



Northern Ireland  
Assembly

**Committee for Finance and Personnel**

**OFFICIAL REPORT  
(Hansard)**

**Barnett Formula: Departmental Briefing**

**21 March 2012**

# NORTHERN IRELAND ASSEMBLY

## Committee for Finance and Personnel

### Barnett Formula: Departmental Briefing

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**Members present for all or part of the proceedings:**

Mr Conor Murphy (Chairperson)  
Mr Dominic Bradley (Deputy Chairperson)  
Mrs Judith Cochrane  
Mr Leslie Cree  
Mr David Hilditch  
Mr William Humphrey  
Mr Paul Maskey  
Mr Mitchel McLaughlin  
Mr Adrian McQuillan

**Witnesses:**

Mr Peter Jakobsen	Department of Finance and Personnel
Mr Bill Pauley	Department of Finance and Personnel

**The Chairperson:** You are very welcome, gentlemen. I remind members that the purpose of the meeting is to take initial evidence from the Department of Finance and Personnel (DFP) that will inform the Committee's inquiry into the Barnett formula. I welcome Bill Pauley, the head of strategic policy, and Peter Jakobsen from DFP's central expenditure division, to talk us through the issue. We sent the Hansard report of our meeting with the expert witnesses to DFP for a response. Perhaps, gentlemen, you could kick off the meeting, after which we will open the floor to questions.

**Mr Bill Pauley (Department of Finance and Personnel):** We will address the Committee briefly, Chairman. Thank you. We have provided a short paper containing general points as well as our comments and views on the expert witnesses' evidence. The strategic policy division and the central expenditure division are represented here because, although staff in the strategic policy division cover some technical aspects of Barnett, other issues that were covered with your expert witnesses, such as the disputes process, end-year flexibility and other aspects of the statement of funding policy, are led much more by the central expenditure division in the central finance group.

As we say in the paper, we are not aware of any current or planned review of the Barnett formula. The current statement of funding policy recognises that a revision of the statement of funding policy may be necessary as a result of the outworkings of the Calman and Holtham commissions. At present, however, our expectation is that there will be no review of the Barnett formula in the current spending review. However, it is common for there to be revisions to some wider aspects of the statement of funding policy.

The Department is not working on a review of the Barnett formula, and nor are we looking at changing it in any way. The most important thing about the Barnett formula and the way in which we work with it is to understand what it is and what it is not. We work with it on the basis that it is a formula that provides a population-based proportion of comparable changes of expenditure in England; that is the basis on which we look at changes to it. We know which aspects of our expenditure are excluded from Barnett; they are defined in chapter 5 of the statement of funding policy.

I will stop there. I am happy to take questions.

**The Chairperson:** Thank you for your response. The expert witnesses said that Barnett is not a fix and that it was never intended to be a permanent measure. That is why it surprises me that the Department is doing no work in preparation for a change in Barnett, because it was never a fixed form, even though it has long outlasted its intended time frame.

The expert witnesses' evidence was that the graph of Barnett in whatever benefits could have been said to have accrued to devolved regional Administrations is starting to turn in the other direction. Even if Barnett were not to change, it may lead to a worse deal for this region. In that regard, I am surprised that DFP officials are not at least advising the Minister that Barnett is progressively becoming a worse deal for the North, if you concur.

The fact that you are not doing any work at all means that there is no assessment in the Department of whether Barnett continues to provide as it originally did; whether it will continue; whether it is in our interest to change Barnett; whether it is in our interest to go along with constant minor revisions; or whether we should consider the benefits of a more fundamental review of Barnett. I am a little surprised that the Department is doing no work on that at all, because whatever you consider our influence to change Barnett in our interests to be, we need at least an assessment from the Department on whether it continues to work for us or whether it is starting to work against us.

**Mr Pauley:** We would agree with the expert witnesses that, at times of rising public expenditure, we would expect some convergence towards the public expenditure per head with England, although that can also depend on the comparability of different changes that happen. Therefore, depending on which areas of expenditure increase or decrease in England, the level of convergence is not a given. At times of falling public expenditure, the convergence effect is different; it goes the other way.

As signalled by the Government, we expect that — at a time, such as now, when the Scotland Bill may change, and there would be a settling period of public expenditure beyond the period of this spending review — there would be a review of expenditure arrangements. That is based more on the fact that after Calman and the Scotland Bill, 30% of their resource income will come from tax and other revenue, as opposed to the much larger proportion of it that is determined by the Barnett formula.

**The Chairperson:** Therefore, your assessment is that there is a different analysis: expert witnesses say that there is a graph that is starting to go downwards; and yours, which is more of peaks-and-troughs argument. You say that, because public expenditure is going down, the effects of Barnett will be more negative but that that will change again if public expenditure goes up. That is a direct contradiction of —

**Mr Pauley:** The convergence effect is different at a time of falling public expenditure than it would be at a time of rising public expenditure. That is simply because it is a mathematical formula, and the maths mean that, when expenditure is going up, we move more towards the per head expenditure in England. It works the other way when expenditure is going down.

