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# **A BACKGROUND PAPER ON THE BARNETT FORMULA**

This research paper provides background information that is essential to understanding the Barnett Formula and its implications throughout the United Kingdom, particularly in Northern Ireland.

Research Papers are compiled for the benefit of Members of the Assembly and their personal staff. Authors are available to discuss the contents of these papers with Members and their staff but cannot advise members of the general public.

## SUMMARY OF KEY POINTS

- This research paper was prepared for the Committee of Finance and Personnel (the Committee) to provide background information on the Barnett Formula.
- The “Barnett Formula” is a non-statutory mechanism used by central government in the United Kingdom (UK) to apportion public expenditure changes to Northern Ireland, Scotland and Wales: it is based on population, not need.<sup>1</sup> Thus the Formula determines the change to the inherited level of spending for each devolved administration, namely the Northern Ireland Assembly, the Scottish Parliament and the National Assembly of Wales.<sup>2</sup>
- Three pieces of basic information appear essential to understanding the Formula and its implications. First, the Formula concerns the public expenditure category of devolved administrations’ total budgets that is set over three year periods, namely Departmental Expenditure Levels (DEL); specifically those items in DEL that are within the assigned budget of the UK central government, i.e. most programme spending, (e.g. health, education, housing).
- Second, the Formula has been considered a robust mechanism for public expenditure allocation for 20 years, despite its apparent intended temporary use. It largely replaced the need for direct negotiation about public expenditure allocation between UK Treasury Ministers, Secretaries of States and Ministers of devolved administrations, which were very time consuming.<sup>3</sup> But the Formula’s long history appears to have been far from straightforward.
- Third, three factors are used to determine the net change under the Formula to the spending allocations for each devolved administration. These factors include the following:<sup>4</sup>

Change to the department of the UK Government’s Programme	X	Comparability percentage	X	Appropriate population proportion
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- There are various implications of the Barnett Formula. Amongst the practical implications relating to Northern Ireland, England, Wales and Scotland include are, e.g., insufficiency and incomparability of relevant financial documentation, higher spending per head in devolved administrations, and the “Barnett Squeeze”. (Section 2.1 of Part 2 of this paper explains these and other practical implications.) On balance, it appears that both positive and

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<sup>1</sup> The Formula is commonly referred to by its inventor, namely Lord Joel Barnett, formerly Chief Secretary to the Treasury.

<sup>2</sup> HM Treasury. *Funding the Scottish Parliament, National Assembly for Wales and Northern Ireland Assembly*. (A Statement of Funding Policy). 31 March 1999, p. 6. See <http://www.hm-treasury.gov.uk/pub/html/docs/swni.html>.

<sup>3</sup> See the evidence of Her Majesty’s Treasury in House of Commons Select Treasury Committee. 22 December 1997, p. 12.

<sup>4</sup> Ibid, p. 6, para 3.5.

negative effects arise from these practical implications for Northern Ireland, Scotland and Wales, as well as for England.

- The Barnett Formula has a number of identified advantages and disadvantages. Amongst such advantages are, e.g.: (i) higher spending per head for Northern Ireland, Scotland and Wales; (ii) devolved administrations' discretion to allocate; and (iii) the Formula's objectivity.
- Whereas amongst such disadvantages are, e.g.: (i) population-, not needs-based Formula; (ii) potential erosion of the protection that the Formula was intended to afford to inherited expenditure; and (iii) lack of openness and transparency in the application of the Formula.
- There appears to be growing consensus for a review of Barnett's use in the UK. It seems two clear positions have emerged, i.e. (i) replace Barnett and (ii) retain it. This paper highlights that a replacement of the Formula with a needs assessment-based mechanism may be fraught with difficulties, particularly in light of past discussions about developing such a mechanism.
- Governmental positions throughout the UK concerning Barnett's use highlight both potential support and lack of support to reform the Formula. (These positions are outlined in Section 3.2 of Part 3 of this paper.)
- It remains uncertain as to what Westminster's intentions are for the future use of Barnett in the UK; although the Government announced that the Formula would remain in place until at least 2004.
- Given the apparent complexity of the Barnett Formula, the Committee may find it appropriate to seek specialised assistance from both inside and outside the Department of Finance and Personnel to fully formulate its views in this area. Such specialised assistance could authoritatively expand on the points raised in this paper.

## CONTENTS

<b>INTRODUCTION</b> .....	1
<b>PART 1:</b> .....	2
<b>SECTION 1.1 - THE DEPARTMENTAL EXPENDITURE LIMITS (DEL)</b> .....	2
What are DEL? .....	2
How do DEL relate to the Barnett Formula? .....	3
<b>SECTION 1.2 - HISTORY OF THE BARNETT FORMULA</b> .....	3
What is the Barnett Formula? .....	3
Underlying Reasons of the Formula .....	5
Since Barnett’s Introduction .....	5
<b>SECTION 1.3 - BARNETT’S CURRENT THEORETICAL AND PRACTICAL APPLICATION</b> .....	7
Theoretical Basis of Barnett.....	7
Practical Example of Barnett .....	8
<b>PART 2:</b> .....	10
<b>SECTION 2.1 - PRACTICAL IMPACT OF BARNETT THROUGHOUT THE UK</b> .....	10
<b>SECTION 2.2 - IDENTIFIED ADVANTAGES AND DISADVANTAGES OF BARNETT</b> .....	12
Advantages.....	12
Disadvantages .....	13
<b>PART 3:</b> .....	15
<b>SECTION 3.1 – POTENTIAL REVIEW OF BARNETT AND PROPOSED ALTERNATIVES TO IT</b> .....	15
Review and Potential Replacement of Barnett .....	15
Retention of Barnett.....	16
<b>SECTION 3.2 - CURRENT POSITIONS ON THE BARNETT FORMULA THROUGHOUT THE UK GOVERNMENTS – POTENTIAL BARNETT REFORM?</b> .....	17
<b>PART 4: CONCLUSION</b> .....	19
Appendix A – HM Treasury Funding Principles .....	21
Appendix B - Comparability Factor in the Barnett Formula.....	23
Appendix C - Population Proportions in the Barnett Formula .....	25
Appendix D - Public Expenditure Statistical Analyses .....	27
Appendix E - Needs Assessment - Background Information .....	37
Bibliography.....	41

## **INTRODUCTION**

The “Barnett Formula” is a non-statutory mechanism used by central government in the United Kingdom (UK) to apportion public expenditure changes to Northern Ireland, Scotland and Wales: it is based on population, not on need.<sup>5</sup> Thus the Formula determines change to the inherited level of spending for each devolved administration.<sup>6</sup> It does not determine the expenditure totals for the devolved administrations - namely the Northern Ireland Assembly, the Scottish Parliament and the National Assembly of Wales.

This paper is prepared for the Committee of Finance and Personnel (the Committee) to provide background information that is essential to understanding the Barnett Formula and its implications. The paper largely draws on secondary sources of information, and should be viewed only as a useful starting point to assist the Committee in developing its understanding of the Formula. In using this briefing, the Committee may find it appropriate to seek specialised assistance from sources both outside and inside the Department of Finance and Personnel to fully formulate its views in this area. Such assistance could authoritatively expand on the points raised throughout the paper.

Part 1 outlines basic information about the Formula and its implications. It includes three sections. Section 1.1 contextualises the Formula. It sets out in basic terms (i) what Departmental Expenditure Limits (DEL) are; and, (ii) how DEL relate to the Barnett Formula. Section 1.2 proceeds with a history of the Formula, in particular an outline of (i) its original formulation, (ii) the reasons for its introduction, (iii) what it replaced and (iv) alterations to it since its introduction. Section 1.3 proceeds with an explanation of the theory currently underpinning the Formula, accompanied by an illustration of how it presently works in practice.

