

BRIEFING

III

# REGIONAL FUNDING AFTER BREXIT

OPPORTUNITIES FOR  
THE UK'S SHARED  
PROSPERITY FUND

**Kate Henry and  
Marley Morris**

February 2019



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## ABOUT THIS PAPER

This briefing aims to relieve poverty, unemployment, and disadvantage by advocating for a well-designed replacement for EU structural funding. We also seek for the new fund to advance the voluntary sector and the efficiency of public services.

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# SUMMARY

Regional inequality is a dominant feature of the UK's current economic landscape. Power and prosperity are concentrated in London and the South East, while other areas of the UK experience lower levels of output and productivity. Poverty and inequality still exist in London, but such a concentration of wealth is not found in any region outside of the capital.

The UK's forthcoming departure from the European Union brings uncertainty over the future of funding allocated to the nations and regions of the UK. EU regional policy provides significant investment in the form of European structural and investment funds (ESIF). This funding has supported many local projects and the largest amounts have been allocated to places outside of London. Numerous charities, organisations and recipients of EU structural and investment funds have highlighted the vital importance of funding designed to target regional inequalities in the UK and provide consistent and long-term support to less prosperous areas. After Brexit, the UK will need to continue to give targeted support and investment into regions with lower levels of growth and higher levels of poverty, or it risks worsening the geographical divide.

Despite the uncertainty, leaving the European Union also brings an opportunity: a chance to redesign regional funding and create sustainable and inclusive regional economies. The government has named the ESIF replacement as the 'UK Shared Prosperity Fund' (SPF) – a fund committed to tackling inequalities between communities by raising productivity in areas of the country that are 'furthest behind' (Brokenshire 2018). It intends to consult on the design of the SPF in the immediate future. If designed well, the SPF could provide a chance to tackle regional inequality and close the prosperity gap between the different nations and regions of the UK.

This briefing aims to outline three challenges facing the UK: **regional inequality; centralisation of power; and a lack of community voice**. It then provides recommendations for how the Shared Prosperity Fund could be designed effectively to tackle these problems.

## 1. TACKLING INEQUALITY IN THE UK: WHERE SHOULD THE SHARED PROSPERITY FUND GO?

Regional inequality is a persistent challenge for the UK. Viewing inequality through the lens of the 'North-South divide' is too simplistic, when areas such as Cornwall and the west of Wales also experience low levels of output in comparison to London and the South East (ONS 2018a).

European structural funding is designed to help to address these regional disparities and target areas across Europe that are less well off. The amount of ESI funds allocated is calculated using gross value added (GVA) per head, which is the value added in a region divided by the resident population of that region (ONS 2018a).

While GVA per head estimates provide an indication of the economic activity happening within regions and can shed light on inequality, the measure does not provide adequate insight into poverty or quality of life. Nor does it fully capture concepts like environmental sustainability, social cohesion or wellbeing.

When looking at other measures, such as disposable income and the Regional Human Poverty Index (RHPI), we gain a more nuanced view of the regions experiencing the highest rates of poverty. Our research shows this is particularly significant in the West Midlands, which has the lowest levels of disposable income levels and scores highest for poverty rates when using the Regional Human Poverty Index (Eurostat 2018; Dijkstra and Weziak-Bialowolska 2014). This is also significant for areas such as South Yorkshire and West Yorkshire who miss out under the current measure of GDP per head.

We therefore recommend that the Shared Prosperity Fund is distributed using a dashboard of economic well-being indicators, including measures such as GVA per head, disposable income levels, and the RHPI, to help better capture regional inequality. The process for deciding the precise methodology for distributing the funds should involve a range of stakeholders and voices, including consultations with local government, community groups, and the public. It should be periodically reviewed and consulted on to ensure that it is meeting local and regional needs.

This distribution should be made at the NUTS 2 geography (the EU population size for distributing regional funding) and be designed to be consistent with EU state aid rules, which are likely to continue to apply after Brexit. Funding should be given as a long-term investment, operating over seven-year cycles at a minimum to allow for more long-term and strategic planning. Through this approach, the Shared Prosperity Fund could be used to develop a new and innovative methodology for measuring and rectifying regional inequalities.

## **2. CENTRALISED POWER AND POLICY: THE NEED FOR GREATER DEVOLUTION**

Power, policy and fiscal control are highly centralised in the UK – this is particularly evident in England, where power is concentrated in Whitehall and Westminster. While EU structural funds are in some cases partially administered locally, much of the power over decision-making has not been fully devolved.

In order to empower local areas to control their own funds, we recommend that combined authorities (which currently cover about a quarter of the population of England) be given responsibility over their SPF budget and the power to manage contracts and evaluate projects. Combined authorities are the sensible model for this as they already have responsibility for many of the place-based elements of industrial strategy, including economic development, regeneration and local transport services.

In addition to devolving powers to local government, we argue that communities themselves should be able to shape decisions over investments in their localities and regions. Regions should therefore speak to a diverse range of local residents before developing their strategy for spending SPF funds. How this works in practice could vary depending on each region's priorities and track record of citizen involvement. For instance, some local authorities have developed a range of new approaches for ensuring that local residents participate directly in decision-making – from Poverty Truth Commissions and community research to user groups and citizens' juries. Where processes already exist, local areas could draw on existing practice; where they do not, local areas could set up and facilitate residents' panels to explore communities' priorities for how the funds should be distributed and delivered.

To ensure accountability, each regional fund should be supervised by a resident advisory panel tasked with overseeing how funds are spent. The panel would have the power to review individual complaints and make recommendations for how they should be resolved.

Finally, for the devolved administrations we recommend a different approach. Scotland, Wales and Northern Ireland may choose to adopt aspects of the above

framework, such as the involvement of residents' panels, but this should not be obligatory. ESI funds were a devolved responsibility under the bracket of economic development and therefore the delivery of the UK SPF should also be devolved.

### **3. DELIVERING AN INCLUSIVE SHARED PROSPERITY FUND**

The Shared Prosperity Fund provides an opportunity to develop an ambitious approach to regional economic development based around the idea of an 'inclusive economy'. But this requires rethinking how structural funds are managed and operated to ensure that the aim for inclusion is not simply window-dressing and secures meaningful change. Unlocking community power and promoting an inclusive economy should therefore be a key part of the design of the fund.

There are three key ways the Shared Prosperity Fund should be designed to support an 'inclusive economy' agenda. First, while some of the shared prosperity funding will need to support large-scale investments such as improving transport connections at the regional level, we recommend at least 20 per cent go directly to priority areas at the neighbourhood level such as developing social infrastructure or community spaces. Second, for this neighbourhood level funding, local areas should ensure that communities have direct control over where the funds are directed. Third, the government should encourage regions to experiment with new and innovative approaches to using the funds, such as through supporting local community wealth building and alternative models of economic governance (eg community-owned businesses and cooperatives).

As highlighted in IPPR's previous research, Brexit risks further exacerbating the UK's regional inequalities. But it also provides the UK with an opportunity to reshape its regional policy through the design of the Shared Prosperity Fund. As this report argues, the new design should be centred on empowering local communities to shape how funds are spent. Critically, however, the Shared Prosperity Fund is a relatively small amount of funding in the context of the economy as a whole; it is therefore vital that the design and management of the SPF forms only one part of regions' wider economic strategies.

