HOUSE OF COMMONS LIBRARY

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The UK Shared Prosperity Fund

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Summary

After the UK leaves the European Union, it will no longer receive structural funding (which is worth about £2.1 billion per year). This funding is used for boosting several aspects of economic development, including support for businesses, employment and agriculture, and is administered by the different nations of the UK.

In order to replace this funding, the Government has pledged to set up a Shared Prosperity Fund to "reduce inequalities between communities".[1]

There are several issues that will need to be considered when setting up the Fund. These include:

- the priorities and objectives of the Fund;
- the amount of money to be allocated;
- the method of allocating it between the countries and regions of the UK, and whether this is based on need (and what measure is used to determine need);
- the model by which funding will be allocated, whether pre-allocating an amount for a country or region or inviting competitive bids from across the UK;
- the length of the planning period and the way in which this could conflict with domestic spending priorities;
- who administers the funds (whether they are controlled from Westminster or by the devolved administrations) and the degree to which local authorities are involved;
- the implications of the Fund for state aid rules.

Although the Government has not yet published its consultation on the Fund, a number of organisations have already made comments about the possible design. Although these vary in their emphasis (for example, the Welsh Government is strongly opposed to the idea of administering the Fund from Westminster), most organisations seem to agree that the level of funding should be at least maintained at its current level, it should largely be allocated based on need, and local authorities and partners should be closely involved.

[1] Conservative Party, *Forward, Together: Our Plan for a Stronger Britain and a Prosperous Future*, 18 May 2017

1. Background to the Fund

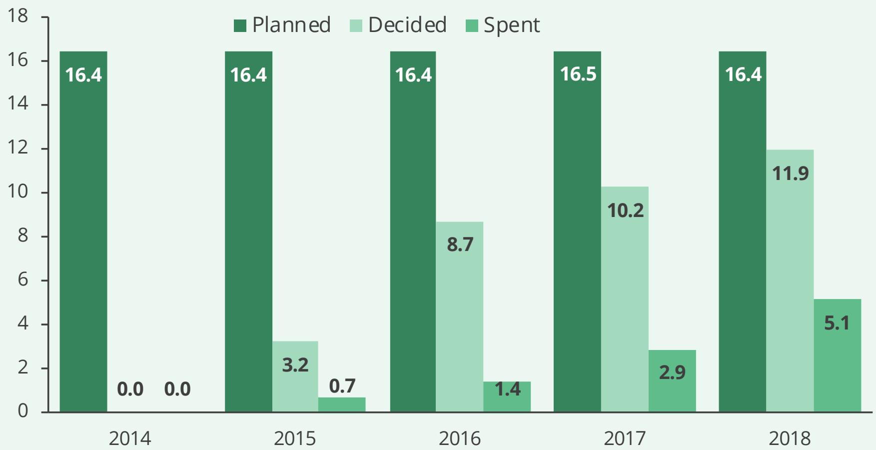
1.1 Structural funding from the EU

The European Union provides several streams of funding to its Member States, for various purposes. One of these streams – the European Structural and Investment (ESI) funds – aims to reduce disparities in the level of development in the regions of the EU and to help less developed regions to catch up.

The EU has allocated €16.4 billion in structural funding to the UK between 2014 and 2020.

The UK's ESI funding allocation over the 2014-20 financial framework period is **€16.4 billion** (around £15.0 billion at September 2019 exchange rates) – when combined with co-financing from the UK, €26.7 billion is expected to be spent on ESI-related projects over this period. As of 31 December 2018, €7.8 billion of this had been spent, of which €5.1 billion was EU funding.[2]

EU structural funding to the UK, by year
Cumulative 2014-20 totals at year end, € billions



Source: European Commission, ESIF 2014-2020 Finance Implementation Details, 2 September 2019

Within the UK, ESI funding comes via four funds: the European Regional Development Fund (ERDF), the European Social Fund (ESF), the European Maritime and Fisheries Fund (EMFF) and the European Agricultural Fund for Rural Development (EAFRD). Of these, the ERDF and ESF are the largest, between them accounting for over 60% of ESI funding over the current 2014-20 programming period.

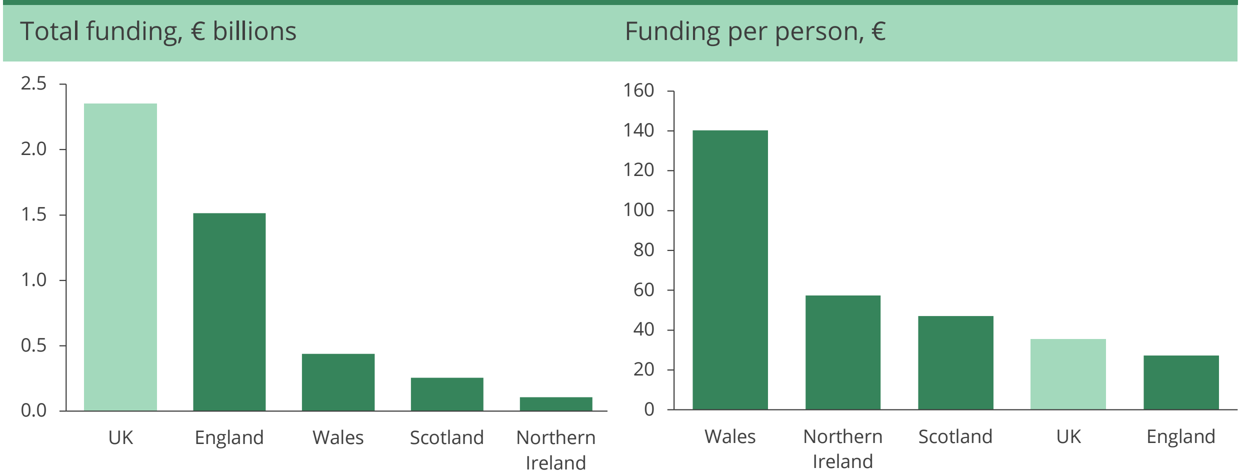
Country and regional breakdown

Allocations from the ESI funds are made on the basis of classifying regions into different categories, based on their economic development as measured by GDP per person. Regions which are classified as less developed receive proportionally more funding; this results in the different nations of the UK receiving different amounts.