Part 2 includes two sections that analyse various implications of the Barnett Formula. Section 2.1 specifically outlines practical implications of the Formula in relation to Northern Ireland, England, Wales and Scotland. Section 2.2 discusses identified advantages and disadvantages of the Formula.

Part 3 provides background information that is relevant to any discussion on the future use of the Barnett Formula in the United Kingdom. It includes two sections. Section 3.1 examines the issue of potential review of the Formula, highlighting calls for its replacement as well as its retention. Section 3.2 outlines current positions on the Formula in each devolved administration in the UK and the UK’s central government (Westminster), highlighting both potential support and lack of support to reform the Formula, if Northern Ireland actually sought such reform.

Finally, Part 4 concludes drawing on main points from each section, outlining key findings about the Barnett Formula and its implications.

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<sup>5</sup> The Formula is commonly referred to by its inventor, namely Lord Joel Barnett, formerly Chief Secretary to HM Treasury.

<sup>6</sup> HM Treasury. *Funding the Scottish Parliament, National Assembly for Wales and Northern Ireland Assembly*. (A Statement of Funding Policy). 31 March 1999, p. 6. See <http://www.hm-treasury.gov.uk/pub/html/docs/swni.html> .

## **PART 1:**

### **SECTION 1.1 - THE DEPARTMENTAL EXPENDITURE LIMITS (DEL)**

Prior to a discussion on the Barnett Formula, it first is necessary to highlight the context in which the Barnett Formula is used, i.e. public spending, and more specifically the Departmental Expenditure Limits (DEL). This section sets out in basic terms – (i) what DEL are and (ii) how DEL relate to the Barnett Formula.

#### **WHAT ARE DEL?**

Responsibility for public expenditure allocation across the UK currently belongs to central government, specifically Her Majesty's Treasury (HM Treasury).<sup>7</sup> The total budgets of devolved administrations have two public expenditure categories, (i) Departmental Expenditure Limits (DEL) set over three years and (ii) Annually Managed Expenditure<sup>8</sup> (AME) set annually, e.g. social security benefits.<sup>9</sup> This sub-section concentrates on DEL given it's relevancy to the Barnett Formula.

DEL are public expenditure levels that are fixed for three years ahead and include most programme spending.<sup>10</sup> DEL are composed of those items within the *assigned* budget of UK central government, (e.g. health, education, housing), and those within its *non-assigned* budget, (e.g. Housing Loan Charges, European Union Peace and Reconciliation Programme, EU funded gas and electricity inter-connector, Hill Livestock Compensatory Allowances, Welfare to Work).

Most expenditure within DEL concern assigned budget items that are undifferentiated because, as mentioned earlier, devolved administrations have full discretion over their spending priorities. Whereas the remainder of DEL spending are devoted to non-assigned budget items that are ring-fenced for specific spending priorities.<sup>11</sup>

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<sup>7</sup> This means that the public expenditure budgets of devolved administrations are determined within central government's framework of UK public expenditure control. Although it should be noted that once central government determines devolved administrations' public expenditure budgets, devolved administrations have freedom to make their own spending decisions within the overall budget totals on their devolved programmes. Ibid, p. 2.

<sup>8</sup> AME covers items whose provision is reviewed and set for the coming year annually in March and certain self-financed expenditure. AME expenditure cannot be recycled from one AME programme to another or recycled to increase the DEL. Within AME expenditure is classified between "Main Departmental Programmes in AME" and "other AME spending". Main Departmental programme spending covers policy-specific, ring-fenced items where provision is included within the Vote from the United Kingdom Parliament. The AME element of the budget is reviewed annually, and forecast twice a year for the three years ahead. Thus the AME element of the budget can move up or down and, hence, the total budget itself may move up or down in line with AME. "Other AME" spending includes locally financed expenditure, including expenditure financed by the Scottish Variable Rate of Income Tax; these are not ring-fenced and may be allocated as the devolved administrations consider appropriate. Id.

<sup>9</sup> Ibid, p. 3, para 1.6.

<sup>10</sup> Id. This has been in operation since 1998. DEL will be reviewed only if inflation varies substantially from forecast made at the time of a spending review (plus or minus 1.5 per cent from the cumulative projections for inflation for years two and three of a spending review period).

Id.

<sup>11</sup> Id.

## **HOW DO DEL RELATE TO THE BARNETT FORMULA?**

UK central government applies certain principles in the allocation of public expenditure throughout the UK.<sup>12</sup> (See Appendix A for an outline of these principles.)

Amongst these principles is the use of the population-based Barnett Formula. Central government uses the Formula when reviewing its spending plans: the Formula determines changes in the spending allocations to the devolved administrations' DEL, specifically their DEL assigned budget items, by applying the Formula to changes in planned spending on comparable services in departments of central government.<sup>13</sup>

**IT MUST BE NOTED THAT ASSIGNED BUDGET ITEMS OF DEL ARE SOMETIMES COMMONLY REFERRED TO AS "BLOCK" MONEY. HOWEVER, IT ALSO MUST BE NOTED THAT THE TERM "BLOCK" IS SOMETIMES USED TO DESCRIBE THE TOTAL AMOUNT OF DEL AND AME EXPENDITURE. THIS RESULTS IN SERIOUS CONFUSION. IT THEREFORE MUST BE NOTED THAT ANY REFERENCES IN THIS PAPER TO THE TERM "BLOCK" CONCERNS ONLY EXPENDITURE THAT IS DETERMINED BY THE OPERATION OF THE BARNETT FORMULA, I.E. "ASSIGNED BUDGET ITEMS OF DEL".**

Hence, the Barnett Formula arises in the context of central government reviewing its spending plans and making changes in the spending allocations to the devolved administrations' assigned budget items of DEL.

## **SECTION 1.2 - HISTORY OF THE BARNETT FORMULA**

The Barnett Formula first was introduced for Scottish public spending in the fiscal year 1979-80 (in the context of preparations for devolution in Scotland that subsequently did not occur). Its application to Northern Ireland and Wales followed two years later.

### **WHAT IS THE BARNETT FORMULA?**

The ratio originally used in the Formula was 10:5:85. The Formula's inventor Lord Barnett explains the ratio as follows:<sup>14</sup>

*...Scotland, 10 per cent, Wales, 5 per cent, and England, 85 per cent. Thus, if Government decided to increase expenditure in England by £85 million, Scotland would gain £10 million and Wales £5 million. The Formula clearly precludes Treasury attacks on the specific levels of public expenditure in Scotland and Wales, therefore, and protects their relative advantage...*

The Northern Ireland dimension of the Formula, essentially the "son-of-Barnett", allocated Northern Ireland an extra £2.75 when expenditure in Great Britain on services equivalent to those in Northern Ireland increased by £100.<sup>15</sup>

(For a detailed discussion of the Formula's current theoretical basis and practical application, refer to Section 1.3 of this paper. The present section concentrates on the Formula's history since its introduction.)

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<sup>12</sup> Ibid, pp. 4-5.

<sup>13</sup> Ibid, p. 5, para 3.1.

<sup>14</sup> Lord Barnett. "The Barnett Formula: How a temporary expedient became permanent". *New Economy*. IPPR. June 2000, pp. 69-71, 69.

<sup>15</sup> Heald, David. 1994. p. 148.

The Formula is not prescribed by statute; rather it is a policy. It is described as an example of:<sup>16</sup>

*...a non-statutory policy rule based on mutual understanding between parties within the policy network, the implementation of which is subject to both sides observing the “behavioural rules of the game”.*

The Formula is basically a means to share out changes in public expenditure plans between countries in the UK, using population as the basis. It therefore determines change to the inherited level of spending for each devolved administration, i.e. it's departmental baselines. It does not determine the overall budget levels of devolved administrations.