# 1. INTRODUCTION

The UK's forthcoming departure from the EU has prompted a period of uncertainty over the future of funding allocations to the different nations and regions of the UK. Numerous charities, organisations and recipients of EU structural and investment funds have highlighted the importance of EU funding designed to combat regional inequalities in the UK and provide consistent and long-term support to less prosperous areas (Equality and Diversity Forum 2018).

The series of structural investments targeting regions across Europe originate from the EU's Cohesion policy in 1988 (Di Cataldo 2016). The UK received EU Structural and Investment Funds (ESIF) worth €17.2 billion in the 2014-2020 funding period (House of Commons Library 2018). Broken down annually, the two main structural funds are worth approximately £2.4 billion a year to the UK. From this, £1.2 billion comes from the EU and the rest is matched by public and private sources (Tinker 2018). These funds have helped to support a range of projects across the UK, from environmental sustainability projects; employment and youth skills training; to supporting growth in small and medium sized enterprises (European Commission 2019a).

The UK government has guaranteed funding for the European Structural and Investment Fund projects (ESIF) until 2020, regardless of the outcome of the Brexit process, but after this, the future of funding is uncertain. The UK has expressed that it would like to continue to participate in some EU programmes, but this will be subject to further negotiations and will not apply to the EU's structural funds for which UK participation will cease (HM Treasury 2018). The successor fund – outlined in the 2017 Conservative Manifesto – is the UK Shared Prosperity Fund (SPF) which will operate across the devolved nations and regions of the UK. The government has said that it will aim to ensure the SPF operates with reduced bureaucracy and be delivered in conjunction with local growth and industrial strategies (Brokenshire 2018).

Our research has found that EU funding is valued by many communities and organisations across the UK. While the end of ESIF poses a risk to organisations, the UK SPF also provides an opportunity to redesign the funds in order to more effectively tackle the UK's regional inequalities. A redesigned regional fund could pioneer a new approach to tackling geographical imbalances – one that is shaped and led by local communities and that truly delivers more inclusive and sustainable regional economies.



## 2. BACKGROUND ON EU FUNDING

### 2.1 EU FUNDING EXPLAINED

All EU member states contribute to the EU budget. Between 2010 and 2017, the UK was one of nine net contributors to the EU budget, contributing an average of €9.2 billion each year and receiving an average of €6.8 billion in funding in return (House of Commons Library 2018).

The Multi-Annual Financial Framework (MFF) is the framework for how EU funds are spent. The five headings are: smart and inclusive growth; sustainable growth: natural resource; security and citizenship; global Europe; and administration. The EU argues that the MFF provides a helpful framework for better budgeting and financial planning and enables the delivery of common policies over a longer period (House of Commons Library 2018).

EU funding is allocated to the EU member states in two different ways.

1. 76 per cent of funds are allocated to member states to manage – for instance, the European Structural and Investment funds. This is administered in partnership with regional and national authorities.
2. Directly allocated funds from the European Commission. These funds do not go to EU member states. Instead, organisations (such as small businesses, civil society organisations, research institutions) can apply directly for funding.

The ultimate political responsibility for how the EU funding is spent lies with the European Commission. However, most of the funding is managed within countries and therefore responsibility for checks and audits lies with domestic governments (ibid).

### 2.2 WHAT ARE THE DIFFERENT EU FUNDING SOURCES?

The main expenditure of the UK is allocated under the objective headings ‘smart and inclusive growth’ (42 per cent) and ‘sustainable growth: natural resources’ (54 per cent) (ibid). Two major channels are the delivery mechanisms for this funding – the European Structural and Investment (ESI) Funds and the European Agricultural Guarantee Fund. The UK has been allocated €17.2 billion and €22.5 billion respectively from these two funds for the 2014-20 funding period (ibid).

Of these two EU funding streams, the ESI funds are designed to reduce disparities in the level of development of various regions and help less developed regions to catch up. The ESI funds operate in multi-year periods in line with the current MFF.

ESI funding is broken down into five main different funds.

- The **European Regional Development Fund (ERDF)** promotes economic and social cohesion by reducing imbalances between regions. It invests in research and innovation, digital, support for small to medium sized enterprises, and the creation of a low carbon economy (European Commission 2019b).
- The **European Social Fund (ESF)** provides investment for education, vocational training, retraining and job creation schemes (European Commission 2017). It targets vulnerable groups who fall through the gaps of mainstream public

services, such as those with health conditions, disabilities or other complex barriers to employment (Gregory 2018).

- **The Cohesion Fund** supports member states that have a GDP of less than 90 per cent of the EU average – the UK therefore does not qualify for this fund (House of Commons Library 2018).
- **The European Maritime and Fisheries Fund (EMFF)** is a specific fund for the support of the fisheries sector.
- The **European Agricultural Fund for Rural Development (EAFRD)** supports rural economic development (European Commission 2019c).

In addition to these five funds, EU member states also receive funding from the Youth Employment Initiative (YEI) - which supports projects providing young people not in education, employment or training (NEETs) with employment, education, traineeships and apprenticeships (European Commission 2019d).

The bulk of UK ESI funding comes from the European Regional Development Fund (ERDF), through which it has been allocated €5.8 billion of EU funds, and the European Social Fund (ESF), with an allocation of €4.9 billion (House of Commons Library 2018).<sup>1</sup>

### 2.3 HOW ARE THE STRUCTURAL AND INVESTMENT FUNDS CALCULATED?

The EU budget determines the amount of structural funding available for each Member State. The funds for regions of each member state are calculated at the second level of the Nomenclature of Territorial Units for Statistics (NUTS). This is referred to as NUTS 2. The NUTS 2 category is essentially a way of breaking down the EU into sub-national levels at the regional level. The NUS Level 2 population generally falls within the range of 800,000 and 3 million (Scottish Government 2016). There are 41 NUTS 2 sub-regions in the UK, including five NUTS 2 regions in Scotland and two in Wales; Northern Ireland is considered to be a single NUTS 2 region (ONS 2016).

Funding is allocated using GDP per head and compared to the EU average. Depending on where the population sits the regions are categorised in three different ways.

