get the consequentials, as do Wales and Northern Ireland, but it is hardly a level playing field. I do not know whether you have a view on that, Mr Gray.

Sir Tom Scholar: While he is collecting his thoughts, in the particular case that you raise with the Ministry of Defence, it is true that there is a major centre in Bristol, but of course there are some very large Ministry of Defence bases in Scotland, generating a large number of local jobs, including through supply chains. The Ministry of Defence is an important employer in Scotland, but also right across the country.

Q67 **Douglas Chapman:** Will you write to the Committee on that? Is that the plan?

Sir Tom Scholar: Yes.

Q68 **Chris Evans:** A large part of the Barnett formula calculation is based on population, yet the historical part of the block grant just rolls forward without taking population into account. How do you arrive at that, Mr Gray? Can you just walk me through that?

Sir Tom Scholar: Tell me if this is wrong, but the simple answer to that is that in 1978, when the formula was first developed by the Treasury, it was designed as a way to reach agreement with, at that time, the Scotland Office on funding for the year ahead. They took the existing level of spending and just agreed a marginal change, in which at the margin they would look at changes in population. That was initially intended as a one-year settlement, but it then got rolled on and on and on. No one has ever changed that element of it. I think that is—

Q69 **Chris Evans:** My understanding is that it does not take account of population changes, even though the population has increased in all the home countries in the past 40 years. Is that correct?

Sir Tom Scholar: No. The formula, as the Report clearly says—

Q70 **Chris Evans:** This is the historical part of it.

Sir Tom Scholar: Yes. It does not go back and calculate the baseline. It does not adjust that for population change. Of course, it is only to the extent that there is a relative change in population that it matters, because if the change in population was exactly the same across all parts of the country, that would just drop out of the figures. To the extent that there is a relative change in population, there is a consequence. Now, you could redesign the formula to take account of that. The consequence of that would be some areas would win and others would lose, and some people would be pleased and some would not be pleased. There is no magic way of taking away disagreement or controversy over this.

Q71 **Chris Evans:** Just based on that point, if we were talking about calculation of population, how sensitive would that be? Would you include, for example, immigration, migration, or people just moving? What would be included in that calculation?

Sir Tom Scholar: My understanding is that—I am not sure which figures are used for looking at population, but it is population defined in the full sense.

Chair: Whoever is living there.

Sir Tom Scholar: So how many people are living there and what the change in population of the country is, whatever the source of that change.

Q72 **Chair:** It is purely numbers, is it? It is not, for instance, looking at a Welsh valley where it might be more difficult to deliver certain services to a population because of the geography, compared with, say, Shoreditch. You are nodding, Mr Gray.

Sir Tom Scholar: In respect of the Barnett formula, it is purely numbers. In respect of Wales, as it happened, one of the things that the Holtham commission assessed was the greater cost of providing services where populations are dispersed.

Q73 **Chair:** But not in somewhere like the Western Isles, where obviously there must be a huge cost to delivering services.

Sir Tom Scholar: I think other mechanisms have been used to try to cater for the special needs of the Highlands and Islands.

Q74 **Chair:** The more we talk about it, the more we realise the imperfections of the formula.

Sir Tom Scholar: It is not a scientific business.

Chair: Exactly. It is what it is.

Q75 **Chris Evans:** That is an interesting point. Sorry to be philosophical about this, but if you look at the Holtham commission, they talked about allocated need. To the Chair's example of the Valleys, they do have the highest level of need, but they also have the highest level of migration out of there: people moving to Cardiff. If you based it on that, Cardiff would be the winner there, which is the most populous area in Wales. Am I right?

Sir Tom Scholar: Where the relative population of Cardiff and other parts of Wales comes into the calculation is when the Welsh Government then chooses to allocate its resources between different parts of Wales.

Q76 **Chris Evans:** Why do you need to allocate direct funding outside of the Barnett formula process?

Sir Tom Scholar: Let me start, and Mr Gray can add as need be.