It does not apply to the following:<sup>17</sup>

- certain programmes within DEL;
- all AME items; and
- other expenditure outside DEL.

Hence, Barnett figures\* for 1998-99 to 2001-02 are as follows:<sup>18</sup>

	<b>1998-98</b>	<b>1999-2000</b>	<b>2000-01</b>	<b>2001-02</b>
<b>Scotland</b>	£ 13.1 bn	£13.8 bn	£14.5 bn	£15.1 bn
<b>Wales</b>	£ 6.7 bn	£ 7.0 bn	£ 7.4 bn	£ 7.8 bn
<b>Northern Ireland</b>	£ 5.7 bn	£ 5.9 bn	£ 6.2 bn	£ 6.3 bn

[\*Note that the above-stated figures include the total amount of DEL, so they include a small proportion of monies that are not determined by Barnett, and instead are centrally negotiated. However, the figures are used to highlight the amounts determined by Barnett.]

Once Barnett monies are allocated, each devolved administration has discretion to allocate them as it thinks fit in relation to local needs and priorities. However, the actual

<sup>16</sup> Twigger, Robert. “The Barnett Formula”. House of Commons Library – Economic Policy and Statistics Section. Research Paper 98/8. 12 January 1998, p. 15, referring to Thain, C. and M. Wright. *The Treasury and Whitehall: The Planning and Control of Public Expenditure*. Clarendon Press. London: 1995, see chapter 14. Note that HM Treasury accepted that description as “broadly right”. House of Commons Select Treasury Committee. *The Barnett Formula*. (Second Report - 22 December 1997). Session 1997-98, p.1.

<sup>17</sup> HM Treasury. 31 March 1999, p. 8, para 4.1.

<sup>18</sup> Day, Karen. 8-14 October 1999, p. 24.



scope of this discretion has been noted to be limited because in practice most public spending is incremental and must take account of other factors, e.g. pay settlements.<sup>19</sup>

### **UNDERLYING REASONS OF THE FORMULA**

Underlying reasons for establishing the Formula have been explained as follows:<sup>20</sup>

*It was set up for a variety of reasons. ... the need to recognise that the spending levels between the various parts of the UK-population sparsity in Scotland, transport needs, needs because of relative ill health, rural needs for education and so on and industrial needs....*

The Formula's inventor, Lord Joel Barnett, further explains that:<sup>21</sup>

*Fundamentally, it was decided on a population basis. I would not, however, have been able to obtain Cabinet agreement without first satisfying English departmental cabinet ministers that there were reasonable grounds for allocation of a greater level of public expenditure to Scotland and Wales than population figures alone justified. In substance, it was the different levels of income per head in England, Scotland and Wales that convinced ministers. ...After persuading Cabinet to agree a total level of public expenditure for Great Britain, and within that to agree the Barnett Formula, I then had the very tough job of persuading departmental ministers to accept the amounts I had allocated to them. One of the major arguments I used in difficult, bi-lateral discussions was that I could not let them have any more money, Cabinet having agreed the total and approved the distributive Formula.*

The Barnett Formula therefore largely replaced the need for direct negotiation about public expenditure allocation between UK Treasury Ministers, Secretaries of States and Ministers of devolved administrations, which were very time consuming.<sup>22</sup>

However, it does not appear that the Formula was intended to be a permanent replacement. Apparently the Formula was intended only as a temporary measure.<sup>23</sup> In this regard, Lord Barnett maintains that:<sup>24</sup>

*The Formula was intended to be approximately population-based and was intended as a stop-gap until a needs-based system came into operation. In fact, no such change to take account of needs has been made.*

### **SINCE BARNETT'S INTRODUCTION**

Since its introduction over 20 years ago, the Formula has been in continuous use in public expenditure surveys with only minor alterations made to it. Such changes

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<sup>19</sup>“The Barnett Formula”. The Scottish Parliament – The Information Centre. RN 00/31. 4 May 2000, p. 4.

<sup>20</sup> See the evidence of Lord Barnett in House of Commons Select Treasury Committee. *The Barnett Formula*. (Second Report - 22 December 1997). Session 1997-98.

<sup>21</sup> Lord Barnett. June 2000, p. 70.

<sup>22</sup> See the evidence of Her Majesty's Treasury in House of Commons Select Treasury Committee. 22 December 1997, p. 12.

<sup>23</sup> Twigger, Robert. “The Barnett Formula”. House of Commons Library – Economic Policy and Statistics Section. Research Paper 98/8. 12 January 1998, p. 7, relying on House of Commons Select Treasury Committee. 22 December 1997.

<sup>24</sup> Lord Barnett. June 2000, p. 70.

included the re-calibration of the Formula in 1992 when population ratios underpinning it were updated, resulting in Scotland receiving a greater proportion than Northern Ireland and Wales.<sup>25</sup>

Moreover, in 1998 central government committed itself to revising the population ratio annually. It indicated in the White Paper on Scotland's Parliament that:<sup>26</sup>

*... that the Formula would be updated regularly, to reflect the actual population ratio. In response to pressure from English MPs, Alistair Darling, Chief Secretary to the Treasury at the time, gave a commitment that it would be revised annually.*

Since the Formula's introduction, however, it appears that it has been by-passed in significant ways, particularly in the 1980s, so that incremental expenditure has not always been allocated in accordance with the Formula.<sup>27</sup> Identified examples of "formula by-pass" include the following:<sup>28</sup>

- additional expenditure allocations which arise during the financial year, (for example, the National Health Service pay awards), are fixed on the basis of costed amounts, and not on the basis of the Barnett Formula;
- certain expenditure functions within the Scottish, Welsh and Northern Ireland blocks may have no English counterparts, thus necessitating some other basis for determining expenditure increases; and,
- certain expenditure changes, perhaps initiated for macro-economic reflation or deflation, are allocated on bases other than those of the Barnett Formula

It further should be noted that on at least one occasion since the Formula was introduced, HM Treasury implemented an 'across-the-board' percentage reduction in departmental baselines before applying the Formula.<sup>29</sup> This enabled ministers to state that the Formula was implemented, but consequently eroded the protection afforded by the Formula to inherited expenditure.<sup>30</sup>

Other factors that seem significant in the history of the Barnett Formula are disconnected changes in the public expenditure planning system: these include the

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<sup>25</sup> For Scotland, instead 11.76 per cent of changes in equivalent English expenditure, the block received an increment of 10.66 per cent, which is equivalent to 10.59 per cent. For Wales, the new figure was 6.02 per cent, revised from 5.88 per cent. For Northern Ireland, the new figure was 2.87 per cent. Heald, David. "Territorial Public Expenditure in the United Kingdom". *Public Administration*. Summer 1994, pp. 147-175, p. 148.

<sup>26</sup> Lord Barnett. June 2000, p. 69.

<sup>27</sup> Heald, David. "Fiscal Opportunities". *Hard Choices – Policy autonomy and priority-setting in public expenditure*. Democratic Dialogue. Belfast: Autumn 2000, p. 4. See <http://cain.ulst.ac.uk/dd/report10d.htm>.

<sup>28</sup> Heald, David. Summer 1994, p. 169. Notwithstanding, it is difficult to know the quantitative importance of such by-passes in the absence of detailed information about them. *Ibid*, p. 170. However, it appears that most identified cases seem to have benefited, rather disadvantaged, Scotland, Wales and Northern Ireland. Heald, David. Autumn 2000, p.4.

<sup>29</sup> *Ibid*, p.5.