**The Chairperson:** Therefore, DFP is of the view that there are no long-term concerns if Barnett were to remain unchanged, as it would not progressively disadvantage this region.

**Mr Pauley:** Public expenditure trends may change, although it is hard to see how immediately. The Government's priority is still to deal with the deficit. We expect the work to continue and remain a feature of the spending review period after this one. In that time, concerns about the convergence

effect of Barnett would not be as great as they may be under a different trajectory of public expenditure.

**Mr D Bradley:** The expert witnesses raised a point about the lack of transparency in the Barnett formula. What is your experience?

**Mr Pauley:** The formula is transparent; a vast volume of information is now published by the Government on expenditure and changes in expenditure that we can track and see. The changes to comparability factors that we have had have been minimal. There has been minimal change in that area. The statement of funding policy clearly sets out that it uses the mid-year Estimates and updates the population based on most recent data. That aspect of it is transparent.

Many other aspects can affect the amount of money that we receive beyond Barnett; that is where there are areas of less transparency. It is around how a decision is taken, for example, that the Olympics be excluded from the Barnett calculation. It is around the approaches to end-year flexibility or the public expenditure treatment of European funding that are included in other chapters of the statement of funding policy that it becomes more difficult to see and to track openly all the changes that can happen and where decisions can affect our total expenditure.

**Mr D Bradley:** In his evidence on 8 February, Mr Trench said:

*"Part of what is needed is much greater publication of information by the Treasury about, for example, what money goes to which Government for which services. At the moment, data and information are scattered over various sources. Details of changes in block grant allocations for Scotland and Wales, but not for Northern Ireland, are published in the annual reports of the Scotland Office and the Wales Office. Those figures are simply put into the public domain; there is no way for anyone outside to assess their accuracy."*

Do you agree?

**Mr Pauley:** The Government publish a vast volume of expenditure information through which those issues can be tracked; it can be difficult and time-consuming to move between various documents. In some ways, it is similar to our review of the financial processes whereby different publications can use slightly different definitions or have different meanings depending on their purpose. The simplification of that will help with the simplification of published data, but this Government publish a vast volume of information on expenditure at a very low level. We could not ask them to go to a lower level of information. It is to do with the ability to find a way through a vast volume of information and to look at aspects of it. As a Department, we are asked about changes and checks, and we consult the spending Departments to check their knowledge of the changes that might have happened. We look at significant changes when we get Barnett consequentials — the pluses and minuses — and we arrive at our net figure. It is not easy, but a vast volume of information is published.

**Mr D Bradley:** Are you satisfied that there is enough transparency in the system to ensure that Northern Ireland benefits from Barnett consequentials to the extent that it should on each occasion?

**Mr Pauley:** Beyond the disputes are issues that are excluded from Barnett. We can do a reasonably detailed analysis to check whether the sums have been calculated correctly. It is more difficult when decisions are taken on whether expenditure should be included as part of the comparable expenditure.

**Mr Peter Jakobsen (Department of Finance and Personnel):** We routinely challenge the Treasury on its funding of English Departments as to whether it is Barnett for us or not. We ask for explanations, and, if we are not happy, we will continue to ask. For example, we took it to a formal dispute over the Olympics, because we were not content with the explanation given. When there is a logical explanation, we are quite content. So we do challenge.

**Mr Cree:** The Barnett formula was designed as a temporary measure, but it has been here for a long time. Given its unhypothecated nature, do you think that it satisfies people on this side of the water rather than proceeding into a needs-based application?

**Mr Pauley:** We are content with the unhypothecated nature of Barnett, as we can allocate expenditure in line with our needs as we perceive them and in line with the priorities towards which we are working.

Intellectually, a needs-based system sounds more appropriate. With our budget and system, we try to allocate public expenditure in line with needs. Population is, of course, an indicator of need, but what else could be added? For many areas, reference is made to the population of different age groups and other such issues.

However, a needs-based system could be hugely complex. Some people have suggested a restriction to three or four indicators, which would leave the system no more transparent, just as difficult to understand and perhaps as hard to challenge in the way that Peter has described, in some of the additions and changes that have happened. It is not clear where we would emerge in a needs-based approach or whether our allocation would be different. In the absence of that, it is difficult to know what to wish for.

**Mr Cree:** If it were a needs-based approach, there would be flexibility to meet emerging needs as they occur rather than the current inertia. Our system suits us. There are problems around the edge — for example, when it is UK-wide, we get our share. Do we stick with what we have rather than having the hassle of a more difficult situation that would involve continuous work?