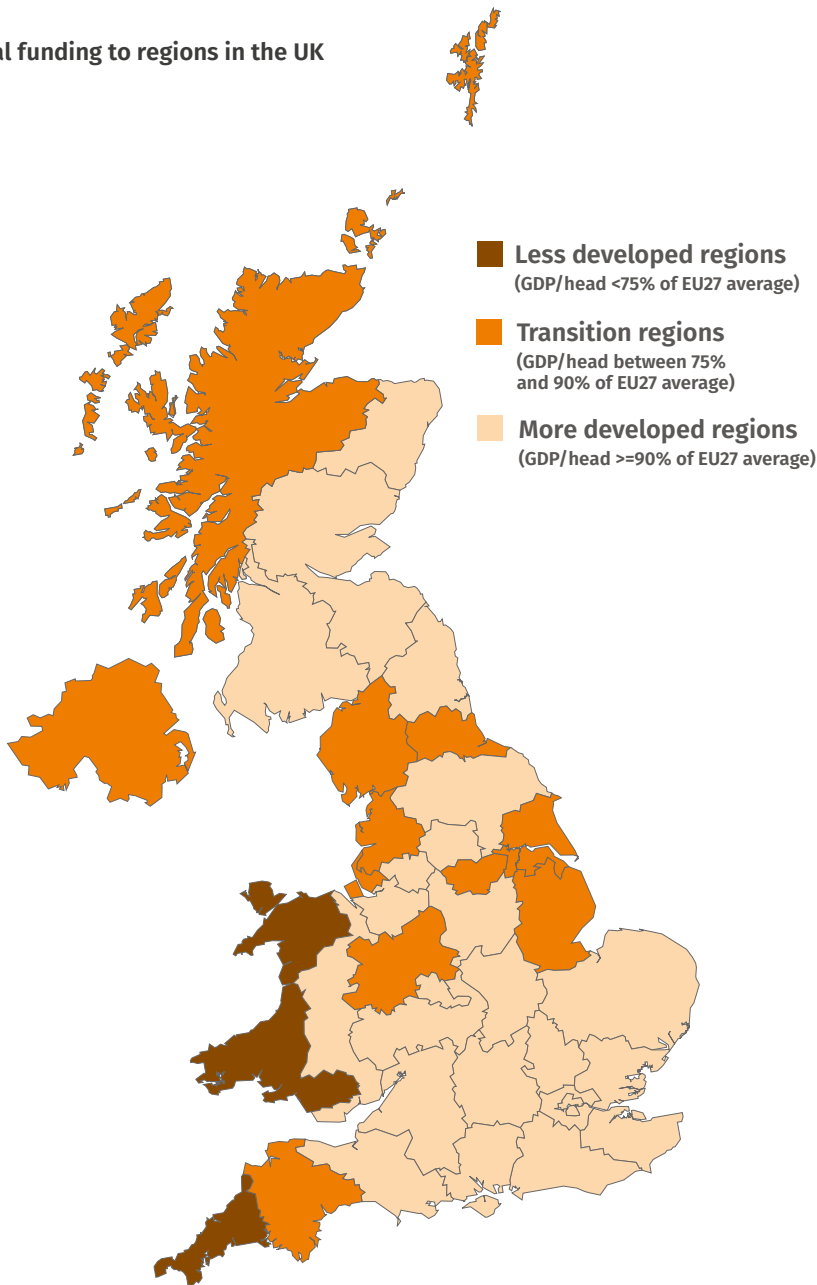
- **More developed regions** where GDP per person is above 90 per cent of the EU average.
- **Transition regions** where GDP per person is between 75 per cent and 90 per cent of the EU average.
- **Less developed regions** where GDP per person is less than 75 per cent of the EU average.

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<sup>1</sup> For funding round 2014-2020.

**FIGURE 2.1**

**EU structural funding to regions in the UK**



Source: House of Commons Library 2018

As shown in the map, the 'less developed' areas are West Wales and the Valleys and Cornwall and the Isles of Scilly (European Commission 2014a). These regions therefore receive the greatest amount per person per year in EU funding. For the 2014-20 period, in the Cornwall and the Isles of Scilly LEP, funding per person was the highest in England at €1,077 per person (House of Commons Library 2018).

For the post-2020 period, three additional areas (South Yorkshire, Tees Valley & Durham, and Lincolnshire) would have been classified as 'less developed' regions (CPMR 2019). In addition, in 2016 the Scottish government bid to change NUTS 2 boundaries to classify 'Southern Scotland' as a new NUTS 2 region, arguing this better reflected the economic reality of region (Scottish Government 2016). Under

these proposals Southern Scotland would be likely to be entitled to EU funding as a 'less developed region' in future EU funding rounds (after 2026).

ESI funds are not distributed evenly across the UK and are strongly weighted towards the 'less developed' category. On average, the UK receives €24 per person, per year from the ESF and EDRF. Broken down per person per year this equates to: €27 for England, €140 for Wales, €47 for Scotland and €57 for Northern Ireland. In the 2014–2020 period Wales received the largest share of ESF and EDRF funding (around €340 million per year), followed by the South West (around €210 million per year). The South East, on the other hand, received only an annual average of €40 million.

In 'more developed' regions, there is less flexibility on what ERDF funds can be spent on – 80 per cent of funding must be spent on at least two EU thematic concentration priority areas such as innovation and research, digital, SME support or the low carbon economy, whereas 'less developed' regions only have to commit 50 percent of their funds to these priority areas (European Commission 2014b).

## 2.4 HOW ESI FUNDS ARE ADMINISTERED

The UK government is responsible for administering the funding and setting the policy for ESI funding. The Department for Business, Energy and Industrial Strategy (BEIS) is responsible for policy on the ESF and the EDRF, and the partnership agreement with the EU. The Department for the Environment, Food and Rural Affairs (DEFRA) leads policy for EAFRD and EMFF. The devolved administrations are responsible for delivering their own ESI funds (House of Commons Library 2018).

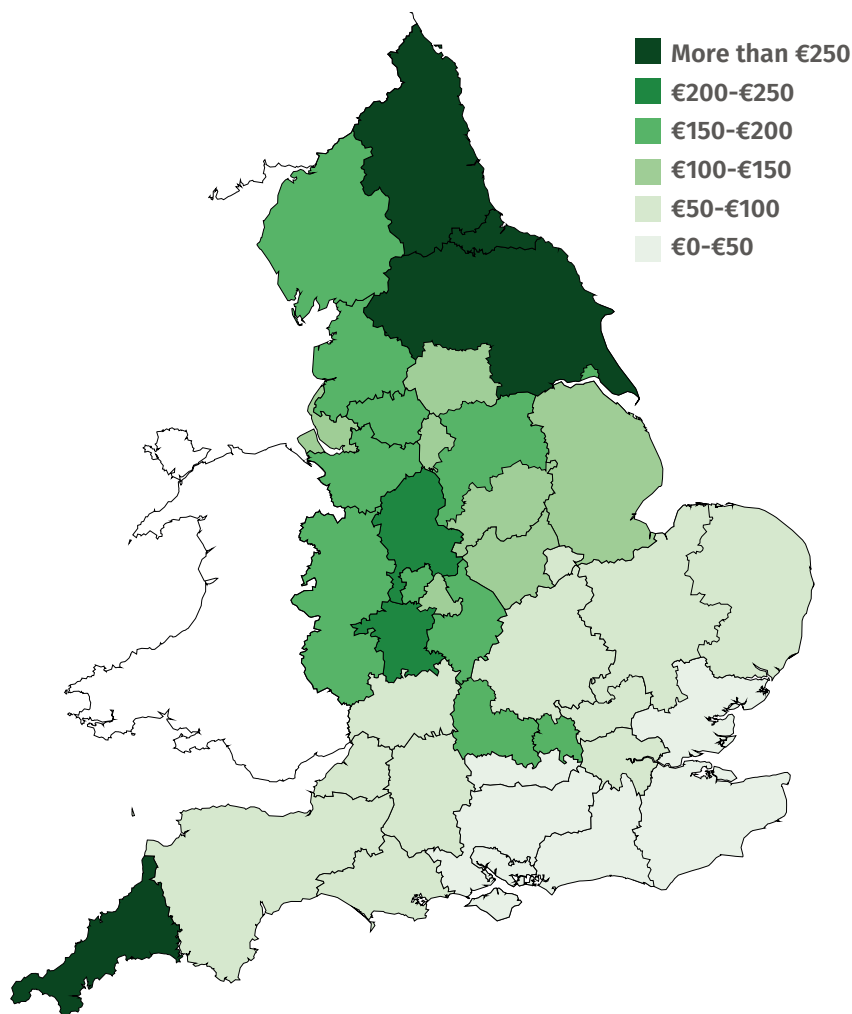
In England, the government notionally allocates ESI funds to local enterprise partnership (LEP) areas (BEIS 2015). LEPs are public-private partnerships between local businesses and local authorities and set the local priorities for achieving economic growth in their area (National Audit Office 2016). There are 39 LEPs in England, each formed around functional economic hubs. The amount allocated to LEP areas is calculated using NUTS 2 geographies and is then converted to LEP areas according to population size (see figure 2.2). If LEPs overlap, their allocations are divided equally between the relevant LEPs according to their population size (House of Commons Library 2018).

