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Welsh Government

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25 November 2024

Dear Peredur,

I am pleased to enclose the Government's response to the recommendations contained in the Finance Committee's report on Fiscal Intergovernmental Relations.

Yours sincerely,

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Rydym yn croesawu derbyn gohebiaeth yn Gymraeg. Byddwn yn ateb gohebiaeth a dderbynnir yn Gymraeg yn Gymraeg ac ni fydd gohebu yn Gymraeg yn arwain at oedi.

We welcome receiving correspondence in Welsh. Any correspondence received in Welsh will be answered in Welsh and corresponding in Welsh will not lead to a delay in responding.



Finance Committee report: Fiscal Intergovernmental Relations

Welsh Government Response

25/11/2024

In October 2024, the Finance Committee submitted its report on Fiscal Intergovernmental Relations following an inquiry. The report includes 18 recommendations. This is the Welsh Government's response to those recommendations.

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1. Introduction

Since the start of this Inquiry, there has been a change in UK Government following the UK general election. This has provided an opportunity to re-set relations and begin a new era of partnership, with two governments working together on a shared vision for Wales' future. The starting point for this partnership must be rooted in intergovernmental relations founded on mutual respect and a commitment to repair and extend devolution.

The Welsh Government continues to believe that the Review of Intergovernmental Relations, agreed in January 2022, can provide the machinery needed to bring the governments of the UK together - to discuss the right things, at the right times.

The Welsh Government looks forward to working with the new UK Government and addressing together the many challenges Wales and the rest of the UK face.

With a joint focus on renewing public services, securing sustained economic growth and accelerating to net zero, through a new approach that backs Wales's green growth potential, barriers can be removed, to unlock more ambitious opportunities, creating a fairer society.

The Cabinet Secretary for Finance and Welsh Language thanks the members of the Finance Committee for their report on Fiscal Intergovernmental Relations. He has set out his response to the Report's individual recommendations below.

2. Response to the 18 recommendations

Recommendation 1

The Committee recommends that the Treasury should, as a matter of principle, differentiate between devolved governments and UK Government departments when making funding allocations and in sharing fiscal information ahead of announcements, as a way of respecting the constitutional realities of the UK that would strengthen intergovernmental relations and make processes more effective and transparent.

Response:

The recommendation is for HM Treasury.

Financial Implications: None. Able to take forward within existing resources.

Recommendation 2

The Committee recommends that the Welsh Government should press the UK Government to develop legislative proposals, in consultation with the devolved governments and parliaments, to place intergovernmental relations on a statutory basis, in accordance with the recommendation of the Independent Commission on the Constitutional Future of Wales.

Response: Accept.

The Welsh Government accepted the recommendation of the Independent Commission on the Constitutional Future of Wales, noting that statutory underpinning for intergovernmental relations would be an important step in addressing the fragility and variability of current arrangements. This is naturally a four-nation issue, which will require discussion with the Scottish Government, Northern Ireland Executive and the UK Government. As a first step, the Welsh Government will work with the new UK Government to repair and strengthen devolution and renew intergovernmental relations. The Prif Weinidog was pleased to attend the first meeting of the Council of the Nations and Regions in October, and the Welsh Government looks forward to working with partners to build new opportunities to the benefit of Wales and the whole of the United Kingdom.

Financial Implications: None. Able to take forward within existing resources.

Recommendation 3

The Committee recommends that the Cabinet Secretary pursues the following changes so that:

- the Finance Interministerial Standing Committee becomes the most appropriate platform for the Treasury to share financial information to the devolved governments, in confidence if necessary, in advance of fiscal announcements;
- the rules and processes of the Finance Interministerial Standing Committee are developed to ensure that they are sufficiently robust and to reduce the discretion currently afforded to the Chief Secretary to the Treasury in its ways of working;
- the dates of Finance Interministerial Standing Committee meetings for the year ahead are agreed with finance ministers from the devolved governments in a timely manner; and
- updates are provided to the Committee on progress in these areas.

Response: Accept.

The terms of reference¹ of the Finance: Interministerial Standing Committee (F:ISC) include 'consideration of emerging economy and finance issues and longer-term challenges that affect all governments, where collaboration and sharing of information supports planning, policy development and decision-making'. Whilst the F:ISC is the most appropriate platform for HM Treasury to share financial information to the devolved governments, in confidence, if necessary, it is not always practically possible to arrange meeting dates to coincide with when that information is available. There is however a facility to arrange exceptional meetings which has been used. Information can also be provided in a co-ordinated way on a bilateral basis.