**Mr Pauley:** Our relative needs would need to change in comparison with those of the UK.

At varying levels of data, Northern Ireland ranks differently to other regions. At NUTS 1 level, in many of the economic indicators, we are often at the bottom or second or third from the bottom. If we move to NUTS 2 level data, that position is more varied, and we are often about midway in the ranking of UK regions on the main indicators. That is a feature of how different aspects of expenditure — for example, European funding — is allocated at NUTS 2 level. The money that we receive under different structural funds programmes is determined at that level. That is when areas such as Cornwall, West Wales and the Valleys are seen at higher levels of need. Parts of England such as the north and the north-west score highly on some indicators of need. Therefore, Northern Ireland's ranking in a needs-based system depends on what system is put in place.

**Mr Cree:** You referred to the economy, which is interesting. The structure was set up to allow the regions to converge on the tight south-east; however, the opposite has happened, and it has gone the other way in that it is diverging. Instead of the tight south-east, we now talk about the greater south-east. The regions on the periphery are suffering, but no one has done anything positive to tackle that. Perhaps it is the same with the Barnett formula. Would that be fair?

**Mr Pauley:** This Government would argue that they are attempting to rebalance the economy —

**Mr Cree:** The jury is still out on that one.

**Mr Pauley:** — and the effects of that.

**Mr McLaughlin:** My question is pretty much on the same line. The evidence is very interesting in that a design feature of Barnett deliberately overlooks that variation. There is talk about convergence almost as a principle. However, first, convergence is never achieved, and, secondly, there is no attempt to develop mechanisms because that would go in the direction of a needs-based application. The expert witnesses may not necessarily have been travelling in the same direction, but they seem to arrive at the same conclusion: it is possible to have a simplified approach that uses four or five indicators, which would give a 96% outcome. They thought that that was very good because it would be difficult to attain perfection, and, were it to be applied across the different regions, it would address directly the issue of convergence and the underlying parity argument that sometimes pops up here and gets in the way of political discussions and decision-making. In a sense, the unhypothecated arrangement simply sets aside the parity argument because it is a perfect example of the Assembly using its own judgement as to the best place to apply the available resources. Therefore, parity is not such a principle here either when it comes to it.

There are good pragmatic reasons — I support them — for applying our best judgement to local needs. However, it would appear that, although the negotiations would be difficult, the regional Assemblies could apply the needs indicators to develop or strengthen the argument that, although the current approach is convenient and a relatively mechanistic, formulaic process that makes life easy at Westminster, we could add value in a way that allows the Assembly to address unmet needs. Could the Assembly consider running its own exercise, if only to give strength to the arguments of our Ministers when it comes to this engagement?

**Mr Pauley:** As I said, we are not undertaking any such work. However, indicators of need are used by Departments in their bids for expenditure here, and many indicators exist nationally to do that. If we were to try to get four or five indicators that would apply across the whole of the UK, I am not sure how quickly that could be agreed and whether all the regions would agree. Various indicators would benefit different parts of the UK differently. Part of the debate would be influenced by where it was thought that the outcome was going. It would be extremely complex to arrive at even a small number of indicators, and the debates about whether they were fair or better might well continue.

**Mr McLaughlin:** However, from the beginning, the experts accepted that many indicators could be reached to give what I thought would be a fairly pragmatic conclusion. They had run tests and had modelled it. For instance, they said that using indicators such as demographics, health, poverty, deprivation and sparsity of population could give a 96% outcome. They said that that would be a good outcome and would result in a more responsive formula than the current arrangements; it appears to me that that is correct.

If you were start with a green field, it might be difficult to get all the regions to converge. However, if you were, as a basis for negotiation with the Treasury, to offer the regions a model that pre-identified four or five headings that could be weighted, there would be a better chance of buy-in from them, if only to test and see. Others could be added over time, or you may settle for a 96% outcome whereby people were at least comfortable that need was being quantified and that they were getting a reasonable and fair response through an agreed formula.

Work is being done in universities in England; the expert witnesses come from that experience. I wonder whether our universities could tap into that and whether we can take the discussion further rather than accepting what I think is a very one-sided arrangement here. Up to a point, the arrangement suits. In the previous mandate, I was part of a delegation from this Committee that met the House of Lords Select Committee on the Barnett Formula. That Committee accepted and recommended that a needs-based approach was fairer. That was not accepted by the Government, but the Select Committee recognised the evidence. Perhaps we need to do a bit more to help ourselves.

**Mr Pauley:** Intellectually, the argument is strong. A needs-based approach has many attractions for all regions.

**Mr McLaughlin:** It would be a mistake to overcomplicate it.

**Mr Pauley:** An outcome of 96% for four or five indicators is very good, and, if five or six, or six or seven, indicators were used, the percentage would probably rise slowly, although I do not know that for sure.