Less economically developed countries and regions receive proportionally more funding.

[2] European Commission, *European Structural and Investment Funds*, as of 2 September 2019

ESI funding across the UK, 2014-20 average per year



Source: European Commission, ESIF 2014-2020 Finances Planned Details, retrieved 6 September 2018

Although England receives more ESI funding than any other country of the UK in total, this is largely because of its much higher population; in per-person terms, Wales receives more than twice as much as any other country of the UK (€140 per person per year, compared to a UK-wide average of €36).

What the funding is spent on

Money from the ERDF and ESF, the two funds which make up the majority of ESI funding, has been spent on the following priorities so far in the 2014-20 programming period:

ERDF and ESF funding, by priority axis
2014 - July 2019

	£ millions	% of fund
European Regional Development Fund		
1: Research and innovation	426.5	22%
2: Enhancing access to, and use and quality of, ICT	59.8	3%
3: Enhancing the competitiveness of SMEs	898.9	46%
4: Supporting the shift towards a low carbon economy in all sectors	364.0	19%
5: Promoting climate change adaptation, risk prevention and management	37.1	2%
6: Preserving and protecting the environment and promoting resource efficiency	42.6	2%
7: Sustainable transport in Cornwall and the Isles of Scilly	29.8	2%
8: Promoting social inclusion and combating poverty and any discrimination	28.5	1%
9: Technical Assistance	49.6	3%
European Social Fund		
1: Inclusive Labour Markets	1,031.3	73%
2: Skills for Growth	358.6	25%
3: Technical Assistance	22.3	2%

Source: MHCLG, European Structural and Investment Funds List of Operations 2014 to 2020, July 2019

This shows that the ERDF mainly focuses on support to small businesses and on research and innovation, with a smaller emphasis on moving towards a low carbon economy. The Government has produced a booklet of case studies of projects that have been funded under these three priorities; many of the projects described focus on creating research centres and workspaces, or providing technical support to businesses.

Most funding is focused on economic development through research and boosting employment.

The ESF, on the other hand, is very strongly focused on employment, with most of the projects listed in the Fund's most recent case studies booklet relating to getting people into the workforce or helping to improve their skills. They do this in a variety of ways, either by building networks between employers, local authorities and charities, or by working directly with disadvantaged or disabled people to help them move into work.

The impact of structural funding

The impact of structural funding is hard to measure, particularly in wealthy countries like the UK.

Between 2012 and 2014, the Government carried out a "Review of the balance of competences" of the EU, which was intended to be "an audit of what the EU does and how it affects the UK". This included a report on Cohesion Policy, which looked at the impact of the structural funds.

This report suggested that the impact of the funding was hard to measure and that such evidence as we did have was mixed, particularly for richer countries such as the UK:

> The contribution that structural funds have made to convergence within richer member states is much less clear, in part because they represent a very small proportion of available funding. West Wales and the Valleys remained a less developed region for 2014-20, despite having been an objective one region in 2000-06 and a convergence region for 2007-13, and its GDP per capita had

> fallen from 74.1% of the EU25 average in 2000 to 64% of the EU28 average in 2011. The Welsh Government noted in its evidence to the review that this was because of long-standing economic challenges and a more general decline in UK GDP and suggested that, in terms of employment and skills, West Wales had closed the gap with other parts of the UK. The Welsh Local Government Association asserted that the strong redistributive nature of the EU regional policy had benefited Wales in the absence of a robust redistributive regional policy within the UK. Policy Economics on behalf of the European Movement noted that the number of UK regions that fell into the lowest category – whether objective one, convergence or less developed – had fallen.[3]

In general, the Review suggested that funding such as that provided by the structural funds was certainly useful in countries and regions where this funding made up a significant proportion of GDP. In the UK (where this is not the case) it is much harder to see the impact, particularly due to a lack of reliable data and the difficulty of separating out the effects of other policies and general economic conditions.

In 2012, the Communities and Local Government Committee held an inquiry into the European Regional Development Fund. The inquiry report concluded that it was difficult to see the impact and value for money of the Fund at a regional level, but that it was "highly valued by local authorities and other recipients," and had made "vital contributions to a variety of projects across the country".[4]

Administration of the funds

ESI funds are administered jointly between the EU and nominated Managing Authorities in the Member States. The Managing Authority puts together an operational programme, laying out their strategy and priorities for the funding; this is then agreed with the European Commission, which then allocates funding to the Authority so they can distribute it.

BEIS and Defra are the Managing Authorities for England, while the devolved administrations in Scotland, Wales and Northern Ireland take on this role in their respective countries.

The end of funding

After the UK has left the EU, this funding will stop. The Withdrawal Agreement currently before Parliament includes provisions to maintain the current arrangements for structural funding until the end of the transition period; however, when this transition period ends (or if the UK leaves the EU without a deal), the funding will cease.[5]

For more information on the ESI funds, and on EU funding in general, see the Library's briefing on UK funding from the EU.