A regular review of the F:ISC Terms of Reference is undertaken every 18 months to ensure the rules and processes are sufficiently robust. The next review is due to take place in the New Year.

The Welsh Government continues to pursue a schedule of meeting dates for the year ahead and the Cabinet Secretary for Finance and Welsh Language will raise this again when he hosts the F:ISC early next year.

As set out in the Inter-institutional relations agreement between the Welsh Government and the Senedd, the Cabinet Secretary for Finance and Welsh Language will inform the Finance Committee in advance of F:ISC meeting dates and agendas, and provide an update on discussions. As the Cabinet Secretary for Finance and Welsh Language's predecessor did last time the Terms of Reference were reviewed, he will also provide an update to inform the Committee of any changes.

Financial Implications: None. Able to take forward within existing resources.

¹ [Terms of Reference for the Finance Interministerial Standing Committee - GOV.UK](#)

Recommendation 4

The Committee recommends that the Cabinet Secretary continues to engage with the UK Government to advocate for a needs-based funding mechanism to ensure fairer funding for Wales and provides an update to the Committee on progress.

Response: Accept.

The Welsh Government has consistently made the case that resources should be allocated across the UK on the basis of relative need. As set out in 'Reforming our Union: Shared governance in the UK' (June 2021), the Welsh Government proposes that operation of the devolved resourcing arrangements, including determinations of devolved governments' spending power and borrowing limits, should be the responsibility of an independent public body accountable to all four administrations jointly. This would secure the legitimacy of the fiscal framework across the UK.

Spending power for the devolved governments should be determined, having regard to proposed levels of spending for England, by reference to a set of agreed objective indicators of relative need, so that spending power is fair across the different governments and an equivalent level and quality of public goods can be delivered in all parts of the UK.

The UK Government should not be able to arbitrarily allocate additional funding to any particular part of the UK outside these arrangements, or to create new UK-wide spending programmes in areas of devolved responsibility without the consent of the respective devolved governments.

The Barnett formula should be replaced, and a new relative needs-based system, implemented within a comprehensive and consistent fiscal framework to which all Governments in the UK agree.

Financial Implications: None. Able to take forward within existing resources. If a needs-based funding mechanism was introduced, the Welsh Government would not expect the funding Wales receives to be reduced.

Recommendation 5

The Committee recommends that the Cabinet Secretary presses the UK Government for action to ensure that:

- the dates for UK fiscal events are published well in advance to enable the Welsh Government to plan its budget more effectively; and
 - more consideration is given by the UK Government to the Senedd's budgetary timetable when planning UK fiscal events, and when making
-

announcements at short-notice outside of planned UK fiscal events; and provides an update to the Committee on progress in these areas.

Response: Accept.

While the timing of UK fiscal events is a matter for the UK Government, the Welsh Government continues to highlight the importance of providing the devolved governments with greater certainty and clarity in relation to the timing of UK fiscal events, given the impact this has for their respective budget planning and procedures – including impacting scrutiny time of their respective legislatures

The timing of such events can cause the Welsh Government challenges as seen with the UK Spring Budget (6 March 2024) which occurred the day after the Welsh Government's Final Budget was approved by the Senedd (5 March 2024).

The Welsh Government has consistently pressed the UK Government for a clearer and more predictable timetable for its fiscal events through the appropriate channels, including the FISC and bilateral meetings with the Chief Secretary to the Treasury.

In July, the Chancellor confirmed that moving forward there will be a single UK fiscal event each year and there would be a return to rolling programme of multi-year spending settlements which will provide stability for the public finances and much needed certainty for public and third sector partners in Wales going forward.

The Welsh Government will continue to use the appropriate channels to ensure HM Treasury is aware of the implications of timing of UK Fiscal events on the Welsh Government budget process.

Financial Implications: None. Able to take forward within existing resources.

Recommendation 6

The Committee recommends that the Cabinet Secretary presses the UK Government for action so that:

- the Welsh Government has greater engagement with and influence on UK Spending Reviews; and
- multi-year spending reviews are delivered as a matter of course to provide greater funding certainty to the Welsh Government at an earlier stage; and provides an update to the Committee on progress in these areas.

Response: Accept.

As outlined in the response to recommendation 5, the timing of UK Fiscal events is a matter for UK Government. One of the first steps taken by the Chancellor was

to confirm a rolling approach to future spending reviews will be adopted whereby the UK Government will review its spending plans every two years to ensure no future cliff edge for annual settlements. This will support planning of future Welsh Government budgets and of its partner organisations.