<sup>30</sup> *Id.* Heald explains that "[m]oney 'saved' by applying a constant percentage cut to the territorial blocks and to comparable expenditure can be then passed through the Barnett Formula, generating formula consequences' supplementary to those generated year-on-year increases in comparable expenditure. Naturally, the arithmetical effect is disadvantageous to the territories because the constant percentage cut generates more savings' from their blocks than they subsequently receive back in these artificial' formula consequences".

introduction of cash planning in 1982 and the new planning total in 1990, both of which affected the operation of the Formula.<sup>31</sup> It has been argued that a substantial part of the complexity of the effects of the Barnett Formula stems from the switch since 1982-83 onwards from public expenditure planning in volume terms to cash planning.<sup>32</sup> This switch apparently caused a great acceleration in the predicted erosion of the initial expenditure advantage under the Formula for Scotland, Wales and England.<sup>33</sup>

Another development that impacted Barnett was the creation of the devolved governments in 1998 - namely the Scottish Parliament, the National Assembly of Wales and the Northern Ireland Assembly, and the devolution of power. The Barnett Formula subsequently became a mechanism to allocate money between the levels of government, and not within a government.<sup>34</sup> Devolved administrations may place increasing demands on central government for detailed information about the Formula's application, arguably forcing central government to be more transparent and accountable.<sup>35</sup>

A final factor that appears significant in the history of the Barnett Formula is the recent fundamental change in the way the UK government, (central and devolved), accounts for and controls public expenditure arises from Resource Accounting and Budgeting (RAB). Resource accounts replaced Appropriation Accounts with effect from the financial year 2001-02, moving accounting to an accruals basis.<sup>36</sup>

Although it should be noted that RAB does not change the principles applied in the allocation of public expenditure (as set out by HM Treasury's Funding Statement in March 1999). This means that the Barnett Formula continues to apply. But HM Treasury states that resource accounting inevitably will require changes in the application of the Barnett Formula.<sup>37</sup> In March 1999, HM Treasury stated that it would consult the devolved administrations about these changes. It is unclear whether such consultation took place.

In sum, this section highlights that while the Barnett Formula is considered a robust mechanism for public expenditure allocation, its long history appears to have been far from straightforward.

### **SECTION 1.3 - BARNETT'S CURRENT THEORETICAL AND PRACTICAL APPLICATION**

Section 1.3 provides a synopsis of HM Treasury's explanation of Barnett's current theoretical basis as well as an illustration of the Formula's practical application.<sup>38</sup>

#### **THEORETICAL BASIS OF BARNETT**

At the outset, it is worth repeating that the Barnett Formula does not determine the total allocation for each devolved administration. Rather, it determines changes to the

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<sup>31</sup> Id.

<sup>32</sup> Id.

<sup>33</sup> Id.

<sup>34</sup> Id.

<sup>35</sup> Id.

<sup>36</sup> The aim of this change is to focus more on resources consumed rather than cash spent; to treat capital and current expenditure in a way that distinguishes their economic significance and to focus on achievement of outputs, aims and objectives. HM Treasury. 31 March 1999, pp. 4-5, paras 1.7 –1.8.

<sup>37</sup> Id.

<sup>38</sup> Ibid, pp. 6-8, paras 3.3-3.16.

spending allocations within the assigned budgets of the devolved administrations, effectively sharing out changes in public spending. Under the Formula, Northern Ireland, Scotland and Wales receive a population-based proportion of changes in planned spending on comparable UK central government services in England, England and Wales or Great Britain as appropriate.<sup>39</sup>

### *The Formula*

During the course of a public expenditure round, DELs for Scotland, Wales and Northern Ireland are largely determined by the Barnett Formula. The Formula is based on three factors:<sup>40</sup>

1. the *quantity of the change* in planned spending in departments of the United Kingdom Government;
2. the extent to which the relevant United Kingdom department programme is *comparable* with the services carried out by each devolved administration; (see Appendix B for a detailed explanation of the Comparability Factor in the Barnett Formula); and
3. each country's *population* as a proportion of England, England and Wales or Great Britain as appropriate; (see Appendix C for a detailed explanation of the Population Proportion in the Barnett Formula).

These three factors combine to determine the net change to the spending allocations for each devolved administration in the following manner:<sup>41</sup>

Change to the department of the UK Government's Programme	X	Comparability percentage	X	Appropriate population proportion
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Using the various components of the Barnett Formula as outlined above, a calculation is made for each UK departmental programme in DEL. The results of each calculation consequently form the aggregate net change to the assigned budget element of DEL for each devolved administrations. It then is for each devolved administration to allocate spending within their assigned budgets according to their own priorities.<sup>42</sup>

### **PRACTICAL EXAMPLE OF BARNETT**

This sub-section outlines the illustration provided in HM Treasury's statement in March 1999 to highlight the practical application of the Barnett Formula.<sup>43</sup>

If for example:

- (i) the Government decides to increase or decrease the DEL of a UK department's DEL by £100; and

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<sup>39</sup> Ibid, p. 6, para 3.3.

<sup>40</sup> Ibid, p. 6, para 3.4.

<sup>41</sup> Ibid, p. 6, para 3.5.

<sup>42</sup> Ibid, p. 6, para 3.6.

<sup>43</sup> Ibid, Annex B.

- (ii) the comparability for each devolved administration is 75 per cent for the programme (perhaps because the department in question already carries out some expenditure at an all UK level; and
- (iii) the population proportions are 10.34 per cent for Scotland, 5.93 per cent for Wales and 3.41 per cent for Northern Ireland of England's population or 2.93 per cent of Great Britain's population for Northern Ireland;

then the following changes are then added to or subtracted from each countries' overall baseline:

**Scotland** -  $100 \times 0.75 \times 0.1034 = \text{£ } 7.76 \text{ million}$

**Wales** -  $100 \times 0.75 \times 0.0593 = \text{£ } 4.45 \text{ million}$

**Northern Ireland** -

*Pre-1999 method :*

English change :

$100 \times 0.75 \times 0.0292 = \text{£ } 2.19 \text{ million}$

Aggregate\* Scotland and Wales change:

$(7.84 + 4.46) \times 0.0292 = \text{£ } 0.36 \text{ million}$

Northern Ireland Total\*:

$\text{£ } 2.55 \text{ million}$

7 % VAT abatement\*

$\text{£ } 2.37 \text{ million}$

*Post-1998 method :*

English Change:

$100 \times 0.75 \times 0.0341 = \text{£ } 2.55 \text{ million}$

7 % VAT abatement (which is 2.5 %)\* :

$\text{£ } 2.37 \text{ million}$

HM Treasury explains that two methods are shown above to calculate Northern Ireland's provision under the Barnett Formula: the first uses the share of Great Britain's population for England, Scotland and Wales changes – this was applied up to and including the 1998 Comprehensive Spending Review; and the second uses the share of England's population, consistent with the method for Scotland and Wales, and this will be applied in future reviews.<sup>44</sup>

HM Treasury further explains that the devolved administrations do not have to adjust their programme spending in line with the UK departments, they are free to adjust spending on any of their functions: (the same calculations will be carried out for all comparable UK spending), and the sum of these changes will give the overall change in each devolved administration's baseline.<sup>45</sup>

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<sup>44</sup> Ibid, p. 8.

<sup>45</sup> Id.