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[3] BIS and FCO, *Cohesion policy: review of the balance of competences*, paragraph 3.24, 21 October 2013

[4] Communities and Local Government Committee, *European Regional Development Fund*, 4 July 2012

[5] According to Article 132 of the Withdrawal Agreement, ESI funding would also stop after the end of 2020 even in an extended transition period, as the ESI funds are part of the 2014-20 financial framework.

1.2 Promised replacements for funding

Structural funding will end when the UK leaves the EU. The Government has promised to replace it with a Shared Prosperity Fund.

In the short term, the Government has guaranteed all EU funding agreed before the UK leaves the EU, even in the event of no deal being reached.[6] This includes the structural funds, so even if funding from the EU stopped, beneficiaries would still receive their money from the UK public purse instead.

The Government has also said that it will create a long-term replacement for the ESI funds. The first mention of doing this by means of a Shared Prosperity Fund was in the 2017 Conservative Manifesto (emphasis added):

> We believe in one nation – in helping every part of our country share in the prosperity and opportunity of our great United Kingdom. Yet there is much to do. Current EU-wide structural funding was designed to tackle disparities but it is expensive to administer and poorly targeted. As we leave the European Union, we must look at how we can better reduce and eliminate these inequalities.
>
> **We will use the structural fund money that comes back to the UK following Brexit to create a United Kingdom Shared Prosperity Fund,** specifically designed to reduce inequalities between communities across our four nations. The money that is spent will help deliver sustainable, inclusive growth based on our modern industrial strategy. We will consult widely on the design of the fund, including with the devolved administrations, local authorities, businesses and public bodies. The UK Shared Prosperity Fund will be cheap to administer, low in bureaucracy and targeted where it is needed most.[7]

The commitment to a Shared Prosperity Fund was then echoed in November 2017 in the Industrial Strategy white paper.

In July 2018, James Brokenshire (Secretary of State for Housing, Communities and Local Government) made a Written Statement setting out more details about the Fund. The main points of this statement were:

- The purpose of the Fund is "to reduce inequalities between communities across our four nations";
- The method for doing this is "strengthening the foundations of productivity as set out in our modern Industrial Strategy to support people to benefit from economic prosperity";
- The role of the Industrial Strategy is heavily emphasised, both at a national and local level, with local areas in England "being asked to prepare Local Industrial Strategies to prioritise long-term opportunities and challenges to increasing local productivity";
- The Government will "respect the devolution settlements in Scotland, Wales and Northern Ireland" so that the Fund works across the UK;

6 HM Treasury, *The government's guarantee for EU-funded programmes if there's no Brexit deal*, 3 December 2018

7 Conservative Party, *Forward, Together: Our Plan for a Stronger Britain and a Prosperous Future*, 18 May 2017

- Consultation on the design of the Fund would take place later that year.

Throughout the rest of 2018, the Government continued to say (both in the Chamber and in responses to PQs) that it would be consulting on the Fund that year. In December 2018, PQ responses began to say instead that the consultation would be published "shortly"; in January 2019, a further PQ implied that the delay had been due to no-deal Brexit planning:

The consultation on the Fund has been delayed, and it is not clear when it will take place.

> PQ 212622, House of Commons: **UK Shared Prosperity Fund**
>
> **Ministry of Housing, Communities and Local Government**
>
> *Asked by Dan Jarvis (Barnsley Central) on 25 January 2019*
>
> To ask the Secretary of State for Housing, Communities and Local Government, pursuant to Question 207151 and with reference to the oral contribution of the Prime Minister on 21 January 2019, Official Report Column 52, when he plans to start the consultation on the UK Shared Prosperity Fund; and for what reason that consultation has been postponed.
>
> *Answered by Jake Berry (Rossendale and Darwen) on 30 January 2019*
>
> Whilst the Government remains committed to securing a good Brexit deal, it is right that we also plan for a no-deal scenario and we have therefore continued to review our approach to the UK Shared Prosperity Fund (UKSPF) consultation accordingly. The Government recognises the importance of reassuring local areas on the future of local growth funding once we have left the European Union and providing clarity on UKSPF. Therefore we intend to publish the full consultation document shortly.

More recent PQ responses have said that final decisions on the Fund's design will be taken during the Spending Review.[8] The plan was originally to hold a full Spending Review in 2019, alongside the Autumn Budget; however, this has now been postponed to 2020, with a one-year Spending Round replacing it to provide spending plans for 2020-21.[9] The Government has not said whether it intends to publish the Shared Prosperity Fund consultation at this Spending Round, or leave it until later; however, an oral answer from Minister Kwasi Kwarteng on 27 June 2019[10] suggested that details on the Fund would not now be released until 2020.

1.3 Parliamentary debates

There have been two debates in Westminster Hall about the Fund since its announcement. In the first, on 14 May 2019, Members raised the issue of when the consultation would be brought forward, and there were speeches supporting the idea of decisions being taken locally, funding going to the devolved nations, and inequality being tackled.

Jake Berry, the Under-Secretary of State for Housing, Communities and Local Government, agreed that tackling inequality was important, but

8 See, for example, PQ 214087 on 4 February 2019.
9 For more details, see the Library's briefing on Background to the 2019 Spending Round.
10 HC Deb 27 June 2019 c789

would not commit to specific decisions on the form taken by the Fund before the consultation had taken place.