The statement of funding policy, which I think we first published 20 years ago and have revised several times since, explains the whole Barnett formula, but then also makes it clear that UK Ministers ultimately have the flexibility to allocate resources as they decide, including outside the formula to the nations and regions of the country. Those are decisions that are made by Ministers on the basis of perceived need in different areas. I mentioned earlier the question of particular allocations for policing where a particular issue arises in, say, Northern Ireland—or, actually, a couple of years ago when the President of the United States visited the UK. He visited Scotland as well, and that imposed a particular cost on Scottish policing. We were able to fund that directly.

More recently, city deals are maybe an area that is an interesting recent development, and has led to—I think I would be right in saying—a larger share of funding provided outside the Barnett arrangement than had existed until, say, five years ago. As I said earlier, those city deals are assessed on the basis of business case, local support and local funding, and we look at bids from wherever in the country they come from, but I think it is an interesting area. It is now a significant quantity of funding that is being allocated, at least in part, outside the Barnett process.

Q77 **Chris Evans:** I am going to be mischievous for a minute and roll back to the earlier part of your answer about Northern Ireland. Some £410 million was allocated through a deal done between the Government and the Democratic Unionist party. How was the Department justified in not paying consequentials to other nation states when Northern Ireland received an increase in direct funding because of that deal?

Sir Tom Scholar: The straightforward technical, mechanical answer is that the Barnett formula only calculates consequentials from increases in funding in England. In the case of the agreement between the Conservative party and the DUP, that was additional allocation in Northern Ireland, so it does not enter into the Barnett calculation. That is not to say whether that is in any sense the correct or the incorrect outcome; it is just a description of the way the formula works.

Q78 **Chris Evans:** Were there any discussions in the Department before that deal was signed about the impact that would have on the other nations—

in particular England, which has lost out in all this as well?

Sir Tom Scholar: The negotiation of the funding happened as part of the negotiation of a confidence and supply arrangement. That was a negotiation between the Conservative party and the DUP. As part of that negotiation, the £1 billion funding was agreed. That funding has now been translated into a UK Government-Northern Ireland Executive agreement, but the number came from the process between the two parties. We were not involved in that process.

Chair: It was a political fix.

Q79 **Chris Evans:** So that was a decision imposed on you for a political fix?

Chair: It was a Government decision in the end.

Chris Evans: It became a Government decision.

Chair: I think Sir Tom has been pretty candid, actually, for the Treasury.

Sir Tom Scholar: As I say, it was not our negotiation. It was a discussion between the two parties.

Q80 **Gareth Snell:** Sir Tom, unless I am being somewhat naïve in my interpretation, what you describe renders the last hour and a half entirely moot. If a Minister or the Government of the day decide they want to give any nation or region of the United Kingdom any money it likes, they can, as long as they feel they can justify it to themselves, regardless of what the Barnett formula says and regardless of the core block funding.

You made the point that Governments can spend money only if Parliament grants it. Why was there no parliamentary scrutiny of that £410 million? Why was there no parliamentary sign-off of that £1 billion decision? Regardless of the consequentials, if Ministers can just give as much money to the nations as they wish, what is the point of the Barnett formula and all the other revenue streams we have discussed in the last hour and a half?

Sir Tom Scholar: Taking that second question first, the Barnett formula is by far the largest determinant of what gets allocated to which part of the country.

Q81 **Gareth Snell:** I appreciate that, but that is not my point. We all know majority Governments can do whatever they want—fine. We have talked a lot about the mechanics of the various formulas that are in place, but in your answers to Mr Evans in the last two minutes you seemed to allude to the fact that a Minister—the Prime Minister—can, should they choose to, give an indiscriminate amount of money of their choosing to Wales, Scotland or Northern Ireland as they see fit, and, as long as they see fit to do so, the money is available from the Treasury and it is all fine. What is the purpose of having all these structures and levers in place to secure fair and balanced allocations based on per capita spends and various other things, but on the other hand having a massive free-for-all for whoever has the stickiest fingers and can make the best argument for votes in this place?