**PART 2:**

**SECTION 2.1 - PRACTICAL IMPACT OF BARNETT THROUGHOUT THE UK**

Practical implications of the Barnett Formula include the following:

- **Control of public expenditure changes** - The Barnett Formula aims to control, not public spending *per se*, but changes in public spending in the UK.<sup>46</sup>
- **No on-going negotiations needed** – There has been no need for Northern Ireland, Scotland and England to engage in on-going lengthy negotiations about equal treatment on each occasion that a relevant programme in England/GB receives increased funding. Pre-Barnett, such negotiation was a very time consuming process.
- **Discretion to allocate** - The devolved administrations, (previously the Secretaries of State), have retained the freedom to allocate the monies received under Barnett as they think fit given local needs and priorities. However, it has been noted that the actual scope of this discretion is limited because in practice most public spending is incremental and must take account of other factors, e.g. pay settlements.<sup>47</sup> Moreover, devolved administrations can use this discretion to re-allocate Barnett monies.
- **Insufficiency and incomparability of documentation** – There apparently has been insufficient information in either the *Financial Statement and Budget Report*, (commonly referred to as the “Red Book”), or the Departmental Expenditure Reports to show how the Formula actually has operated,<sup>48</sup> making it difficult to make comparisons between the respective block expenditure in England, Northern Ireland, Scotland and Wales. Moreover, it has been pointed out that there has been serious terminological confusion, apparently what has been described in the published documentation as the “Northern Ireland block” is not comparable to the Scottish and Welsh blocks.<sup>49</sup>
- **Lack of convergence** - As mentioned in the previous section, strict application of the Barnett Formula should in theory cause spending *per capita* between the different parts of the UK to converge over time.<sup>50</sup> However, research shows that convergence has not occurred in practice.<sup>51</sup> It has been argued that this deviation between theory and practice arises from two factors: (i) the “constant ratio effect” and (ii) the “formula by-pass effect”.<sup>52</sup>

The “constant ratio effect” is a concept that has been used to refer to the fact that there was only one revision in the population share proportions of the Formula during the first 20 years of its use. It has been pointed out that at the same time,

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<sup>46</sup> McLean, Iain. “Getting and spending: Can (or should) the Barnett Formula survive?”. *New Economy*. IPPR. 2000. pp. 76-80, p. 77.

<sup>47</sup> “The Barnett Formula”. The Scottish Parliament – The Information Centre. RN 00/31. 4 May 2000, p. 4.

<sup>48</sup> Twigger, Robert. 12 January 1998, p. 10.

<sup>49</sup> Heald. Autumn 2000, p. 9.

<sup>50</sup> Heald. Summer 1994, p. 164.

<sup>51</sup> Bell, David. “The Barnett Formula”. Department of Economics, University of Stirling. January 2001 and Heald, David. Summer 1994, p. 164.

<sup>52</sup> Heald, David. Summer 1994, p. 172 and Heald, David. Autumn 2000.

the relative size of the population in Scotland actually fell when compared to England. It therefore has been argued that these factors collectively resulted in the ratio over-estimating the additional block money that should have gone to Scotland, which consequently has off-set the convergence effect to a certain extent.<sup>53</sup>

The “formula by-pass effect” is a concept that has been used to refer to the fact that not all additions to block expenditure are allocated through Barnett. Apparently non-Barnett additions can occur when blocks are adjusted to reflect the transfer of responsibilities from Whitehall to the devolved administrations. Moreover, the UK Government apparently may decide to make uniform adjustments to the level of the block to pay for certain spending commitments.<sup>54</sup>

- **Higher spending per head** - The actual operation of the Barnett Formula over the last 20 years appears to have protected, to a large extent, the situation where spending per head in Northern Ireland, Scotland and Wales is above the UK national average.<sup>55</sup> (See Appendix D for expenditure statistics, but note that there are difficulties in making comparisons between the expenditure levels as the statistics include both DEL and AME, making them broader than Barnett.) However, it has been argued that Barnett is not the cause of relatively high per capita spending levels in Northern Ireland, Scotland and Wales.<sup>56</sup> Rather, it seems that the “generosity” of the initial settlements made at the time of the Formula’s introduction are responsible.<sup>57</sup>
- **Initial ratio favourable to Scotland** - It has been argued that the initial ratio under the Formula was favourable to Scotland, as the Scottish population share was rounded up from 9.57 to 10, and unfavourable to Wales, as the Welsh population share was rounded down from 5.12 to 5.<sup>58</sup> A separate point has been suggested in this regard in relation to the Northern Ireland formula proportion; that it was expressed to two decimal points in relation to it’s base of GB, resulting in an adverse rounding as the population percentage at mid-year 1976 was 2.79.<sup>59</sup>
- **Differential expenditure** - Northern Ireland and Scotland may have fared better under Barnett due to expenditure relatives in Northern Ireland and Scotland having been kept at a higher level than their needs relatives: whereas Wales may have done less well comparatively.<sup>60</sup>
- **Re-calibration** - It has been observed that the issue of relative population change under the Formula for Scotland and Northern Ireland is of particularly marked contrast. The population ratio of Scotland to England has changed from 11.24 per cent in 1976 to 10.45 per cent in 1996. In contrast, Northern Ireland’s population ratio to GB has risen from 2.79 to 2.91 per cent. Therefore, the convergence effect of application of the Barnett Formula on *per capita* expenditure relatives has been attenuated in Scotland, but accentuated in Northern Ireland.<sup>61</sup> Moreover, the re-calibration resulted in population proportion changes whereby Wales received a

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<sup>53</sup> National Assembly for Wales - Library. 13 January 2000, pp. 3-4.

<sup>54</sup> Ibid, p. 4.

<sup>55</sup> Bell, David. January 2001, p. 13.

<sup>56</sup> Id.

<sup>57</sup> Id.

<sup>58</sup> National Assembly for Wales - Library. 13 January 2000, pp. 1-2.

<sup>59</sup> Heald, David. Autumn 2000, p. 3.

<sup>60</sup> Ibid, p. 2.

<sup>61</sup> Ibid, p. 4.

slightly higher share of the ratio, and Scotland received a substantially lower share. The new ratio being roughly 5.1:9:85.<sup>62</sup>

- **“Barnett Squeeze”** – It appears that both the 1992 re-calibration which moved the GB component of the formula to two decimal places and the 1997 modification that was to ensure annual population updating, have eliminated rounding as an inhibitor of long-run convergence.<sup>63</sup> If the Barnett Formula is re-calibrated on such a basis, it has been argued that the percentage increases in comparable expenditure will be smaller. This has been labelled the “Barnett Squeeze”.<sup>64</sup> For example, it has been argued that Scottish public spending will increase more slowly in percentage terms relative to England and Wales over a period of time,<sup>65</sup> and that Northern Ireland will receive a smaller percentage share of overall UK public expenditure.<sup>66</sup>
- **Post-devolution** – It has been noted that local authorities’ expenditure constitute a large claim on Scottish and Welsh blocks; whereas their limited role in Northern Ireland’s means that a much larger proportion of it’s block will be under the direct control of the Northern Ireland Assembly.<sup>67</sup> Moreover, there is no comparable under the Barnett Formula for water, sewerage, public transport, and some roads in Northern Ireland as they are outside the public expenditure regime since devolution: Barnett therefore must help to pay for them.
- **Unforeseen and disconnected government decisions** - The effect of particular territorial financial mechanisms crucially can depend upon seemingly unforeseen and disconnected government decisions, e.g. the impact of the switch to cash planning upon the operation of the Barnett Formula, as well as any future potential impact of RAB on it.<sup>68</sup>

On balance, the practical implications of Barnett seem to include both positive and negative effects for Northern Ireland, Scotland and Wales, as well as for England.

## **SECTION 2.2 - IDENTIFIED ADVANTAGES AND DISADVANTAGES OF BARNETT**

This section briefly outlines apparent advantages and disadvantages to the Barnett Formula for Northern Ireland, as well for England, Scotland and Wales.