The second debate was on "Replacement of EU structural funds for less developed regions", and took place on 26 June 2019. Many of the concerns raised were the same as in the previous debate, but there was more of an emphasis this time on the total amount of money that would be made available to the Fund.

Much of the debate was informed by a piece of analysis published in January 2019 by the Conference of Peripheral Maritime Regions (CPMR),[11] which argued that GDP per person has decreased in a number of regions across the UK relative to the EU average. The result of this would be that if the UK were to remain part of the EU during the 2021-27 framework period, a total of five regions in the UK would be categorised as 'less developed regions' (up from the current two), and the UK would therefore receive around €13 billion in regional development funding over this period.

The Library has attempted to replicate this analysis, with some success – the latest data indicate that at least six regions could in fact be classified as less developed regions in the next framework period (Tees Valley and Durham, South Yorkshire, Lincolnshire, Cornwall and Isles of Scilly, West Wales and the Valleys, and Southern Scotland). The 'Outer London – East and North East' region is also on the borderline for this classification.

However, this does not necessarily mean that these regions would have received the amount calculated by the CPMR. First, the amounts received are always subject to negotiation. Secondly, the allocations proposed by the EU for the next framework period assume that the UK will have left the EU at that point; if it had remained, the negotiations may have proceeded differently. Moreover, the EU has also proposed to limit increases by 8% relative to the previous framework period.[12]

The CPMR's data also confirm that many regions in the UK have been growing more slowly than the EU average, particularly since 2016. However, this does not necessarily indicate greater regional inequality within the UK, as the trend is also affected by the high growth in the Eurozone around 2016-17.

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11 Conference of Peripheral Maritime Regions, UK entitled to €13bn regional funding if it remains in EU, January 2019

12 See paragraph 11, Annex XXII of the proposed regulation setting up the funding structure for the next framework period.

2. The Fund's design

The design of the Fund will need to take several factors into consideration.

The Shared Prosperity Fund will of course require considerable thought in its design, with a number of different factors to take into consideration. The Government has carried out some stakeholder engagement events to collect views on the design of the Fund – according to a PQ in April 2019,[13] there have been 25 such events so far.

Some possible issues to consider in the Fund's design are listed below.

2.1 Funding priorities

The main EU structural funds were set up in the EU Treaties – for example, the legal basis for the ERDF is set out in article 176 of the Treaty on the Functioning of the European Union:

> The European Regional Development Fund is intended to help to redress the main regional imbalances in the Union through participation in the development and structural adjustment of regions whose development is lagging behind and in the conversion of declining industrial regions.

This means that the priorities and aims of these funds are in line with the priorities of the EU. As the UK Government replaces structural funds with the Shared Prosperity Fund, it can define its own priorities.

The Conservative manifesto said that the new Fund would be designed "to reduce inequalities between communities across our four nations", and this was echoed in James Brokenshire's Written Statement (which said that it would "tackle inequalities between communities by raising productivity, especially in those parts of our country whose economies are furthest behind"). These priorities are therefore very similar to those of the existing structural funds, but there are opportunities for them to be developed further.

2.2 Overall size of the funding pot

Because the UK is a net contributor to the EU budget, it would in theory be possible to reallocate some of the money that currently goes to the EU into the Shared Prosperity Fund with no further impact on the public purse. In practice, this is unlikely to be the case – the economic impact of Brexit may mean that there is less money to go around, and there are already several interests competing for a share of this money (for example, then-Prime Minister Theresa May pledged to fund her increase in NHS funding partly by using this 'Brexit dividend').[14]

The amount of funding that goes into the Shared Prosperity Fund will therefore be a balancing act between trying to maintain economic development in the countries and regions of the UK and trying to keep control of public spending. The decision on how to change the size of

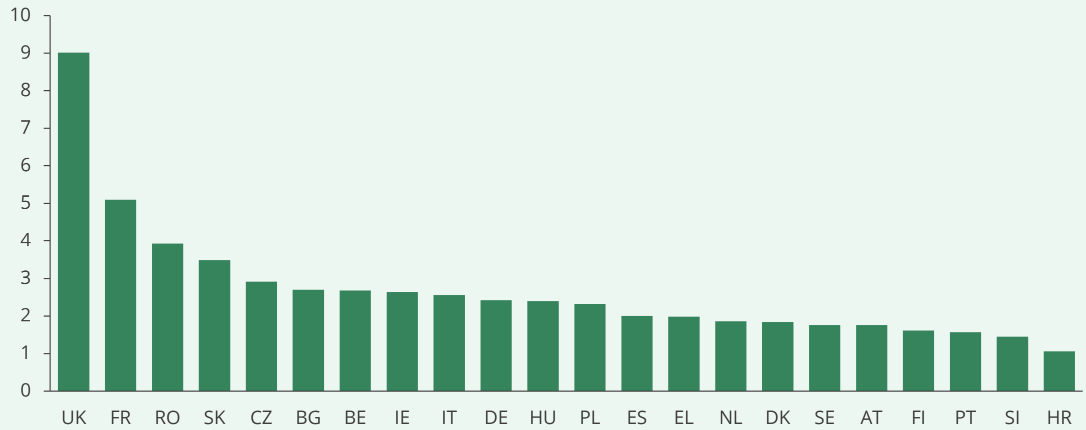
[13] PQ 240520, 8 April 2019
[14] For more details on this, please see both the Library's briefing on Brexit deal: Economic analyses and Full Fact's article Does the 'Brexit dividend' exist?

the Fund over time will be similar, and linked to the choice of how to determine the needs it is meeting (see below).