The current Spending Review is taking place in two phases. Phase 1 concluded at the UK Autumn Budget and provided the Welsh Government with its settlement for 2025-26. There has been a willingness from the new UK Government to listen and engage with the devolved governments. This has been illustrated through the earlier sharing of information and a significant increase in public spending and capital investment in the UK Budget. The UK Budget also delivered Welsh Government priorities including an investment of £25m in coal tip safety, an £80m commitment to support the work of the Tata Steel Transition Board and delivering the next stage of the Celtic Freeport.

The Welsh Government has also had early, positive engagement with UK Government on the development of a UK wide Industrial Strategy, a 10-year plan which aims to encourage growth and create jobs by providing businesses with the stability and certainty they need to invest.

The Welsh Government will continue to work with the UK Government as plans for phase 2 of the Spending Review progress. The Welsh Government is in discussions with the UK Government in relation to securing additional budget flexibilities, fair rail investment and establishing the financial framework for post-2026 replacement EU funds, including Shared Prosperity Fund and Levelling Up funding. A full review of the UK Statement of Funding Policy will also be undertaken in Phase 2 of the UK Spending Review which will conclude in late spring. The Cabinet Secretary for Finance and Welsh Language will keep the Committee informed of progress.

Financial Implications: None. Able to take forward within existing resources.

Recommendation 7

The Committee recommends that the Cabinet Secretary calls for annual and in-year Treasury funding announcements to be:

- less ad hoc; and that information impacting on Welsh Government tax and budgetary policy is shared prior to UK fiscal events on a confidential basis;
- more transparent in terms of whether they are funded with new money or through savings or reprioritisation exercises undertaken by UK Government departments to enable Barnett consequentials to be calculated; and
- provides an update to the Committee on progress in these areas.

Response: Accept.

It is important that the Welsh Government understands any changes at UK fiscal events to its budgets and reserved taxes or the equivalent taxes to its devolved taxes as early as possible, in order that it can consider the implications for its budget and the tax landscape in Wales.

The Welsh Government has consistently made the case for earlier, and more scheduled, sharing of information impacting on Welsh Government tax and budgetary policy prior to UK fiscal events. Ahead of the UK Budget the Cabinet Secretary for Finance and Welsh Language met with the Chief Secretary alongside the other UK Finance Ministers at the F:ISC on 3 October and separately in a bilateral to discuss Wales specific matters. They also held a short call on the morning of the Budget.

The Chief Secretary has confirmed he has sought to provide information on the potential changes to the Welsh Government budget at a point much earlier than has recently been the case and changes to the Welsh Government settlement have been confirmed as far as possible within the Autumn Budget.

Clarity around whether UK Government announcements are funded through new funding or through existing funding is important to enable the Welsh Government to fully understand the implications for its budget. Welsh Government officials have a good working relationship with HM Treasury officials, which enables the timely sharing of information in this respect, although the nature of the UK Budget arrangements mean that it is not always clear until later in the process whether some initiatives will be funded through new money are from within current budgets.

The Cabinet Secretary for Finance and Welsh Language will keep the Finance Committee informed of progress in these areas through the usual engagement.

Financial Implications: None. Able to take forward within existing resources.

Recommendation 8

The Committee recommends that the Cabinet Secretary takes action to ensure that the Welsh Government is engaged in the development of future Statement of Funding Policy (SoFP) documents to mitigate project categorisation issues.

Response: Accept in principle.

The Statement of Funding Policy (SoFP)² is a HM Treasury published document. The Welsh Government will continue to use the appropriate channels to encourage engagement and seek to influence the development of the policy.

² [Statement_of_Funding_Policy_addendum.pdf](#)

An addendum to the SoFP was published alongside the UK Budget on the 30 October. The addendum was a factual update reflecting changes since the last SoFP publication. Prior to the publication of this addendum there was an officials' meeting to discuss and a draft was shared in advance for devolved governments to comment.

A full review of the SoFP will take place as part of phase 2 of the Spending Review. HM Treasury has requested the Welsh Government's views, and the Welsh Government expects them to establish a working group with devolved governments shortly to take forward this work.