**Mr McLaughlin:** They have tested it, and that seems to be their observation.

**Mr Pauley:** It is not clear what differences that would make to our allocations.

**Mr McLaughlin:** It was tested in Wales, and it was discovered that Wales could be £300 million better off annually. Perhaps if we tested it, we might discover that we would not be better off. However, it was done on a regional basis, drawing comparators from England, and it was discovered that Wales is being underfunded.

**Mr Pauley:** About 10 years ago, extensive work was done in the Department, and it was inconclusive. It was carried out across a much larger number of indicators than four or five, and it looked at different areas of expenditure.

**Mr McLaughlin:** I know that there would need to be political will to take the idea any further, but it seems to me that the Committee will have something of interest to explore.

**Mr Pauley:** That is certainly interesting work. The Department is looking closely at how some of the other features of the funding policy might adjust it, particularly how the changes in Scotland and in some other regions will affect financial allocations there and the mechanisms that are being put in place. I understand that there is a ministerial statement at Westminster today on adjusting Scotland's block grant. It will cover some of the detail of how that will happen. In the immediate future, there will be an examination of how those processes might be adjusted, how Scotland will handle the additional risks and how mechanisms might be put in place to adjust for changing economic circumstances in Scotland relative to England. It is an area of new work — of changing focus — that will affect 30% of Scotland's budget. Were we to secure the devolution of corporation tax, perhaps 17% to 20% of our budget, depending on what we pay for corporation tax, there is a substantial chunk of what might happen to the block grant on which we would be doing some of our first work.

**Mr McLaughlin:** It means that we are hostages to what happens in other regions. We are not adding value to the data that will be used to inform those decisions.

**Mr Pauley:** The separate chapters in the statement of funding policy are quite short, although they may be longer post-Calman.

**Mr McLaughlin:** In their impact.

**The Chairperson:** Your paper states that it is not necessarily about the complexity of using variants on the basic Barnett formula. Obviously, they are used to calculate European funding, at least for exercises in Wales and Scotland, and also to allocate money internally in England. It is about the political fallout when the Treasury decides to use whatever indicators it wants to its own advantage, or our being a much smaller region in the overall picture, we get screwed, if you like, in any negotiations, and the variants that would suit us are not used. Is my understanding correct, that it is not so much the complexities of trying to put these things together, because that information is there, but the political fallout of an attempt to change it?

**Mr Pauley:** That process would be difficult at an official level; it leads to a political level, which is where debates are resolved or left unresolved because of disagreements. It would be hugely complex. There are different combinations of different indicators, as we see internally in Northern Ireland as we look at the deprivation indicators and how different ones work for different areas, and those same issues would emerge, even as we tried to have a small number of well-recognised indicators of economic or social well-being here compared with other parts of the UK. Those debates would be protracted and difficult.

**The Chairperson:** Debates generally are protracted and difficult, but that should not put us off them.

The Finance Minister reacted to the speculation about regional pay and the potential for that to be devolved here. Would any variations in regional pay affect Barnett? How would any adjustments be calculated and implemented?

**Mr Pauley:** We do not have any precise conclusion that we can give you on that at the moment. The position in Barnett of most public sector pay is different to the situation for pensions. Pensions are included in chapter 5 of the statement of funding policy; they come under annually managed expenditure (AME), whereas pay is in resource departmental expenditure limit (DEL).

Resource DEL changes in England would, through Barnett, automatically be reflected here. The extent of any English expenditure that is changed as a result of any significant changes in pay would automatically be reflected in Barnett. It then comes down to the proportions of public sector jobs that

might be affected in England as opposed to other areas. We have not determined how that would work. However, I can tell you that it affects us in a different way than pensions, because, quite simply, pensions are an AME expenditure whereas most pay is in resource DEL, and it would flow through in that way.

**The Chairperson:** It is not an area that you have gone into, but if there were a regional separation in certain public sector pay, and the Government in Westminster decided to increase nurses' pay, that would not necessarily flow to here as a Barnett consequential.

**Mr Pauley:** Nurses' pay is in resource DEL; that would be an increase in expenditure in health. The comparability factor is more than 99%, so we would get a significant Barnett consequential if the Department's expenditure as a whole increased in England and was not compensated for by a reduction elsewhere. Resource DEL and most pay is in Barnett, whereas pensions expenditure is in AME. It would work differently.

**The Chairperson:** We will probably want to return to that issue as it rolls out. At the moment, it is a battle of press releases rather than any detail, but we will see how it goes.

**Mr Pauley:** We have not had detailed discussions with the Treasury at official level to look at what exactly is being proposed — that is not yet known — and the outworkings. However, that will be done.

**The Chairperson:** Thank you very much.