2.3 Method of allocating spending between regions

The economic development of the UK's regions is extremely varied – measured in terms of GDP per person, which is the measure the EU uses to classify regions, it is in fact the widest in the EU.

The UK has the biggest GDP/person ratio difference between regions in the EU
Ratio between highest and lowest GDP per person by NUTS2 region, 2015



Source: Eurostat, databases nama_10r_2gdp and nama_10r_3popgdp, retrieved 1 February 2019

The most developed region in the UK by this measure – West Inner London – is over nine times more developed than the least developed region, West Wales and the Valleys (although see Box 1 below for details on why this comparison may be flawed). The way in which funding is distributed will therefore be very important.

Box 1: How do we measure economic development?

The measure of economic development that the EU uses in the structural funds is GDP per person – this measures the amount of economic activity and divides it by the number of people present in the area, which should give an idea of how economically developed the region is.

However, because GDP per person looks at the economic contribution of *workers* and then divides it by the number of *residents*, it can provide a very distorted picture in areas where a large proportion of the workers in the region commute in from their homes in other regions. This is certainly the case in central London, which may explain why the UK's regional economic development appears to be so unequal.

A better alternative might be to use GDP per employee working in a particular region (a measure of productivity) or household income. Indeed, the most productive region in the UK has productivity just over twice as high as the least productive, a much lower ratio than the 9:1 for GDP per person.[15] Carefully choosing the geographical areas for comparison (to minimise the effect of commuting) can also lead to a much more useful comparison.[16]

15 Library calculations, based on ONS, *Subregional productivity: labour productivity indices by UK NUTS2 and NUTS3 subregions*, 6 February 2019

16 More information on this subject can be found in the ONS's blog post Mind the gap: why the UK might not be the most regionally unequal country, from 23 November 2018.

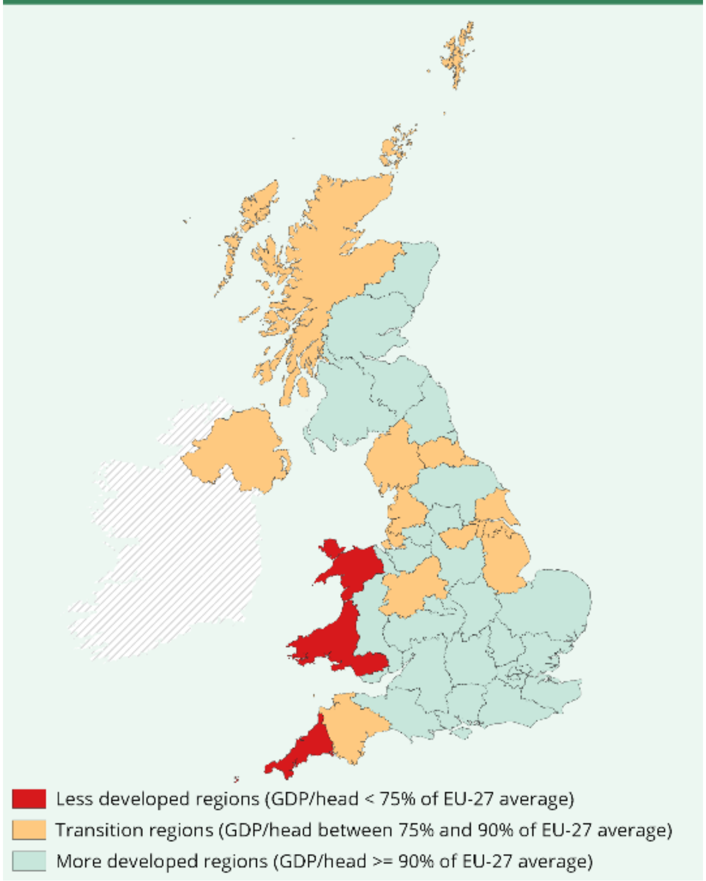
The Barnett formula

Part of the solution for distributing funding among the countries of the UK could be to use the Barnett formula, which is currently used by the Treasury to determine changes in the size of the block grants given to the devolved administrations of the UK. This takes population and the degree to which certain Government functions are devolved into account in order to scale increases or decreases in funding appropriately.

Using this formula could result in the distribution of the funding changing. If the money currently paid into the EU budget were to instead be spent directly by Westminster, this would count as an increase in funding which would then be scaled by the Barnett formula; however, because EU funding is currently higher in per-person terms in the devolved nations of the UK than it is in England, the amount these nations receive may end up lower than it currently is.[17]

In its response to an inquiry by the Scottish Parliament's Finance and Constitution Committee, two researchers from the Institute for Fiscal Studies argued that the Barnett formula would not be an appropriate way to distribute funding. This is because it does not set an initial level of funding, and can lead to funding per person in the devolved administrations converging with that of England (the so-called "Barnett squeeze").[18]

EU funding regions in the UK



Needs-based allocations

EU funding is allocated based on a classification of the sub-regions of the EU that uses their GDP per person, in order to get a rough idea of the economic development of each region (see map). Funding is then weighted towards the relatively less developed regions, of which there are two in the UK (West Wales and the Valleys, and Cornwall and the Isles of Scilly).

Funding from the Shared Prosperity Fund could therefore use a similar system, although it could use measures other than national income if they were considered more useful for identifying needs.