Sir Tom Scholar: The purpose of the system is to provide a system for decisions on those allocations. As I said earlier, the statement of funding policy has always been clear that UK Ministers in the end can make decisions on the allocation of resources. Those decisions, by the way, are not just ministerial decisions; they have to be voted by Parliament as well. The additional money made available to the Northern Ireland Executive was also voted by Parliament.

Q82 **Chair:** You have great faith in Parliament. The estimates process is woefully inadequate. We cannot really reject things. It is very hard to do that. We have tried, and it does not happen very often. The way you described it earlier was, "Once it's gone through the estimates process, the devolved Administrations know it's coming anyway." Are you suggesting that if it was outrageously pork barrel politics, you would have faith in Parliament to knock it back?

Sir Tom Scholar: The main thing I am suggesting is that, if you look over the years, by a very large majority the overwhelming percentage of the funding allocated to the nations within the UK is determined by the Barnett formula. There are changes now because of tax devolution and I think there have been recent changes in respect of city deals which in part are direct-funded, but those are a very small part compared to the amount that comes through the formula.

Q83 **Chair:** But a Government could decide just to do this. So you could have, for example—this is not a crazy scenario—a Government in power and the same party in a devolved nation making grand promises in their manifesto that they would deliver x, y and z, knowing that a decision could be made in the Treasury by a Treasury Minister or a UK Minister or Prime Minister to fund that in some side deal. That would be legitimate within the rules because it is a political decision. That could happen, couldn't it?

Sir Tom Scholar: In the end, in our system of Government, Ministers propose the allocation of resources that Parliament ultimately approves. We do not have a system that prevents Ministers from doing that.

Q84 **Chair:** Would you need a ministerial letter of direction for something that out there, saying, "We are going to build a bridge across Mr Evans's valley to get him re-elected" or his party re-elected, or whatever, in his country?

Sir Tom Scholar: The question of a direction would then arise for whichever Department it was that was administering the money. But relative spending across different parts of the country is inevitably and inescapably a contested and contestable area, as we see from this discussion. There is no getting away from that.

What we have here is a system that has lasted for 40 years and, in successive elections, the main parties have said they remain committed to it. In the case of Wales, with the Holtham commission, and Scotland, with the Smith commission, it has been examined, and again the consensus has been that this is a pretty good way of allocating resources. Ultimately it does not prevent UK Ministers from making decisions outside it, but it is a pretty important constraint and an important guide as to where we will end up.

Q85 **Gareth Snell:** It is a guide that they can wilfully disregard, should they choose to, for political or other purposes. I am afraid, Sir Tom, I do not buy the argument, "We have always done it this way, so it is the best system we can have."

I appreciate that that is a policy decision and outside the purview of the answers you can give today, but if we are saying that the Barnett formula is the best way of allocating additional resources and the block grant, through its needs-based assessments, yet one day an incoming Labour Government—heaven forbid—could decide that it quite likes being in power in Wales, so Wales will get an additional £2.5 billion of expenditure without any consideration of need, projects or what that means for Northern Ireland or Scotland, that raises a question.

If that level of discretion is available, what on earth are the safeguards for that? More importantly, what is the point of a Barnett formula, particularly in a hung Parliament, where pork barrel politics, to use an American phrase, is becoming more and more prevalent in our decision making processes? I do not expect you to answer all those points.

Chair: I think Mr Snell was holding forth on his concerns. You are welcome to come back with a quick response, if you wish, before we move on, but we do need to move on.

Sir Tom Scholar: Right at the beginning of the hearing, I said that what the Barnett formula cannot do is answer the question, "What is the right level of funding or allocation of resources?".

Q86 **Chair:** But you are saying it is at least as fair as the alternatives. Is that what you are saying?

Sir Tom Scholar: I am not making any value or qualitative judgment about it. I am not saying it is the best. I am not saying it is the fairest. I am not defending it; I am explaining it. My job is to explain it.

Chair: Or is this tempting us to hold another inquiry?

Q87 **Gareth Snell:** If you had to explain a better system, what would that look like?