LEPs, however, do not have control of the ESI funds; they work with local partners to set out an evidence-based narrative to explain what they are seeking to achieve and provide a strategic overview (outlining spending plans, outputs and results) for how they will use the ESI funds in their area (HM Government 2014). The strategies are then approved by the government.

The Regional Development Fund and Social Fund are grouped under a specific programme called the ESIF Growth Programme. The Growth Programme Board is the Programme Monitoring Committee, the body responsible for monitoring EU investment in England for the 2014–2020 ESI funds. It has 39 local ESIF subcommittees that each represent an LEP area. These sub-committees advise on local policy and operational matters in respect of the ESI funds. The purpose of the programme board is to monitor the delivery of results and targets at a national level and provide strategic advice to the 'managing authorities' (the bodies responsible for ESIF funding). In the UK the managing authorities refer to government departments like DEFRA, MHCLG and DWP (House of Commons Library 2018).

**FIGURE 2.2**

**Map of funding allocated to LEPs during 2014–2020 funding cycle (€ per person)**



Source: House of Commons Library 2018

The map of LEP funding per person demonstrates the largest amount is in Cornwall and the Isles of Scilly, as well as the Tees Valley and North East. In contrast, the lowest amount of allocated funding per person is for the Buckinghamshire Thames Valley LEP (ibid).

EU funds require co-financing from other public or private sources, and the EU mandates that they should not be a replacement for existing national funding, but an addition to it. ESI co-financing rates are between 50 per cent and 85 per cent depending on the fund and the type of region. For example, ‘less developed’ regions can receive higher financing from the EU and therefore need to obtain a lower level of match funding (ibid). Most match funding in the UK comes from public sources. Examples of co-financing bodies for ESF include DWP, The Big Lottery Fund, Education and Skills Funding Agency, and HM Prison and Probation Service (House of Commons Library 2018).

Organisations such as non-profits, charities, further education colleges, local authorities and businesses can apply for ESI funding (ibid). These organisations can also apply for other forms of EU funding but these are not classified as ESI funds and are obtained by directly applying to the European Commission following calls for applications. Examples of other non-ESI funds include funding from Horizon 2020 and Erasmus+.

## 2.5 STRENGTHS AND WEAKNESSES OF THE ESIF

The ESI Funds are targeted funds designed to address regional inequalities. While there may be debates around the success and effectiveness of the funds, there is evidence that the absence or reduction in funds alters the growth and development of regions (Di Cataldo 2016). For instance, in 2006 South Yorkshire lost its eligibility for a higher rate of EU funding and was unable to sustain earlier gains in labour market and economic performance after its share of EU funds was reduced (ibid). As mentioned earlier, 2019 figures classify Tees Valley and Durham, Lincolnshire and South Yorkshire as ‘as less developed regions’ which helps to illustrate that the absence of sustained funding can result in regions moving backwards (CPMR 2019).

Despite their successes, the way ESI funds are allocated and delivered have been widely described by charities, local government and LEAs as ‘bureaucratic’ (Local Government Association 2018a). The EU structural funds were also criticised by politicians for being difficult to access, expensive to administer and poorly targeted (Conservative Manifesto 2017).

Overall however, evidence suggests that EU cohesion policy has had a positive impact on the creation of jobs and the promotion of economic growth in poorer UK regions (Di Cataldo 2016). Yet its positive impact is at risk when high-intensity investment ends, as can be seen in the case of South Yorkshire.

## 2.6 ESIF CASE STUDIES

The case studies below illustrate the successes of European Structural and Investment Funds between 2007 and 2018 in producing growth and supporting organisations in less productive areas of the UK.

### **Connecting remote areas to superfast broadband**

With a budget of more than €167 million, the Superfast Cornwall project was one of the largest single European investments in broadband infrastructure. The project enabled people to work from remote areas and reduced their need to travel by improving access to services (European Commission 2016).

### **Making low carbon technologies accessible in Sunderland**

This project ran between 2013-2015 as a scheme to bring renewable energy to deprived neighbourhoods in the North East of England. The low carbon pilot based in Sunderland brought solar power and biomass to hard-to-reach social housing estates, helping people to heat and power their homes. It also provided training to local SMEs to help meet the growing demand for green technologies (European Commission 2015).

### **A bridge to job opportunities and further learning in Port Talbot**

The STRIDES Alliance project received €1,802,000 in ESI funds and tackled deprivation in the Port Talbot area in Wales. The goal of the project was to attract economically inactive and/or unemployed people and provide simulated working environments to offer training on employment skills, literacy and numeracy, and work clubs (European Commission 2019e).

As the case studies illustrate, ESI funds have supported thousands of different projects across the UK, including on projects aiming to have a positive impact on regional growth, reduced unemployment, and innovation and sustainable development. The potential reduction in funding for regions after Brexit could risk affecting the performance of regions and organisations reliant on this support. It therefore needs to be ensured that the Shared Prosperity Fund fills the gap left by the absence of EU structural funds after Brexit and addresses the challenges of fiscal and political centralisation in the UK.

### 3.

## CHALLENGE 1: REGIONAL INEQUALITIES IN THE UK

The UK economy faces deep geographical imbalances (IPPR 2018). The benefits of economic growth have been disproportionately concentrated in London and the South East. But while London has the highest levels of labour productivity (ONS 2017a), it also has high rates of poverty and inequality – caused largely by the capital’s housing crisis that has resulted from its economic boom. Other regions experience different problems – regions such as the North East have not received the same intensive central government investment as the capital, and therefore have a form of poverty that results from low productivity, low pay, and relatively high unemployment (ONS 2019). The reality of the ‘North-South divide’ is that each of the UK’s nations and regions have deep, long-term problems that are related to one another, and they all need fundamental reform.

These levels of inequality within the UK contrast starkly with other G7 countries and European neighbours, and many civil society organisations have called for an ambitious long-term endowment to target areas that have missed out on economic growth (Gregory 2018). Recent research also advocates for greater emphasis on ‘place-based’ tailored interventions which are more sensitive to local socioeconomic needs and assets (Di Cataldo and Monastiriosis 2018). Many have also argued that the outcome of the referendum was in part a result of the UK’s deep regional inequalities, although the pattern is more complex than is often portrayed – ‘the North’ didn’t vote en masse for Brexit, while a majority in the East, South East and South West of England voted to leave.

#### HOW EFFECTIVE ARE ESI FUNDS AT CAPTURING INEQUALITY AND POVERTY?

Currently, the ESI funds are calculated using gross value added (GVA) per head, which measures value added divided by resident population of that region (ONS 2018a) and is used to consider differences in the economic performance of areas across the UK (The EU then translates these figures into GDP per head in order to determine funding allocations). Based on this measure, a greater amount of EU structural funds per person was allocated to Cornwall and West Wales – regions with the lowest GVA per head (see figure 2.1).