Box 2: Adjustments to the EU's 2014-20 funding allocation

There has been some concern about the possibility of the devolved administrations losing out when the Shared Prosperity Fund takes over from the structural funds (see chapter 3). However, there is an

[17] For more information, see the Library's briefing on The Barnett formula.
[18] Scottish Parliament, Written Evidence on Funding of EU Competences, 8 June 2018

example of the Government changing the EU's funding allocation to increase the amount that went to the devolved administrations.

Under the strict application of the EU allocation formula for 2014-2020, England would have seen an increase in funding relative to the 2007-13 round of around 9% (nominal terms), while the devolved administrations would have seen cuts of between 20% and 40%. On 26 March 2013, the Government announced that it intended to alter the balance of funding across the UK, thereby deviating from the framework set out under the EU proposals. It did this by taking money that would have gone to England, and reallocating it to the devolved administrations. In a press release, BIS stated that:

> As a result of the new EU formula for allocating Structural Funds, agreed by the European Council in February, there would not have been a fair distribution across the UK, with each of the Devolved Administrations set to lose significant funding vital for economic growth.
>
> In view of this, the UK government has decided to re-allocate EU Structural Funds to minimise the impact of sudden and significant cutbacks in Northern Ireland, Scotland and Wales. The Government will require the approval of the European Commission in order to do this.

The Government received the European Commission's approval for the reallocation, although the proposals were taken to judicial review by a group of councils, including Sheffield and Liverpool, whose areas were significantly affected by the decision. The Court upheld the Government's decision.

The reason England was set to see such a sharp rise in regional funding (despite the anticipated overall amount for the UK being set to fall by around €1bn relative to 2007-13) was due to the way transition regions were defined in the Council's 2014-20 proposals. Specifically, parts of England which in 2007-13 had only been eligible for the lowest funding intensity ('competitiveness and employment'), became 'transition regions' eligible for a higher funding intensity in 2014-20 by virtue of having per capita GDP between 75% and 90% of the EU average. That 'graduation up' in eligibility didn't happen to the same extent in the devolved regions, resulting in a sharp cut in funding there.

2.4 Match funding and additionality

All EU structural funds adhere to the principle of 'additionality', which is the concept that EU funding should not replace existing national funding but should rather supplement it. This means that the recipient country is able to do things that it could not do if it were relying only on its own resources.

The practical effect of this is that structural funds do not cover the entire cost of any given project – the proportion that they do cover is related to the needs of the region, with the remainder being made up through 'match funding' from other UK public sector organisations. As of August 2019, ERDF and ESF funding to England since 2014 had covered 52% of the total cost of the projects, with broadly similar proportions in each region (the highest was 63% in the South West, the lowest 45% in Yorkshire and the Humber).[19]

If the Shared Prosperity Fund aims to result in similar levels of investment as the ESI, then those designing the fund will need to consider the total amount of investment enabled by ESI funds, rather than just the amount provided by the EU. It would also be valuable to look at whether the existing match funding structures should be integrated with the Fund in some way.

[19] Library analysis of ERDF and ESF beneficiaries data from MHCLG, July 2019

2.5 Pre-allocation vs competitive funding

The current system of EU structural funds is pre-allocated – that is, amounts for each area are determined, and it is then up to the Managing Authorities for each area to distribute this funding to beneficiaries. However, this is not the only model available, or indeed the only one used by the EU.

Some funds outside the structural funding system, such as Horizon 2020 – where the funding goes towards research, which could potentially benefit the whole of the EU – are competitive. This means that potential beneficiaries bid directly to the European Commission to receive funding, and are in competition with other possible beneficiaries. This model has also been used in the UK for funding such as City Deals, where an individual region comes to an agreement with the Government to receive funding for a particular development plan.[20]

Competitive funding models increase flexibility because funding can be directed to any project. However, because the allocation is based on the perceived merit of an individual project rather than on general needs of areas, this could lead to less developed areas losing out on funding.

2.6 Length of the planning period

The seven-year financial framework system used by the EU means that areas have certainty over the amount of funding that they have to work with; beneficiaries of this funding also have a three-year period after the end of each framework in which to make their last funding claims and carry out administration.

However, a long period like this is less flexible (if needs suddenly change), and is also harder to guarantee in a system like the UK's where Spending Review periods have never yet been longer than four years (see box below). Any allocations of funding would therefore either have to be made over a shorter time period, or would have to be ring-fenced in some way to prevent them changing when spending priorities change.

Box 3: Spending Reviews

Around half of all public spending in the UK is planned in Spending Reviews, where the Government sets departmental spending totals for the next few years. Reviews typically take place every two to four years, and set out spending plans for the next one to four financial years. This system is intended to provide certainty in terms of the amount of money that departments know they will receive, so that they can plan for the future. The Government initially announced that there would be a Spending Review in 2019 covering three years, and that decisions on the Shared Prosperity Fund would be made as part of this process. However, the Review was then postponed to 2020, with a single-year Spending Round taking its place. The Government has not announced whether decisions on the Shared Prosperity Fund will be announced at this Spending Round.

2.7 Administration of the funds

There are several options for designing a system to make decisions about which projects should receive funding and how beneficiaries

[20] For more information, see the Library's briefing on City Deals.

should be accountable for the way their projects progress. EU structural funds work on a system in which the high level direction of the funding scheme is agreed between Managing Authorities and the EU, and the Managing Authorities then distribute the funding (albeit with oversight and accountability from the EU). The Managing Authorities in England are Government departments, but in the other countries of the UK the devolved administrations take on this role.

The Shared Prosperity Fund could therefore centralise the administration of the funds (by having Westminster take on the current roles of both the Managing Authorities and the EU), or it could choose to decentralise decision-making powers even further (perhaps to local authorities). Alternatively, it could replicate the current system by having separate funds for the different countries of the UK.