### **ADVANTAGES**

Identified advantages include the following:

- The operation of the Barnett Formula appears to have protected, to a large extent, the situation where spending per head was above the UK national average in Northern Ireland, Scotland and Wales – all of which have historically been areas of high need.<sup>69</sup>

<sup>62</sup> National Assembly for Wales - Library. 13 January 2000, pp. 1-2.

<sup>63</sup> Heald, David. Autumn 2000, p.4.

<sup>64</sup> Cuthbert. *The Implications of the Barnett Formula*. Scottish Nationalist Party. Edinburgh. 1998.

<sup>65</sup> The Scottish Parliament – The Information Centre. 4 May 2000, p. 5.

<sup>66</sup> Heald, David. Summer 1994.

<sup>67</sup> Heald, David. Autumn 2000, p. 2.

<sup>68</sup> Heald, David. Summer 1994, p. 171.

<sup>69</sup> Bell, David. January 2001, p. 13.



- The devolved administrations, (previously the Secretaries of State), have retained the freedom to allocate the monies received under Barnett as they think fit given local needs and priorities. (However, it has been noted that the actual scope of this discretion is limited because in practice most public spending is incremental.<sup>70</sup>)
- The Barnett Formula arguably has played a part in minimising conflict between the devolved governments and the central government.<sup>71</sup> It's continued use has eliminated the need for on-going lengthy negotiations about equal treatment on each occasion that a relevant programme in England/GB received increased funding. (Pre-Barnett, such negotiation was a very time consuming process.)
- The Barnett Formula provides a politically rational basis to allocate public expenditure.<sup>72</sup> The Formula is objective.<sup>73</sup>
- In the absence of precision in needs assessments, the Barnett Formula is the best available means for distributing public expenditure throughout the UK, particularly given the tightening up of its application since 1992 and the underlying assumption that Northern Ireland, Scotland and Wales have higher needs than the UK average. Moreover, there is no guarantee that the devolved governments would receive more money through any new needs assessment. Finally, it is questionable as to whether it is worth the bother of undoing Barnett, as the actual amount of money at issue is marginal.<sup>74</sup>

### **DISADVANTAGES**

Identified disadvantages include the following:

- The population-based Formula is too simplistic: it is not based on actual need of Northern Ireland, Scotland and Wales. It appears that this may become a problem, particularly when convergence in the level of *per capita* public expenditure occurs in the various parts of the United Kingdom. As convergence occurs, issues may arise about differential expenditure needs throughout the United Kingdom, e.g. the number of persons within an area that requires medical treatment, the number of children in school, the number of elderly people requiring care, the number of people living in rural areas, coupled with the differential costs of service provision in rural areas.<sup>75</sup> Such potential high public service demands could cause particular concern, especially if combined with low disposable incomes as is the case in the devolved countries, particularly in Northern Ireland, which is the lowest.<sup>76</sup> Per head disposable income levels across the UK for 1999 were: England £101.60; Wales £90.40; Scotland £ 94.80 and Northern Ireland £ 85.90.<sup>77</sup>
- Post-devolution, the pre-existing financial arrangements for public expenditure were not changed; instead they were carried over, including the Barnett Formula. This means that the Barnett Formula, which originally was introduced to allocate funds

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<sup>70</sup> The Scottish Parliament – The Information Centre. 4 May 2000, p. 4.

<sup>71</sup> McConnell, Jack. "Funding devolution: Why Barnett remains better than the alternatives". *New Economy*. IPPR. 2000. pp. 65-68, p. 68.

<sup>72</sup> Midwinter, Arthur. June 2000, p. 73.

<sup>73</sup> Midwinter, Arthur. April-June 1999, pp. 53-54.

<sup>74</sup> Midwinter, Arthur. June 2000, p. 74.

<sup>75</sup> Heald, David. Autumn 2000.

<sup>76</sup> Regional Household Sector Income and Consumption Expenditure. 26 July 2001. See

[www.statistics.gov.uk](http://www.statistics.gov.uk) .

<sup>77</sup> Id.

within government, now is being used to distribute funds between different levels of government, i.e. the central government and the devolved governments in Northern Ireland, Scotland and Wales.<sup>78</sup> Criticisms have been raised about this arrangement, specifically in relation to its suitability. Does it afford too little fiscal autonomy for the devolved governments, preventing them from having proper political accountability?<sup>79</sup> Indeed, one of the prime objectives of devolution is to enable regional preferences to be reflected in policy decisions. Hence, it has been suggested that devolved government may seek to blame central government when it fails to provide any services to the standard desired by its electorate. A devolved government's time therefore may be spent complaining about HM Treasury's parsimony. This especially may be the case in Northern Ireland where, as noted earlier, application of the Barnett Formula is anticipated to lead to a relatively smaller budget from which to fund public services.<sup>80</sup> It potentially raises issues about Northern Ireland's regional rates, e.g. they may need to be increased to clear current shortfalls.

- HM Treasury can implement across the board percentage reduction in departmental baselines before applying the Formula, which erodes the protection afforded by it to inherited expenditure, and consequently allows ministers to state that the Formula has been implemented. (It apparently once did.<sup>81</sup>)
- At present, the Formula is not prescribed by legislation. There consequently is no formal review procedure for the Formula or its operation; it therefore can be altered or possibly misapplied by HM Treasury, which apparently has full discretion to do so, (e.g. 1992 re-calibration, formula by-pass).
- The incomplete application of the Formula during the 1980s and 1990s are causing slower convergence. But now stricter application of Barnett should start moving towards equal *per capita* public spending throughout the UK. It is maintained that such an outcome would be clearly inequitable if one believes that public spending should reflect differences in relative need.<sup>82</sup> Moreover, simulations have shown that over the next 12 years such transition may result in Scotland's relative advantage under Barnett disappearing, Wales also and Northern Ireland having the most rapid rate of convergence.<sup>83</sup>
- It has been further argued that "...convergence to equal levels of *per capita* spending throughout the UK is not the result of a real decline in provision of public services in Scotland, Wales and Northern Ireland. Real expenditure is rising in all cases, but less rapidly in Scotland, Wales and Northern Ireland than in England."<sup>84</sup> It is suggested that this may create political difficulties for devolved governments as England may be perceived as delivering public services that are improving at a faster rate, (e.g. health).<sup>85</sup>
- The Formula generally has not been used in an open and transparent manner, e.g. formula by-pass or insufficiency and incomparability of documentation.<sup>86</sup>

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<sup>78</sup> Id.

<sup>79</sup> Id.

<sup>80</sup> Bell, David. January 2001.

<sup>81</sup> Heald, David. Autumn 2000, p. 5.

<sup>82</sup> Bell, David. January 2001, p. 13.

<sup>83</sup> Ibid, p.9.

<sup>84</sup> Ibid, p. 10.

<sup>85</sup> Id.

<sup>86</sup> Heald, David. Summer 1994.

- Given that the devolved administrations have discretion to allocate the monies calculated under Barnett, they could re-allocate such monies in such a way that some Northern Ireland departments would get less and others get more than what originally was expected, given the comparability factor.
- Since devolution the link between the regional rate and water provision has been broken in Northern Ireland. Consequences flow from this in relation to Barnett as such monies will be used to pay for water and sewerage provision. This is compounded by the fact that the regional rate in Northern Ireland is considerably lower than the rest of the UK. Moreover, there are no water charges as there are in the rest of the UK. This means there are more demands on Barnett monies, at a time when the Formula is being strictly applied, and consequently moving towards convergence. Again, it potentially raises issues about the following: (i) the regional rates in Northern Ireland; and (ii) the inexistence of water charges in Northern Ireland.

A number of identified advantages and disadvantages of the Barnett Formula are outlined above. It may be appropriate for the Committee to seek specialised assistance from both outside and inside the Department of Finance and Personnel to authoritatively expand on the points raised throughout this section.