Sir Tom Scholar: Let me explain briefly a different system. Let me tell you what happens in India. India is obviously a very large country, also with a very complex devolution map—state powers and federal powers in different respects. In India, I think every seven years they set up an independent commission, which is always chaired by a retired senior official.

That senior official travels up and down the country doing town hall meetings, taking representations from local people—representations not just on the allocation of spending, but on the sharing of revenues. It covers both spending and revenue, and is an immense process. It takes about two years, and at the end of that process, the committee of officials make their recommendation to the federal finance ministry, and their recommendation is: "Here is the proper revenue-sharing arrangement and, alongside that, here is the proper distribution of spending." In the whole history of India since independence, the Government have never once turned down the recommendation.

Q88 **Chair:** Sounds like a dream job for a retired Treasury mandarin.

Sir Tom Scholar: No thanks. To turn down that recommendation would, in effect, mean starting all over again, because it is the process of an immense argy-bargy. We could do that in this country; ultimately, it is up to Parliament.

Q89 **Chair:** A retired Sir Tom Scholar might be the first to do it. Are you offering?

Sir Tom Scholar: I am not seeking that. That is just an illustration of the fact that in any country with an important element of devolution in its structures, there is no right answer.

Chair: I have to say, from an official's point of view, stitching it in, because it takes too long to do it again, is one way of resolving funding issues and taking them out of the hands of politicians.

Q90 **Chris Evans:** Before we leave, I wanted to ask one question on the reserve fund. Are you concerned that the money allocated for Northern Ireland to prop up the Government came out of a reserve fund that was meant for nations according to where it was most needed? The Treasury guidance states: "The drawdown of funding from the Reserve is subject to an assessment of need, realism and affordability at the time at which the funds are released." It seems to me that the need to stay in power outweighed the needs of anything else.

Sir Tom Scholar: If you look at the question of need, there are certainly arguments that you can make for the allocation of additional funds in Northern Ireland, taking into account, for example, relative income, the state of the local economy and so on. As I said earlier, the decision on allocation was reached through a negotiation between two political parties, but once that allocation has been made, the money has to be spent in accordance with all the usual principles of spending public money in this country, including value for money. Once the money had been allocated to the Northern Ireland Executive, the same rules applied for spending it as would apply in other parts of the country.

Q91 **Chris Evans:** Does that not make a mockery of the need for additional funding? What you are saying is that just because Northern Ireland has DUP MPs, who are going to prop up the Government, their needs outweigh the needs of impoverished places in Wales, Scotland and parts of England. Is that right?

Sir Tom Scholar: There are other areas where the political process has led to changes in funding in other areas of the country. For example, the

Smith commission in Scotland was set up following the referendum and the expression of views of many people in Scotland about the extent of devolution, including fiscal devolution. Similarly, the Holtham commission was responding to a lot of comments and arguments on relative needs in Wales.

As I have said a number of times in this hearing, every part of the country, including regions in England, is able to make a strong case for their own particular needs. City deals, for example, are one way in which the Government have been able to respond to that. I am sure that different parts of the country will go on doing that. There are many examples across all the areas that we are talking about of political pressure being applied, and of there being some response to that.

Q92 **Chris Evans:** Time is against us, so I will be quick with my last two questions—I would have liked to go on to city deals as well, but I can't. In terms of special cases, why does Wales have a needs-based factor in its funding?

Sir Tom Scholar: Because that was a recommendation of the Holtham commission and has been incorporated into the fiscal framework agreed between the UK Government and the Welsh Government.

Q93 **Chris Evans:** How likely is that to be rolled out to Northern Ireland and Scotland in the future?

Sir Tom Scholar: I would be surprised if there were any major changes to this framework in Scotland in the next couple of years. By the end of 2021, there will be an independent review of the framework in Scotland as it has operated over five years, and we will be able to take all this sort of thing into account at that time.

Q94 **Chris Evans:** My last question is very pertinent. Wales is heavily reliant on EU funding, receiving around £680 million at the moment. What are you going to do to make up that shortfall? What plans have you got for that shortfall?