While at a hustings in Cardiff during the Conservative leadership campaign, Boris Johnson commented that there should be a "strong Conservative influence" over how the money replacing EU funds should be spent in Wales. Mark Drakeford, First Minister of Wales, later commented that this confirmed "some of the fears" he had about the plans for the administration of the Shared Prosperity Fund (see section 3.1 for more on the Welsh Government's position).[21]

One of the problems that has been raised about the existing structural funds is their complexity – indeed, an inquiry report from the Work and Pensions Committee described the European Social Fund as being "mired in inordinate bureaucracy".[22] The Government has said that one of the benefits of having the Shared Prosperity Fund is that it will be easier to administer and will reduce bureaucracy.[23]

The Government has already made some decisions on administration – one that we know of is that funding for fisheries will be handled by four separate funds replacing the European Maritime and Fisheries Fund, rather than by the Shared Prosperity Fund. This has been confirmed in the responses to PQs.[24]

2.8 Implications for state aid

Background: state aid rules

European rules on state aid limit any central or local government policies or aid measures which are bound to give selective advantage, financially or by other means, to certain businesses or sectors. The general prohibition of state aid applies to a wide range of measures, including tax incentives and direct grants for private investment and employment, provided all the other criteria of Article 107(1) of the Treaty on the Functioning of the European Union (TFEU) are satisfied. There are exemptions to the EU state aid rules which allow for certain beneficial government interventions such as the use of state aid to stimulate

[21] BBC News, Tory leadership: Boris Johnson's EU aid comments 'entirely unacceptable', 8 July 2019
[22] Work and Pensions Committee, *European Social Fund*, 4 April 2018, HC 848
[23] See, for example, James Brokenshire's response to Luciana Berger MP in a debate on the Local Government Finance Settlement, 13 December 2018.
[24] See PQ 225597 from March 2019, and PQ 263134 from June 2019.

business investment in deprived areas. As a general rule, state aid cannot be paid out unless a scheme is approved by the European Commission. However, there are many exemptions which allow smaller schemes to be set up without a prior notification in Brussels. More detailed information on the current EU state aid regime is available in the Commons Library Briefing EU State Aid rules and WTO Subsidies Agreement.

EU funding and state aid

With regard to state aid controls, EU funding is treated slightly differently than aid measures which member state authorities finance directly. European Commission's notice on the notion of state aid [2016/C 262/01] explains:

> Resources coming from the Union (for example from structural funds), from the European Investment Bank or the European Investment Fund, or from international financial institutions, such as the International Monetary Fund or the European Bank for Reconstruction and Development, are considered as State resources if national authorities have discretion as to the use of these resources (in particular the selection of beneficiaries). EU funds paid out through the managing authorities of Member States can constitute state aid. This is the case with ESIF, TEN-T funds that are combined with national resources and investments that combine EFSI with national resources. [..] By contrast, EU funds which are granted directly to undertakings without coming under the control of a public authority of a Member State cannot be considered to be state resources.

Currently, EU structural funds managed by UK authorities are subject to state aid controls.

Brexit

In preparation to leaving the EU, the government has been setting up an independent UK-wide state aid regime which would apply from the 'exit day'. The regime is intended to mirror the EU state aid rules in substance. The *EU Withdrawal Act 2018* will maintain a general prohibition of state aid. Yet, the proposed State Aid Regulations 2019 – which incorporates most of the detailed EU rules into UK law as they stand – still has to receive final approval in the Commons. If passed, it would become effective in a 'no-deal' scenario. However, if the regulations are not passed before the UK leaves the EU, the application of state aid controls will be uncertain.

SPF and state aid

The government has not provided specifics as to how state aid rules would be applied to designing the Shared Prosperity Fund. The Institute for Public Policy Research has pointed out in its report Regional Funding After Brexit (January 2019) that state aid rules might restrict the UK's options to some degree:

> For instance, under the regional aid guidelines, the UK must consider the 'common interest' of the EU in designing a new fund and cannot use the SPF to attract investment away from poorer regions of the EU. In particular, the guidelines only allow for the most ambitious regional policy in certain NUTS 2 regions (so-called Article 107(a) regions). These regions can be classified as such

only if they meet EU-wide conditions (i.e. they must have a regional GDP per head of less than 75 per cent of the EU average).

3. Opinions on the Fund's design

3.1 Devolved administrations and local governments

Welsh Government

The Welsh Government and Assembly believe that funding to Wales should not be administered from Westminster.

The Welsh Government has made clear that it is not enthusiastic about the prospect of a Shared Prosperity Fund, because of the potential impact of regional funding being directed from London. In a paper published on 14 December 2017, Mark Drakeford, then Cabinet Secretary for Finance, said:

> We will work constructively with the UK Government on aspects of economic delivery but we will firmly oppose any attempt to centralise regional development policy in London. The UK Government's "Shared Prosperity Fund" approach, if applied on a UK basis and directed from London, would be an attack on devolution, and would risk reducing needs based funding to our poorest communities.

Drakeford's language was even stronger in a more recent update to this paper, in which he said:

> We explicitly and vigorously reject any notion of a UK centralisation of regional economic development policy. A UK Government "shared prosperity fund" approach would be a direct attack on devolution and would risk depriving some of our most disadvantaged communities of the funds they need to develop economically. This would be contrary to the UK commitment that leaving the EU would not leave Wales worse off.[25]

The same paper points out that Wales's share of the UK's contribution to the EU budget is estimated to be smaller than the amount it receives from EU funding programmes; Wales is therefore particularly at risk of losing out when funding from the EU stops.