### **PART 3:**

#### **SECTION 3.1 – POTENTIAL REVIEW OF BARNETT AND PROPOSED ALTERNATIVES TO IT**

The Barnett Formula appears to have raised a certain amount of controversy over recent years. There have been calls for the review and replacement of Barnett as well as calls for its retention.

#### **REVIEW AND POTENTIAL REPLACEMENT OF BARNETT**

Calls of a review and potential replacement of Barnett have included the following:

- The Formula's inventor, Lord Barnett, seeks the Formula's abolition.<sup>87</sup> He explains that the Formula was introduced only as a short-term measure in the late 1970's, but gives no consideration to needs or to where public resources should be allocated.<sup>88</sup> He states that figures comparing GDP per head and public expenditure across the regions are revealing in that within each area and region there are large differences: for example, under the Formula GDP per head was 13 per cent below Scotland in 1997, but government expenditure was not higher – it was 19 per cent lower.<sup>89</sup> Lord Barnett consequently argues that a new way should be found, one based on a more objective measure of relative need.<sup>90</sup> Thus he recommends major review of the Formula, arguing that without one, where and what action is needed will remain unknown.<sup>91</sup>

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<sup>87</sup> "A Formula for Confusion". *The Herald*. 23 June 2000.

<sup>88</sup> Lord Barnett. June 2000, p. 71.

<sup>89</sup> *Id.*

<sup>90</sup> *Id.*

<sup>91</sup> *Id.*

- In its 1997-98 report on the Formula, the House of Commons Select Treasury Committee called for the Formula's review, and argued that a new needs assessment study would help to show if Barnett remained the appropriate method.<sup>92</sup>
- It has been argued that a review is potentially problematic given the lack of comparable data for devolved spending, as well as other differences in services.<sup>93</sup>
- The Scottish National Party (SNP) advocated a system of fiscal separatism that will enable the Scottish Parliaments to have greater fiscal autonomy by raising most of its own spending through its own taxes. This proposed method of the redistribution of public funds is referred to as "the repatriation of capital".<sup>94</sup> Others argued that this will make regional governments accountable to their electorate.<sup>95</sup>

### **RETENTION OF BARNETT**

Calls for the retention of Barnett have included the following:

- Some argue that review is not necessary because the Barnett Formula is politically rational, asserting that it recognises the inherited costs from the UK Government by determining most of the block grant on the base budget. Moreover, the Formula allocates the increments simply by population, eliminating the need for detailed negotiations.<sup>96</sup>
- Some state that the Formula recognises the realistic scope for changes at the margins and that the small sums that a needs assessment exercise might redistribute would not be worth the political turmoil they would create.<sup>97</sup>
- It has been argued that there is no agreed needs formula, and the statutory context of service delivery differs.<sup>98</sup>
- It has been questioned as to whether anyone really knows exactly how a needs assessment should be conducted. The following questions arise:
  - (i) how would a needs assessment take account for regional variations in need or economic prosperity within the regions of the UK, variations that are every bit as dramatic as those found at the more macro level?
  - (ii) who would have the objective credibility to carry out such an assessment?
  - (iii) would there be political consensus for the assessment's findings?<sup>99</sup>
- The Audit Committee in England has stated in its report in 1993 that needs assessment can never be 'perfect' or 'fair'.<sup>100</sup> Whilst others have argued that any needs assessment formula inevitably will be overtaken by the "primacy of politics".<sup>101</sup>

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<sup>92</sup> House of Commons Select Treasury Committee. 22 December 1997, p. 341.

<sup>93</sup> Midwinter, Arthur. 2000, p. 73.

<sup>94</sup> "Taxing Times". *The Guardian*. 9 June 1999.

<sup>95</sup> Bloomfield, K & Carter, C. "People and Government: Questions for Northern Ireland". as cited in "Hard Choices: Policy Autonomy and priority setting in public expenditure", pp. 52-53.

<sup>96</sup> Midwinter, Arthur. 2000, p.73

<sup>97</sup> *Ibid*, pp. 73-4.

<sup>98</sup> *Ibid*, p. 73.

<sup>99</sup> *Id*.

<sup>100</sup> The Scottish Parliament – The Information Centre. 4 May 2000, p. 8

<sup>101</sup> Midwinter, Arthur. "The Politics of Needs Assessment: The Treasury Select Committee and the Barnett Formula". *Public Money and Management*. April-June 1999, pp. 51-54, p. 53.

In sum, it appears that there is growing consensus for a review of Barnett. Moreover, there seems to be two clear positions taken on Barnett and its future, i.e. (i) replace Barnett and (ii) retain it. It further appears that replacement of the Formula with a needs assessment-based mechanism may be fraught with difficulties, particularly in light of past discussions about developing such a mechanism. (See Appendix E for information concerning needs assessments generally and in the UK.)

### **SECTION 3.2 - CURRENT POSITIONS ON THE BARNETT FORMULA THROUGHOUT THE UK GOVERNMENTS – POTENTIAL BARNETT REFORM?**

This section provides a brief outline of the current positions on the Barnett Formula in government in Northern Ireland, Wales, Scotland and England:

#### **Northern Ireland**

- No official position has been taken to date, but there appears for the last two years to be some support for the replacement of Barnett.<sup>102</sup> The First Minister David Trimble stated in March 2001 that: “Our share of new resources has been calculated using the Barnett Formula based on population shares which is inadequate. We will continue to press the Chancellor to agree a new and fairer way of funding [Northern Ireland’s] actual needs”.<sup>103</sup>
- Mark Durkan, the Minister for Finance and Personnel, stated in May 2001 that: There is increasing concern in Northern Ireland that Barnett is working unfairly... We clearly received the least favourable outcome from last year’s Spending Review, despite the very serious infrastructure deficit we face and the fact that demands on health are rising just as quickly here as elsewhere.” The Northern Ireland Executive believes the general standard of public services should be kept broadly in line throughout the UK. However, he believes Barnett does not give Northern Ireland the extra money it would need to match the public services that can be afforded in England. “We need a system that makes proper allowance for the needs of the regions.” He cites examples of Northern Ireland’s needs, including deficiencies in the basic infrastructure of roads, water and sewerage.<sup>104</sup>
- Approximately three months ago, the Northern Ireland Department of Finance and Personnel started to undertake work to review Barnett and to assess overall need in Northern Ireland. This work is in its preliminary stages.<sup>105</sup>

#### **Wales**

- The Welsh Executive does not appear to reject a review of Barnett out of hand. A spokesperson stated in May 2001: “Any review would have to take account the full needs of Wales”.<sup>106</sup> Perhaps the Welsh Executive is against a review that leads to less grant, but in favour of one that gives it more?
- There has been particular concern in Wales that the Barnett Formula will not reflect the special circumstances associated with the designation of West Wales and the

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<sup>102</sup> Gosling, Paul. “Nobody loves Barnett – except the Scots”. *Public Finance*. 18-24 May 2001, p. 23.

<sup>103</sup> OFMDFM News Release. 7 March 2001.

<sup>104</sup> Gosling, Paul. 18-24 May 2001, p. 23.

<sup>105</sup> An official from the Northern Ireland Department of Finance and Personnel informed the author of this paper about such work.

<sup>106</sup> Id.