Sir Tom Scholar: While the UK is still participating in the EU budget—under Government policy, that will be the case this year and next—and that situation continues, Wales and other parts of the country will continue to have the same entitlement to EU funding that they have today. That is the first point. The second point is that in the event of the UK leaving the EU without an agreement and stopping participating in the budget, the UK Government has made a guarantee to recipients of that funding that they will continue to receive the same funding. The third point is that an important part of our leaving the EU is that as a country—this will be for negotiation and debate—we will need to decide how we replace services and funding currently provided by the EU.

Q95 **Chris Evans:** You allocated money to the devolved Administrations for preparations for Brexit. It's the old chestnut: how can you ensure they are spending that money on Brexit preparations?

Sir Tom Scholar: It is up to them. This money gets added to the block grant, and they decide how they allocate the block grant.

Q96 **Douglas Chapman:** You mentioned challenging Treasury decisions. To what extent do the devolved Administrations have an ability to challenge some of the decisions that you have made on funding settlements?

Sir Tom Scholar: We have a mechanism for this. We have arrangements at official level. If there is a dispute, or an Administration think we have made a mistake or an incorrect allocation, ultimately those can be raised at ministerial level in the Joint Ministerial Committee, which the Prime Minister chairs.

Q97 **Douglas Chapman:** What was the last one that you can remember being successful for either of the devolved Administrations?

Sir Tom Scholar: I recall there was a dispute about money allocated to the Olympic Delivery Authority—whether there should have been consequentials for that. In the end, I think that was something the Treasury agreed to. Off the top of my head, I cannot remember any other more recent examples. That is because nearly all of the time, as operating the Barnett formula is a mechanical process, no dispute arises over it. As you said earlier, sometimes people say, "Could you please tell us more quickly?" but it is rare for there to be a dispute over whether it has been correctly applied.

Q98 **Douglas Chapman:** The other issue is that we had a discussion last week about the future of the NHS and whether it is more open to privatisation. Education is a big spending area, and the NHS accounts for a huge spend in Scotland, Wales and Northern Ireland. If the Department of Health decided to privatise a whole part of the NHS, what kind of effect would that have on the Barnett formula?

Chair: Basically, if it is taken out of Exchequer spending for whatever reason, or reduced?

Sir Tom Scholar: It is not something I have previously considered. Since health in Scotland is a devolved matter, my understanding—this is not really a funding question, but a question of how to operate the service—is that it is for the Scottish Government to decide.

Q99 **Douglas Chapman:** What would the impact be of a policy decision made in Whitehall that said, "We're going to have more privatised services"?

Chair: So a reduction in the taxpayer-funded element of a service. Let us say that we all had to pay £10 to go to the GP in England. That would be extra money for the NHS, or reducing the NHS budget, depending on how you look at it, but that would be less taxpayers' money for the NHS, because it would be a direct subsidy by individual patients. Would that have a consequence for the allocation to Scotland, Wales and Northern Ireland?

Sir Tom Scholar: Of course, there is already an example of that in the system: the Scottish Government treats prescription charges in a different way.

Douglas Chapman: But that is a reversal—

Sir Tom Scholar: Exactly; that is the other way round. In effect, what you are talking about is replacing public funding of the health service with private funding to a large degree. That would be of such magnitude that it would inevitably lead to a complete reconsideration. It is not something that you would just do—

Douglas Chapman: But surely there must be parts of the NHS that are being put out to private tender and so on at the moment that do not—

Q100 **Chair:** But they are still funded by taxpayers. The difference is where they are still funded by taxpayers, even if it is a private provider. What we are talking about here is if it is the individual’s insurance or individuals paying for some of the cost. You are saying that it would be such a fundamental change that you would have to go back to the drawing board, in your view.

Sir Tom Scholar: I would have to think about it more carefully, but I think that is the answer, yes.

Chair: That is very clear, thank you.