However, while GVA per head estimates provide an indication of the economic activity happening within regions, they are not an indicator of wealth and do not measure poverty in a region (ONS 2018a). GVA per head does not reveal the full picture of a region’s economy, as it is subject to distortion such as the effects of commuting (ibid). Moreover, taking the value added by people working in a region and dividing it by the number of people living there is a problematic measure because it does not account for the quality of life or poverty in the region.

In addition to this, measures such as GVA per head are limited as they do not fully capture concepts like sustainability, environment or social cohesion and wellbeing (OECD Observer 2005). Instead, they account for monetary transactions based on the production of goods and services (Costanza et al 2009). Measures looking at output or productivity do not track the destruction of natural resources, levels of human exploitation and inequality. Newer measures like Green GDP, the

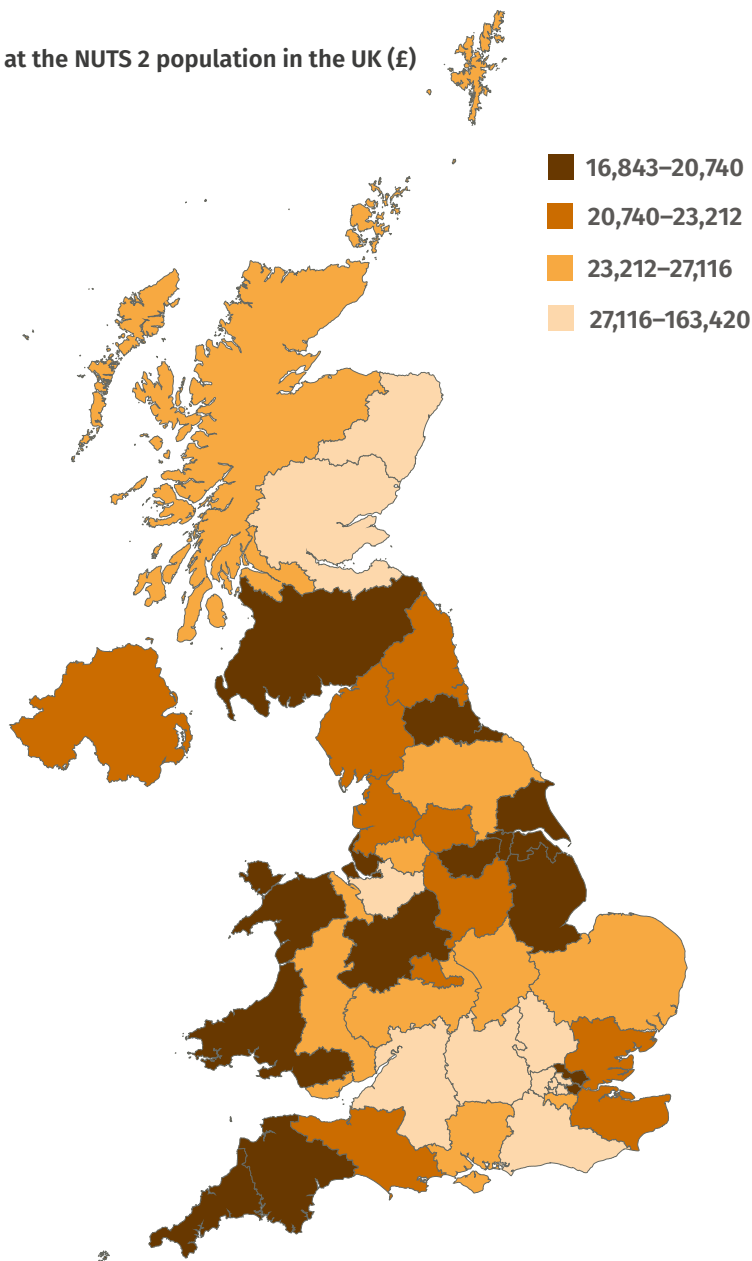


Sustainable Development Index or the Genuine Progress Indicator help to monetise environmental effects by quantifying the cost of pollution, climate change, waste and other relevant factors (Mutert 2010; Sustainable Development Index 2018).

When it comes to calculating and designing a fair and inclusive Shared Prosperity Fund, it is therefore vital to have a wider consideration of measures that better capture poverty to truly assess inequality between regions. The following maps highlight the most deprived areas (measured at NUTS 2 population size) when applying a number of different measures. (These measures are by no means exhaustive; they simply illustrate the range of measures available and the different patterns they reveal).

**FIGURE 3.1**

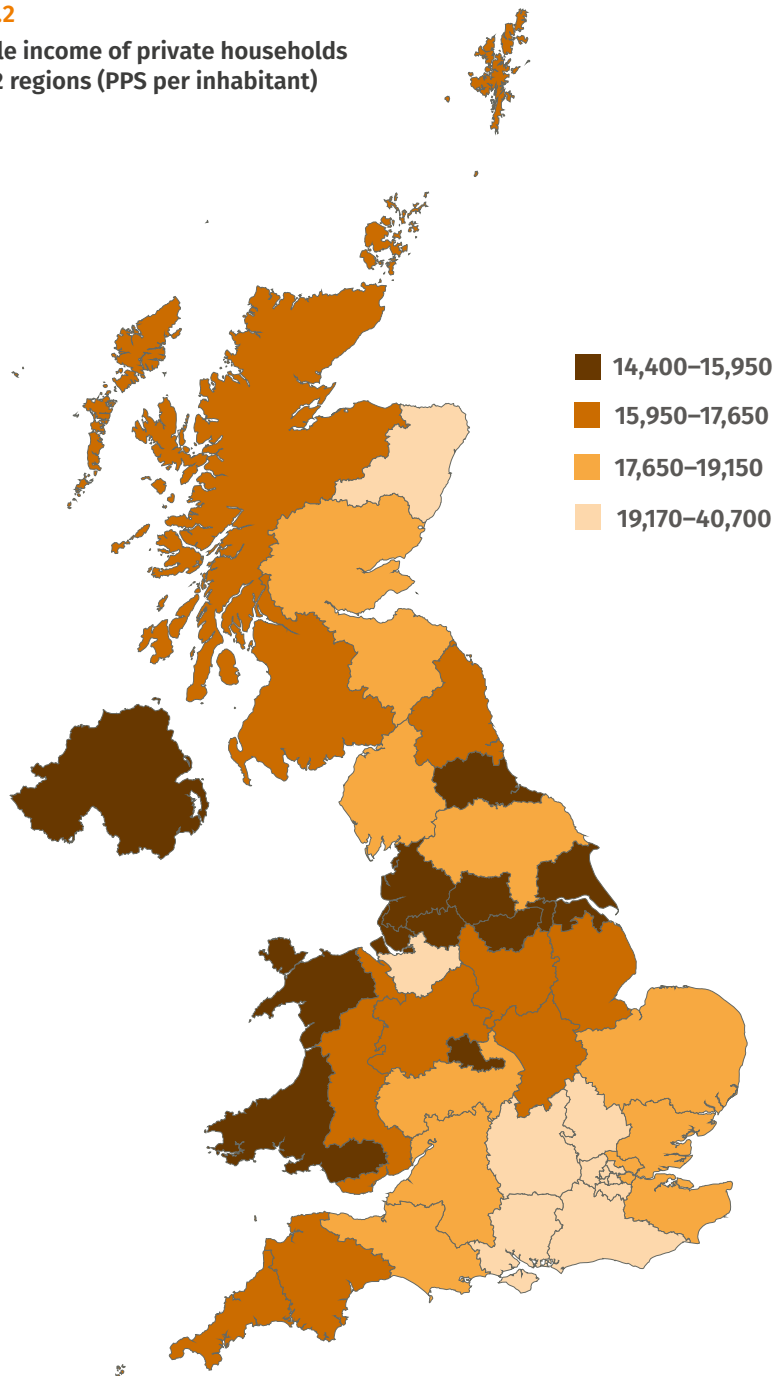
**GVA per head at the NUTS 2 population in the UK (£)**