Valleys as an Objective 1 area under the European Union's structural funds.<sup>107</sup> Structural Funds monies will be largely channelled through the National Assembly of Wales (NAW), and therefore will score against Wales' DEL.<sup>108</sup> In addition, the NAW or its grant-funded bodies will provide some of the 'matching' funds required for structural fund projects, i.e. the proportion of the project cost not met by the EU grant.<sup>109</sup> HM Treasury agreed to consider the implications of obtaining Objective 1 status as part of the 2000 Spending Review.<sup>110</sup>

- The Welsh Liberal Democrat spokesperson Peter Black stated in aid any review of the Formula could give Wales the opportunity to press for extra funding.<sup>111</sup>
- In April 2001, the Welsh Conservatives stated that discarding the Barnett Formula would mean Wales would lose out.<sup>112</sup>

### Scotland

- In approximately October 1999, the then First Minister Donald Dewar stated: "...[h]e fought the 'Yes' campaign for devolution on the basis of the [F]ormula and sees no reason to review it."<sup>113</sup>
- The Scottish Liberal Democratic Leader Jim Wallace defended Barnett in June 2000, but warned that the Scottish Parliament must be vigilant in watching it's operation.<sup>114</sup>
- The Scottish Nationalist Party claimed in May 2001 that the Formula is now gradually reducing Scotland's share of public spending relative to England. It cites the higher spending growth in percentage terms in England as a result of the 1998 Comprehensive Spending Review.<sup>115</sup>

### England

- The Deputy Prime Minister John Prescott stated in April 2001 that there are no plans to change Barnett, which will be in place until at least 2004.<sup>116</sup> But he noted that it was time to consider new financial structures.<sup>117</sup>
- In July 2001, the Chief Secretary to the Treasury, Andrew Smith, stated: "...the Government's spending plans have been set down for the years 2003-04 including ... the Barnett Formula..."<sup>118</sup>

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<sup>107</sup> Twigger, Robert. "Background to the 2000 Spending Review". Research Paper 00/59. Economic Policy and Statistics Section – House of Commons Library. 8 June 2000, p. 21.

<sup>108</sup> Id.

<sup>109</sup> Id.

<sup>110</sup> Id.

<sup>111</sup> BBC News. 24 April 2001.

<sup>112</sup> Id.

<sup>113</sup> Day, Karen. "Barnett Formula – Squeeze falls on Barnett". *Public Finance*. 8-14 October 1999, p. 22.

<sup>114</sup> BBC News. 16 April 1999.

<sup>115</sup> *The Herald*. 19 June 2000.

<sup>116</sup> Gosling, Paul. 18-24 May 2001, p. 23.

<sup>117</sup> *The Guardian*. 24 April 2001 and *The Northern Echo*, 6 July 2001.

<sup>118</sup> The House of Commons Debates, 19 July 2001. See <http://www.parliament.the-stationary-office.co.uk/pa/cm200102/cmhans.../10719-04.ht>.

- In 2001, there is mounting criticism from regional lobby groups, backbench Members of Parliament and senior English ministers that the Formula discriminates against the poorest parts of England, where unemployment is high and manufacturing is steadily declining.<sup>119</sup>
- Liberal Democrats for Newcastle Central want the Formula scrapped and replaced by a flexible new system based on regional need. Their spokesperson Stephen Psallides, stated in May 2001: “The Barnett Formula is quite clearly outdated, inflexible and unfair. Tony Blair is only saying it’s fair because he is visiting Scotland, which gets far more money under the Formula than the North East [in England]”.<sup>120</sup>
- Many of the candidates in the 2000 London Mayor election stated that the Barnett Formula needed to be reviewed and amended as London pays out far more in taxes than it receives in spending, including the currently-elect Mayor Ken Livingstone. Moreover, Steve Norris, the Conservative candidate for Mayor, suggested that the Barnett Formula should be reviewed and that a new assessment of need be carried out to address the fiscal imbalance between London and the rest of the UK.<sup>121</sup>

In light of the above, it seems that there potentially is support in the other devolved governments if Northern Ireland sought to reform the Formula. However, it remains uncertain beyond at least 2004 as to what Westminster’s intentions are for the future use of Barnett in the UK.

#### **PART 4: CONCLUSION**

This paper reveals the apparent complexity of the Barnett Formula. As mentioned in the introduction, the paper should be viewed only as a useful starting point in assisting the Committee to help develop it’s understanding of the Formula.

The main points of the paper are as follows:

- The Barnett Formula arises in the context of central government reviewing its spending plans and making changes in the spending allocations to the devolved administrations’ DEL, specifically the assigned budget items of DEL.
- While the Barnett Formula is considered a robust mechanism for public expenditure allocation, it’s long history seems to have been far from straightforward. For example, the recent fundamental change in the way UK government, (central and devolved), accounts for and controls public expenditure, i.e. Resource Accounting and Budgeting (RAB).
- Currently applied, the Barnett Formula calculates each UK departmental programme in DEL. The results of each calculation consequently form the aggregate net change to the assigned budget element of DEL for each devolved administration. It then is for each devolved administration to allocate spending within their assigned budgets according to their own priorities.<sup>122</sup>

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<sup>119</sup> *The Guardian*. 24 April 2001.

<sup>120</sup> Newcastle Liberal Democrats’ Media Release. 15 May 2001.

<sup>121</sup> “Norris Demands a Fair Deal for London”. 16 March 2000.

<sup>122</sup> *Ibid*, p. 6, para 3.6.

- Barnett figures\* for 1998-99 to 2001-02 are as follows:<sup>123</sup>

	<b>1998-98</b>	<b>1999-2000</b>	<b>2000-01</b>	<b>2001-02</b>
<b>Scotland</b>	£ 13.1 bn	£13.8 bn	£14.5 bn	£15.1 bn
<b>Wales</b>	£ 6.7 bn	£ 7.0 bn	£ 7.4 bn	£ 7.8 bn
<b>Northern Ireland</b>	£ 5.7 bn	£ 5.9 bn	£ 6.2 bn	£ 6.3 bn

\*Note that the above-stated figures include the total amount of DEL, so they include a small proportion of monies that are not determined by Barnett, and instead are centrally negotiated. However, the figures are used to highlight the amounts determined by Barnett.

- On balance, the practical implications of Barnett seem to include both positive and negative effects for Northern Ireland, Scotland and Wales, as well as for England.
- A number of advantages and disadvantages have been identified about Barnett in relation to Northern Ireland, Scotland, Wales and England.
- There is growing consensus for a review of Barnett. Moreover, there seems to be two clear positions taken on Barnett and its future, i.e. (i) replace Barnett and (ii) retain it. It appears that if it was decided that it should be replaced with a needs assessment-based mechanism, developing one could be fraught with difficulties. Moreover, reform of Barnett could result in Northern Ireland receiving less public expenditure.
- It seems that there potentially is support within other devolved governments if Northern Ireland sought to reform the Formula. However, it remains uncertain as to what Westminster's intentions are, apart for the Government's announcement that Barnett would remain in place until at least 2004.

In using this paper, the Committee may find it appropriate at a later date to seek specialised assistance from sources both outside and inside the Department of Finance and Personnel to fully formulate its views in this area. Such assistance could authoritatively expand on the points raised throughout the paper, e.g. what changes will resource accounting inevitably require in the application of the Barnett Formula.<sup>124</sup>

Moreover, the Committee may wish to seek such assistance to investigate whether there are any potential inter-relationships between the use of public private partnerships (PPPs) in Northern Ireland, Scotland and Wales to fund public service provision, and the continued use of the Barnett Formula, which merit further consideration by the Committee, particularly given its recent report on PPPs, e.g. PPPs cutting into Northern Ireland's assigned budget items in DEL.<sup>125</sup>

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<sup>123</sup> Day, Karen. 8-14 October 1999, p. 24.

<sup>124</sup> Id.

<sup>125</sup> Northern Ireland Assembly, Committee for Finance and Personnel. *Report on the Inquiry into the use of Public Private Partnerships*. Session 2000/2001. Seventh Report. The Stationary Office. Belfast: 26 June 2001.