As outlined in recommendation 9, HM Treasury includes a comparability schedule in the Statement of Funding Policy. The Welsh Government remains in discussions with the UK Government on the issue of rail funding and investment. The Welsh Government wants to ensure a fair approach to the application of Barnett, and as part of this it would welcome a review of comparability with the Department for Transport and of the Rail Network Enhancement Pipeline process.

Financial Implications: None. Able to take forward within existing resources.

Recommendation 9

The Committee recommends that the Cabinet Secretary calls on the Treasury to publish detailed workings alongside its funding announcements to improve transparency around devolved funding and project categorisation, to ensure that such decisions are taken on the basis of clear principles and provides an update to the Committee on progress.

Response: Accept.

HM Treasury includes a breakdown of funding changes in its Block Grant Transparency document, last published in July 2023. Transparency would be improved if this document were updated in a more regular and timely fashion. HM Treasury also includes a comparability schedule in the UK Statement of Funding Policy, showing how the Barnett formula comparability factor for each UK Government department is derived. The comparability schedule was updated in the addendum to the UK Statement of Funding Policy published alongside the UK Government's October 2024 Budget.

Financial Implications: None.

Recommendation 10

The Committee recommends that the Cabinet Secretary presses the Treasury to provide credible evidence for using the Central Reserve when this results in

funding outcomes that circumvent the Barnett formula and provides an update to the Committee on progress.

Response: Accept.

The UK Statement of Funding Policy (November 2023) sets out the situation in relation to the UK Reserve in paragraphs 8.7 to 8.11. In general, claims on the UK Reserve by devolved governments are judged using the same criteria as for UK Government departments. There is no automatic application of the Barnett formula to Reserve claims by departments of the UK Government, but the Barnett formula may apply if it is judged the devolved governments face comparable pressures. As noted above, and consistent with 'Reforming our Union: Shared governance in the UK' (June 2021), it is the Welsh Government's position that the UK Government should not be able to arbitrarily allocate additional funding to any particular part of the UK outside normal arrangements.

Financial Implications: None.

Recommendation 11

The Committee recommends that the Cabinet Secretary calls on the UK Government to implement a funding guarantee similar to the Barnett guarantee introduced during the Covid pandemic to provide a degree of certainty regarding devolved funding available and provides an update to the Committee on progress.

Recommendation 12

The Committee recommends that the Cabinet Secretary continues to press the UK Government so that the Welsh Government has the ability to switch capital funding to resource and provides an update to the Committee on progress.

Recommendation 13

The Committee recommends that the Cabinet Secretary continues to press the UK Government for flexibility for the Welsh Government to manage funding increases confirmed after an autumn fiscal event across financial years and provides an update to the Committee on progress.

Grouped Response to Recommendations 11-13: Accept.

The limited budgetary flexibilities currently available to the Welsh Government constrain its ability to respond quickly to emerging needs and present several challenges, including difficulty in using large, unexpected allocations before the end of the financial year in ways which maximise value for money, and in managing unexpected cuts, leaving it dependent on decisions made by the UK Government and exposed to the impact of the timing of those decisions.

The Welsh Government is pressing the UK Government to improve its current fiscal flexibilities and, along with the other devolved governments, is seeking to develop proposals that will improve in-year budget management arrangements, including a solution similar to the COVID Guarantee when making decisions that potentially involve the allocation of substantial sums of money in-year, and full flexibility to make a capital to resource switch or carry any additional funding or reductions forward to manage in the next financial year, where funding is announced after an Autumn fiscal event

The current process for capital to resource switches does not take account of devolved governments' specific needs. There needs to be a process in place that is appropriate to meet the needs of the devolved governments and respects the roles of the devolved parliaments.

These mechanisms would not be necessary if the Welsh Government was provided with sufficient budgetary flexibilities to manage its own resources. Removing all constraints on Welsh Government budget management would allow the Welsh Government to receive its block grant each year without restrictions on carrying funds forward or drawing from previous savings. It could also mean the freedom to switch funds between capital and resource budgets.

Ensuring the devolved governments have appropriate budgetary flexibilities has been raised at recent meetings of the F:ISC meeting and is due to be discussed again at the next meeting scheduled for January. The Cabinet Secretary for Finance and Welsh Language will keep the Finance Committee informed of progress in these areas.

Financial Implications: None. Able to take forward within existing resources.

Recommendation 14

The Committee recommends that the Cabinet Secretary calls on the UK Government to extend the scope for devolved governments to raise a funding dispute, given that such disputes may only be raised if a principle of the Statement of Funding Policy has been breached and provides an update to the Committee on progress.

Response: Accept.