National Assembly for Wales

In September 2018, the Assembly's Finance Committee produced a report on Preparations for replacing EU funding for Wales. This report strongly recommended that the level of regional funding that Wales received should remain at least as high as the level it received from the ESI funds, and that it should be administered by Wales rather than from Westminster. The report also pointed out that the UK has in general been moving towards using challenge-based funds, in which potential recipients compete for funding, and raised concerns about whether Welsh regions could lose out under such a model.

On 6 June, the Assembly's Senedd Research service published an update on the Shared Prosperity Fund. This included Welsh First Minister Mark Drakeford's summary of the Welsh Government's position on the administration of the Fund after Brexit as "not a penny less, not a power lost" – in other words, the Welsh Government is pushing for

[25] Welsh Government, Written Statement - Reforming UK fiscal and funding arrangements after Brexit, 17 July 2018

there to be effectively no change in either the amount of money or the control that they have over its spending.

The Assembly's External Affairs and Additional Legislation Committee has started an inquiry into Proposals for a UK Shared Prosperity Fund. A number of responses to the inquiry have been received, and can be read on the Committee's website.

Local Government Association

Shortly after the 2017 election, the Local Government Association (LGA) published a discussion document called Beyond Brexit: future of funding currently sourced from the EU. This laid out several principles that the LGA felt should be considered in the design of the new Fund:

- Seizing the opportunity of making something "more flexible and responsive" than the current funding arrangements;
- Keeping the new funding "at least equal in value" to the ESI funding. This applies in monetary terms, but also by retaining the ESI funding 'additionality' principle – the idea of this is that funding should bring about results that could not have been achieved without it, rather than just topping up existing projects;
- Integration with other funding streams, in order to avoid "policy silos, duplications, gaps and inconsistencies";
- Long-term funding, retaining the seven-year period over which EU funding is currently allocated;
- Simpler financial management to make it easier to access funding;
- Space for "experimental and creative approaches";
- Bottom-up design of funding interventions, so that they are "based on local determination and local delivery";
- Accountability at the local level, with greater devolution of decision-making to the local government level.

Most organisations think that funding should remain at around the same level and be planned over long periods, in consultation with local authorities.

The LGA also considered several options for the design of the Fund, in particular suggesting that a like-for-like replacement would present a risk that "local areas are left underprepared and less able to adapt to unknown or uncertain post-Brexit scenarios in the UK."

City mayors

On 5 October 2017, the mayors of Greater Manchester, Liverpool city region and Tees Valley met with David Davis, the then Secretary of State for Exiting the EU, to discuss funding for their cities after Brexit. Andy Burnham, mayor of Greater Manchester, said that he "would like to see a 10-year commitment to funding at the current level with more flexibility about how we deploy it".[26]

[26] Financial Times, UK's northern cities lobby Brexit minister over EU funding, 5 October 2017

3.2 Other organisations

Post-Brexit Funding APPG

The All-Party Parliamentary Group on Post-Brexit Funding for Regions, Nations and Local Areas was set up in June 2018, and has produced an inquiry report about the Shared Prosperity Fund.[27] The report's conclusions are, briefly:

- The Fund's budget should be no less in real terms than the funding streams that it replaces;
- It should be administered in multi-year financial allocations "of the longest practicable duration";
- The shares of funding received by the four nations of the UK should be maintained, at least for now, and funding allocations within those nations should be a devolved matter (indeed, the report suggests splitting the Fund into four separate funds to make this clear);
- Funding within England should be almost entirely allocated based on a needs-based formula that uses up-to-date statistics;
- Narrowing the differences in prosperity across the UK should be the Fund's main objective;
- The Fund should engage closely with local authorities and local partners.

In July 2019, the APPG produced an update to this report.[28] This update argued for a total budget for the Shared Prosperity Fund of just over £4 billion per year if the Local Growth Fund was incorporated into the new Fund, and just under £1.8 billion per year if it was not. This calculation assumed that several regions of the UK would have received larger amounts of EU funding in the next EU financial framework period than they currently do.

Joseph Rowntree Foundation

In October 2018, the Joseph Rowntree Foundation (a social policy research charity focusing on poverty) published a report on Designing a Shared Prosperity Fund, which came to the following conclusions:

- The Fund should match the current level of EU structural fund spending and be planned across multiple years;
- It should be focused on 'inclusive growth' and "allocated according to the employment rate and earnings of the least well off";
- Funding should be allocated across the UK based on need rather than on the Barnett formula;
- Revenue and capital streams should both come from a single 'pot' of funding.

27 APPG on Post-Brexit Funding for Regions, Nations and Local Areas, Report of an initial inquiry into the UK Shared Prosperity Fund, November 2018

28 APPG on Post-Brexit Funding for Regions, Nations and Local Areas, A note on the financing of the UK Shared Prosperity Fund, July 2019

NCVO and ERSA

In July 2019, the national Council for Voluntary Organisations (NCVO) and Employment-Related Services Association (ERSA), umbrella bodies representing charities, sent a letter to the new Prime Minister urging him to confirm that:

- The Shared Prosperity Fund would provide support for disadvantaged groups and communities;
- Funding for employment and skills support would not fall below the level provided by the European Social Fund; and
- There would be no gap between the end of EU funding and the start of funding from the Shared Prosperity Fund.

The letter was co-signed by 100 chief executives of charities and businesses in the UK.

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