Source: ONS 2018b

**FIGURE 3.2**

Disposable income of private households  
by NUTS 2 regions (PPS per inhabitant)

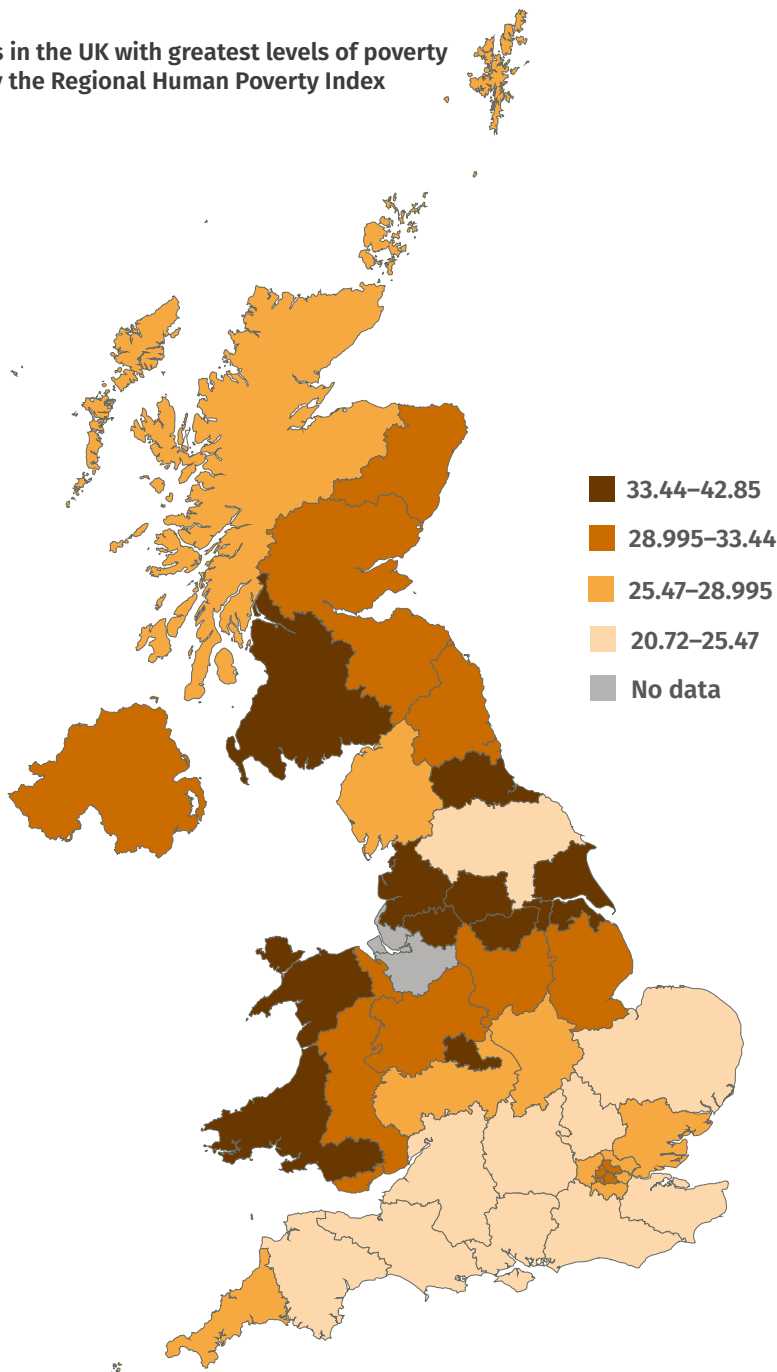


Source: Eurostat 2018

For instance, a measure based on disposable income finds that the West Midlands, South Yorkshire, and East Yorkshire and Northern Lincolnshire rank as the most in need.

**FIGURE 3.3**

**NUTS 2 areas in the UK with greatest levels of poverty measured by the Regional Human Poverty Index**



Source: Dijkstra and Weziak-Bialowolska 2014

Based on the regional human poverty index (RHPI), which combines social exclusion, knowledge, a decent standard of living, and a long and healthy life, the poorest areas are the West Midlands, Greater Manchester, and West Yorkshire (Dijkstra and Weziak-Bialowolska 2014).

As the maps illustrate, the West Midlands performs averagely when measured by GVA per head but it has higher levels of poverty according to RHPI and very low disposable incomes. This indicates that, when used alone, GVA per head is unable to fully capture regional inequality and poverty.

## STATE AID AND SPF

Under the post-Brexit future relationship, it is expected that the UK will continue to follow EU state rules. This is because one of the EU's preconditions for any trading arrangement which removes tariffs and quantitative restrictions is a 'level playing field' on state aid control. As demonstrated in the Irish protocol within the Withdrawal Agreement, this means that the UK will continue to follow EU regional aid guidelines as part of the future relationship.

To some degree, this circumscribes the UK's options in designing a new Shared Prosperity Fund. 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 (ie they must have a regional GDP per head of less than 75 per cent of the EU average).

Notwithstanding these rules, the UK will nevertheless have some flexibility in the design of the SPF and the use of alternative measures to regional GDP per capita. For instance, in designating other poor areas where regional aid can be targeted (so-called Article 107(c) areas), the EU's regional aid guidelines offer greater scope in the choice of criteria used.

## RECOMMENDATIONS FOR THE SHARED PROSPERITY FUND

Three key questions arise when considering how the SPF should be designed and allocated. The first: what is the appropriate size of geography to measure regional inequality at? The second: what type of measure should be used to calculate the funding amounts? The third: how often should funding be renewed?

First, we propose using the NUTS 2 level as the geographical measure for Shared Prosperity Fund analysis. The NUTS 2 sub-region population size is between 800,000 and 3 million (Scottish Government 2016), which broadly aligns with the combined authorities of Greater Manchester, West Midlands, Sheffield City Region, and West Yorkshire and LEP geographies (ONS 2017b). This is the most logical geography to administer funding, as it provides continuity and broadly aligns with the relevant bodies that we would expect to administer the funds (see proposal two).

Second, we recommend a new approach for distributing the SPF that is broader and more accountable than the GVA per capita approach used for European structural funds. Rather than focusing on one measure of economic wellbeing, the distribution should draw on a comprehensive dashboard of indicators, including measures such as GVA per head, disposable income levels, and the regional human poverty index. The process for deciding the precise methodology for distributing the funds should involve a range of stakeholders and voices, including consultations with local government, community groups, and the public. The final decision will also need to be tested to ensure compliance with the appropriate state aid guidelines. The methodology should be periodically reviewed and consulted on to ensure that it is meeting local and regional needs.