The joint Review of Intergovernmental Relations established structures and processes to enable meaningful engagement, and a mechanism that affirms each government's right to refer and escalate a dispute.

In reviewing the F:ISC Terms of Reference in 2023, the dispute mechanism was strengthened, clarifying the process of the appointment of an independent chair

in the event of a dispute and timescale for a Ministerial meeting, to ensure disputes are addressed in a timely manner.

The F:ISC terms of reference are due to be reviewed again in the Spring, this recommendation will be pursued as part of the review. Update on progress will be fed back to the Committee.

Financial Implications: None. Able to take forward within existing resources.

Recommendation 15

The Committee recommends that the Cabinet Secretary continues to pursue with the UK Government that a review is undertaken on the Welsh fiscal framework and that the framework should be amended in line with the Scottish fiscal framework, including:

- linking index borrowing and overall reserve limits to inflation;
- abolishing reserve draw-down limits;
- increasing capital borrowing limits; and
- that the Committee is updated on the outcome of those discussions

Response: Accept.

The UK Labour Manifesto recognised that the Welsh Fiscal Framework is out of date. The Welsh Government has long argued that resources should be allocated across the UK on the basis of relative need, as set out in Reforming the Union; however, the Welsh Government's priority in the near term is to ensure the current funding arrangements deliver for Wales.

The Prif Weinidog and the Cabinet Secretary for Finance and Welsh Language have had a series of collaborative discussions with UK Ministers, during which they pressed for UK Government agreement to update the Welsh Government borrowing and reserve limits from 2018-19 to 2024-25 prices, in line with the latest Budget GDP deflators, and to index these to inflation thereafter, with the Welsh Government annual reserve draw-down limit abolished. The Cabinet Secretary for Finance will raise these issues further in future bilateral meetings with the Chief Secretary to the Treasury.

In addition to these changes, there is also a good case for bigger increases to the annual and aggregate limits on access to capital borrowing, so they are at least in line with inflation, with the aim of providing sufficient flexibility to allow prudent budgetary management from one financial year to the next in, order to maximise the funding available to the Welsh Government.

The Cabinet Secretary for Finance and Local Government raised the wider issue of late UK Government allocations and end of year budget flexibilities alongside the Finance Ministers from Scotland and Northern Ireland at the F:ISC in Belfast

on 3 October. This will form a wider programme of work and will be considered as a substantive item at future meetings of the FISC.

Financial Implications: None. Able to take forward within existing resources.

Recommendation 16

The Committee recommends that the Cabinet Secretary pursues with the UK Government a review of the process for agreeing new devolved tax powers, as outlined in Section 116C of the Government of Wales Act 2006 (as amended) and provides an update to the Committee on progress.

Response: Accept.

The Cabinet Secretary for Finance and Welsh Language discussed the devolution of the powers to introduce a vacant land tax in Wales with the Exchequer Secretary to the Treasury (XST) when they met in September. The Cabinet Secretary for Finance and Welsh Language outlined how the Welsh Government had attempted to progress this through the agreed process, however the previous UK Government had unilaterally stalled the process indefinitely. The Cabinet Secretary for Finance and Welsh Language has since written to the XST to follow up on their discussion and to share the supporting documents in line with the agreed process in the expectation that the Welsh Government will now be able to progress this matter. The Cabinet Secretary for Finance and Welsh Language will keep the Committee updated on this with the intention of returning to the issue of the case for a review of the process once the Welsh Government is clearer on its progress with securing the devolution of powers for vacant land tax.

Financial Implications: None. Able to take forward within existing resources.

Recommendation 17

Subject to recommendation 16, if the UK Government is unwilling to review the process for agreeing new devolved tax powers, the Committee recommends that the Welsh Government utilises the dispute resolution mechanism to progress the vacant land tax, updates the Committee on any progress made, and provides an explanation if it is not pursued.

Response: Accept.

Further to the response to recommendation 16, the Cabinet Secretary for Finance and Welsh Language will keep the Committee updated on progress with securing the devolution of powers for vacant land tax and if appropriate any subsequent review of the process.

Financial Implications: None. Able to take forward within existing resources.

Recommendation 18

The Committee recommends that the Treasury improves its engagement with the finance committees of the devolved legislatures, both individually and through the Interparliamentary Finance Committee Forum, with a view of increasing formal and informal dialogue on fiscal matters relating to devolution.

Response:

The recommendation is for HM Treasury to respond.

Financial Implications: None.