Q101 **Douglas Chapman:** I have another point about the situation in Scotland with regard to the new taxation system and the way the system works. There is quite a considerable time gap between what the Government are expecting to have in taxation revenues and what might actually be collected. Again, what are the processes in place to try to smooth that out, so we do not have a feast and famine situation, and so the new taxation system can bed in properly, without Scotland being so adversely affected annually by the ups and downs of the taxation that is collected?

Sir Tom Scholar: This situation is not unique to Scotland; in fact, it is common to all Governments, including the UK Government. In the UK Government, we make our tax and spending decisions for the future based on forecasts, both of spending and of tax receipts. Inevitably, those forecasts sometimes turn out to be wrong—sometimes we have more receipts than we are expecting, and sometimes we have fewer. At the UK level, we deal with that through varying borrowing from year to year; we have the public expenditure reserve; and sometimes we have to make changes to tax policy or to spending.

That is exactly the situation that the Scottish Government also has under its fiscal framework—it has borrowing powers, and it has a reserve provision, precisely to help it to cope with the ups and downs of tax revenues. As you suggested, the system is just bedding in, so I think it is completely to be expected that people take a bit of time to get used to that, but the framework is designed to be robust to changes in tax receipts, because that is just a normal part of budgeting and forecasting.

Q102 **Chair:** I want to ask a further question on the transparency issue that we touched on right at the beginning. What plans do you have to make it easier for people to understand? In the whole of Government accounts, which we will obviously be talking to you about soon, you have a bit about the big blocks of money, but do you have any plans to make it simpler and easier for people to understand, so they can avoid having to sit through the whole of the Public Accounts Committee, and can just go to one place and find it?

Sir Tom Scholar: We will discuss the whole of Government accounts next Wednesday, I think, and as I mentioned earlier, an important part of that is the analysis of spending by nation and by region. Transparency is something that we have worked hard on. We think that we provided more transparency around the 2015 spending review in how the allocations were made. That is something that we really want to build on in the next spending review. Perhaps I can turn to Mr Gray, who can tell you a bit about what we have done and where we are thinking of pushing it further.

Jean-Christophe Gray: 2017 was the first publication of the block grant transparency publications. That is twofold; it explains the methodology for each of the constituent nations of the UK and for every single budget line per Department. It lists the calculation and shows you how it was done. That was introduced in 2017, so we are only two years in.

Q103 **Chair:** And that is a result of what our sister Committee, the Public Administration Committee—

Jean-Christophe Gray: Yes, that is right. It was a recommendation from the Commons Public Administration Committee. We have put that in place and will continue to look at it. If there are changes that the devolved Administrations would like us to make to that—

Q104 **Chair:** I have to say that it's great that it's happening, but it's incredible that it took until 2017.

Jean-Christophe Gray: We touched on another element. In fact, it triggered a question about the NHS Barnett consequentials. The Government, at the time of last year's NHS funding announcement, published its guidance on what the Barnett consequentials might be in a written ministerial statement. That was a relatively new thing to have done.

As we work up the spending review guidance and engagement, we will continue to look at what more we can do. At the risk of a bit of granularity, Scotland has some of the most developed fiscal devolution, and there is such a debate, which we have just been touching on, about fiscal policy there, so one of the things that the Treasury is trying to do—I am sure we can do more of it—is step up its engagement with stakeholders such as the Fraser of Allander Institute, which is a bit like the Scottish version of the Institute for Fiscal Studies, as we try to play a full role in the debate around these funding decisions.

Chair: We could have a whole other conversation about that, but we will pause it there. We will reflect on what we do, and whether or not we will have you back at some point to discuss the Sir Thomas Scholar retirement plan as an option. You put a bid in, Sir Tom; we won't let you forget it. Our sister Committee, the Treasury Committee, deals with policy, so we will talk to them if we think about taking it further, as well as PACAC.

Thank you very much indeed for your time. Thank you for appearing in front of us for the first time, Mr Gray. As ever, we will be publishing the uncorrected transcript on the website in the next couple of days, thanks to our good colleagues at Hansard, and we will be producing our next report on this maybe just before we have a new Prime Minister.