Third, the SPF should be given as a long-term investment, operating over seven-year cycles at a minimum, similar to the EU funding cycles. This would allow for more long-term and strategic planning.

This method would help to provide a more accurate picture of regional disparities and help to ensure that SPF funding goes to the areas that need it most. Rather than simply relying on GVA per capita as a measure of regional inequality, it would be based on a more nuanced and holistic methodology, factoring in the implications of growth for sustainability and recognising that traditional measures of growth cannot fully capture poverty, physical and mental health, or human well-being. Through this approach, the Shared Prosperity Fund could develop a new and innovative methodology for measuring and rectifying regional inequalities.

## 4.

# CHALLENGE 2: THE UK IS HIGHLY CENTRALISED

The UK has been described as one of the most centralised developed countries in the world (Global Government Forum 2015). While Scotland, Northern Ireland and Wales have obtained a greater degree of devolution, this is most economically significant in Scotland (IPPR 2018). England, on the other hand, is governed from London and, unlike other successful developed economies, has an insufficient amount of regional governance (ibid). Devolution efforts in England have lacked proper financing: the UK government is yet to fully devolve budgets or transfer powers for taxes to be levied substantially at a sub-national level. Such centralisation contrasts starkly to countries such as Canada, which raises nearly 50 per cent of taxes at the local or provincial level (ibid).

Though recent ‘deals’ have included some devolution to metro mayors, devolved decision-making is still only afforded to a few areas such as Cambridgeshire and Peterborough, Greater Manchester, Liverpool City Region, the Tees Valley, the West of England and the West Midlands (Local Government Association 2018b). These devolution deals transfer small amounts of responsibility for spending and the delivery of key areas such as: further education; business support; the Work Programme; integrated transport systems; and planning and land use, but they do not provide the combined authorities with sufficient legislative powers and financial autonomy (House of Commons Public Administration Select Committee 2017). While devolution deals represent some progress, they are nothing of the order required to rebalance the economy and ensure sufficient regional representation.

### EU FUNDING AND CENTRALISATION

The EU structural funds have been a form of consistent investment into UK regions that are at risk of falling behind. As explained in the previous section, ESI funds are delivered through local enterprise partnerships (LEPs). Whilst LEPs can advise on how ESIF funding is spent, they are unable to spend the money on behalf of the government or manage ESIF contracts. As a result, there has been criticism of the capacity and purpose of LEPs as the primary body to oversee structural funds in England. The National Audit Office has highlighted differing levels of transparency and strategic planning among LEPs (National Audit Office 2016) and they have recently undergone a governmental review (MHCLG 2018).

The delivery of ESI funds has provoked mixed responses. Many who agree that the EU Structural funds have had a positive impact in the UK also recognise that they are overly bureaucratic and still very centralised (Local Government Association 2018a). This is exacerbated by the fact that ESIF funding and policymaking is still largely controlled by Whitehall. Meanwhile, EU funding is heavily regulated and operates under strict audit conditions, which means funds can be retrieved if spent inappropriately. This centralisation of criteria has created a risk averse culture among grantees, where considerable time is spent on bureaucratic reporting procedures, preventing focus on the core project outcomes (ibid). ESIF criteria and audit checks have meant that local areas would prefer a single pot that they can spend on what is needed most in their local area. For instance, Greater Manchester Combined Authority reported challenges with the ESI funds’

narrow scope. They provided an example of a burgeoning E-retail industry in Manchester that was unable to unlock ESI funding, because potential beneficiaries of projects were classified as ‘online’ businesses - meaning they missed out on EU funding (GMCA 2018).<sup>2</sup> In many cases, a more locally-led approach with a devolved budget would mean businesses and organisations can coordinate their own strategies and priorities more effectively.

There has been some progress in allowing local areas to have more control. An example of this is the granting of ‘intermediate body’ (IB) status to some local authorities, handing them greater control over managing the funds (eg setting the criteria for EU funding applications) (Cornwall Council 2018). The Greater London Authority (GLA) has full IB status, through which it manages the London ESF Programme (Greater London Authority 2015). This IB status allows the GLA to develop calls for funding and tendering opportunities, appraise applications and sign contractually binding funding agreements, as well as carry out pre-and post-expenditure checks on projects and reclaim ESF and ERDF funds where needed (ibid). IB status does not, however, allow full control of the pot of EU funding. Limited IB status has also been granted to Cornwall Council and to the eight English core cities – Birmingham, Bristol, Leeds, Liverpool, Manchester, Newcastle, Nottingham, and Sheffield (Local Government Association 2015).

## **RECOMMENDATIONS FOR THE SHARED PROSPERITY FUND**

We echo calls for combined and local authorities to be given devolved powers, enabling them to handle the funds from the SPF, as well as manage contracts and monitor and evaluate the progress of projects. We propose that the SPF funding is administered through combined authorities, with LEPs playing an advisory role. We build on the proposals of the IPPR Commission on Economic Justice, which argues that combined authorities should be created to cover the rest of England, in both city and county regions (IPPR 2018). This should happen on an appropriate timescale according to each local area. In the short-term (following the post-2020 period when EU funding is expected to end), where combined authorities do not exist, local authorities working at a LEP geography should nominate a local authority to take on devolved SPF powers on their behalf.

Alongside powers over the management of the funds, local areas should also be able to design the priorities for the funds in coordination with their wider economic strategies. The IPPR Commission on Economic Justice highlighted the need for a new approach to industrial strategy to strengthen key sectors, diversify exports, and rebalance the economy. A core tenet of the Commission on Economic Justice’s approach was the concept of ‘new industrialisation’ – an industrial strategy aiming to foster regional clusters of industry, centred on universities and designed to stimulate research and innovation (IPPR 2018). The SPF should be designed around such local economic strategies and should enable local areas to grow and develop innovation-based industrial clusters.

But granting greater powers over the SPF for local government is only part of the devolution process. The SPF is also an opportunity for residents and communities to shape decisions over investments in their localities and regions. For each region, local and grassroots involvement should be embedded into the strategic direction of the SPF. Combined authorities should speak to a diverse range of local residents before developing their strategy for spending SPF funds. How this works in practice could vary depending on each region’s priorities and track record of citizen involvement. For instance, some local authorities have developed a range of new approaches for ensuring that local residents participate directly in decision-making and that the lived experiences of communities have a meaningful and sustained influence

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2 Interview with Alison Gordon, Greater Manchester Combined Authority, November 2018.

over how policy is made – from Poverty Truth Commissions and community research to user groups and citizens’ juries. Where processes already exist, regions could draw on existing practice; where they do not, regions could set up and facilitate residents’ panels to explore communities’ priorities for how the funds should be distributed and delivered. This approach can help empower residents, secure greater community buy-in, and provide combined authorities with a more nuanced and in-depth understanding of local problems.

This process of local engagement should not simply take place at the initial stage of strategy development; local accountability should be built in throughout the course of the SPF timeline. To facilitate accountability, each region should appoint an advisory panel, involving residents with a diverse range of lived experiences relating to the fund’s strategic priorities. The panel should meet regularly to review the progress of the SPF strategy and the management of the funds. The panel should have the power to make recommendations, which combined authorities would be expected to take account of in their delivery of their SPF programme. Each regional fund should also have a petition mechanism, in order to allow local residents and community groups to raise concerns about the fund. Where a certain threshold of petitions is reached, the advisory panel would review the complaint and make recommendations for how it should be resolved, and the combined authority would be required to issue a formal response.

Alongside the process of devolution to the combined authority level, there should be an overall set of priorities contained within a national framework. (This will work differently for the devolved administrations, as explained below). This overall set of priorities for SPF should be constructed through a programme of local and regional engagement, including a nationally representative citizens’ panel. A mixed sample of the population from different social, ethnic and age groups as well as different parts of the country should be called upon to advise the new SPF framework. The framework could include objectives such as climate change and environmental sustainability; employment and progression; poverty alleviation and social inclusion.

Finally, for the devolved administrations we recommend a different approach. The devolved administrations of Northern Ireland, Scotland and Wales should have the freedom to decide what to spend the UK SPF funds on as their constitutional right determines. They may of course choose to adopt aspects of the above framework, such as the involvement of residents’ panels, but this should not be obligatory. ESI funds were a devolved responsibility under the bracket of economic development and therefore the delivery of the UK SPF should also be devolved (House of Commons Library 2018).



## 5.

# CHALLENGE 3: DELIVERING A FAIR AND INCLUSIVE SHARED PROSPERITY FUND

The concept of ‘inclusive growth’ has dominated the debate on regional economic development in recent years. Put simply, it signifies a recognition of both the ‘pace and pattern’ of economic growth (Lee 2018). While the concept of inclusive growth has been an important development in connecting debates about local growth with parallel concerns over poverty and inequality, it has nevertheless faced considerable critique. Inclusive growth has been described as conceptually nebulous and unambitious. For some, the key flaw of inclusive growth is that it accepts the current economic system and does nothing to challenge the prevailing liberal market approach (Burch and McInroy 2018). Instead, some have called for the term ‘inclusive economy’ in order to better capture the need to rethink the principles and regulatory structures underpinning regional economies (ibid).

For example, the local wealth building movement aims to encourage wealth to be held, generated and rooted locally, meaning communities are placed first and people are provided with dignity and opportunity (CLES 2018). Organisations such as the Local Trust have advocated for a community wealth fund. The principle behind the fund is a place-based model, with long term funding, community control, national support and collaboration with other stakeholders (Gregory 2018).

The Shared Prosperity Fund provides an opportunity to develop an ambitious approach to regional economic development based around the idea of an ‘inclusive economy’. But this requires rethinking how structural funds are managed and operated to ensure that the aim for inclusion is not simply window-dressing and secures meaningful change. Unlocking community power and promoting an inclusive economy should therefore be a key part of designing the fund.

### HOW EU STRUCTURAL FUNDS SUPPORT INCLUSIVE GROWTH

ESI funds provided significant investment into projects combatting social exclusion in different regions of the UK. Recipient organisations of ESI funds have expressed fears about inadequate funding after Brexit for socially excluded groups.

ESIF funding has supported projects to improve Roma inclusion.<sup>3</sup> For instance, structural funding has supported ‘ROMA-NeT’, a transnational project across nine European cities seeking to help support the integration of Roma people (Morris 2016). Other ESI funded projects have helped ex-offenders, recovering drug abusers, ethnic minorities and recent immigrants with poor language skills - all examples of disadvantaged and vulnerable groups at risk of social exclusion (European Commission 2017).

3 It is important to note that the Roma support groups have criticised UK-led ESIF projects for not sufficiently focusing on Roma inclusion (Roma Support Group 2016).

## RECOMMENDATIONS FOR THE SHARED PROSPERITY FUND

There are three key ways the Shared Prosperity Fund should be designed to support an ‘inclusive economy’ agenda.

First, while part of the shared prosperity fund will support large-scale investments such as improving transport connections or enhancing technological infrastructure at the regional level, **a portion of the SPF should be earmarked (at least 20 per cent) to go directly to priority areas at the neighbourhood level.** This would allow specific neighbourhoods to benefit from targeted investment. For instance, funding at the neighbourhood level could go to developing social infrastructure – building shared community centres, creating green spaces or supporting other community level interventions. The amount allocated would be determined using a neighbourhood-level metric (such as community wellbeing indicators).<sup>4</sup>

Second, for this neighbourhood-level funding, **local areas should ensure that communities have direct control over where the funds are distributed.** As part of this, local areas should actively involve communities in deciding the strategy for the funds through different mechanisms for community involvement, whether this be through residents’ panels, user groups, community organisers or Poverty Truth Commissions. Evidence from the ‘Big Local approach’ shows that local talent, ambitions, skills and energy from individuals, groups and organisations are best placed to identify local needs and take action in response to them (Gregory 2018).

There are a range of opportunities for local authorities to connect with and listen to local communities more effectively. For instance, ‘The Way Ahead’ initiative in London which seeks to join up the resources of civil society organisations, independent funders and the public sector by bringing community voices together to influence local government, could be emulated in other parts of the country (The Way Ahead 2019). Strengthening community power and bringing local voices into policy choices requires a radical culture change based on trusting communities to work together to develop their own spending decisions (Locality 2018).

Third, **the government should encourage regions to experiment with innovative approaches for using the funds,** such as through supporting community wealth building and alternative models of economic governance (eg community-owned businesses and cooperatives). For instance, organisations such as Community Catalysts help to develop local community enterprises and ventures to support health and social care (Community Catalysts 2019). The aim should be to harness local anchor institutions in order to encourage funding to stay within communities and bring long-term and inclusive growth. If the SPF is targeted at these emerging forms of community-led projects, it has the power to unlock local resources and deliver lasting change in a neighbourhood.

Together, these recommendations should help to encourage local areas to develop inclusive models of regional economic development. Ultimately, given the devolution of the funds, it will be up to regions to decide their priorities and develop their economic strategies. But through developing an overarching framework and facilitating a culture of innovation and experimentation, the Shared Prosperity Fund can play a key role in helping to revitalise local economic agendas.

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<sup>4</sup> Local authorities can access data on job quality, anxiety levels, social isolation, use of green spaces and physical activity to get better insights into what really matters to their communities, instead of relying on traditional metrics such as unemployment and material deprivation.  
See: <https://whatworkswellbeing.org/product/understanding-local-needs-for-wellbeing-data/>

# CONCLUSION

This briefing has explored the challenge of regional imbalances and outlined the impact of EU structural and investment funds on the UK's different nations and regions. As highlighted in IPPR's previous research, Brexit risks further exacerbating the UK's regional inequalities. But it also provides the UK with an opportunity to reshape its regional policy through the design of the Shared Prosperity Fund.

The report makes three main sets of recommendations. First, we call for the Shared Prosperity Fund to be distributed on the basis of a wider set of measures than GDP per capita, in order to more effectively target the UK's most deprived regions and account for factors such as environmental sustainability, physical and mental health, and social well-being. Second, as part of efforts to move away from years of fiscal and political centralisation, we propose devolving the management of the SPF to the local level. Third, we argue that local communities should have direct input into how the funds are designed and delivered, and that some of the funds are directed to help foster community wealth building at the neighbourhood level.

If these recommendations are followed, then the Shared Prosperity Fund could be a key instrument for tackling regional inequalities post-Brexit and empowering local communities to shape how funds are spent in their areas. Critically, however, the Shared Prosperity Fund is a relatively small amount of funding in the context of the economy as a whole; it is therefore vital that the design and management of the SPF forms only one part of a wider agenda for regional economic development.

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