Brexit, EU Area-based Policies, and the Devolved Governments

David Bell
Stirling Management School, University of Stirling
and Centre for Constitutional Change

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Introduction

Since the EU referendum, the post-Brexit future for agricultural, regional and rural policies in the UK have been hotly debated. Few of these debates have taken account of the role of the devolved governments in relation to these policies. Although agriculture, regional and rural policy have been heavily influenced by the EU for decades, the devolved governments have played an important role in their development and administration. Repatriating the policies to the UK will pose many political and economic challenges. This paper discusses alternative futures for these policies, taking into account the potential role of the devolved governments. There is little doubt that decisions over their future will affect the relationship between the UK government in Westminster and the devolved governments in Scotland, Wales and Northern Ireland.

Clearly, the UK government is the prime actor in decisions over policy repatriation. It is about to embark on negotiations with the EU which will result in the withdrawal of the UK from these ***area-based*** policies - policies that are linked to specific locations within the UK, such as those dealing with agriculture, regional and rural issues. It will soon be negotiating trade deals with the EU and with other countries. It must decide how it will treat issues such as agricultural support in these negotiations. Agriculture is often a difficult issue in trade negotiations. Changes to agricultural tariffs and income support mechanisms will also affect the budgets of the devolved governments. They will wish to have a significant influence on the U.K.'s negotiating stance in relation to these policies, since the outcomes from trade negotiations may affect their competences.

Continuation of area-based policies along the same, or similar, lines to the present structure is not guaranteed. Some argue that existing EU regional and rural policies do not provide value for money anyway and have consistently failed to achieve their objectives, such as reducing spatial inequality or increasing national growth. If the UK government accepts such arguments and redirects funding to other priorities[1], conflict with the devolved governments is inevitable.

Even if the UK government decides to continue with area-based policies, important decisions must be made about the allocation of responsibility for their design, administration and evaluation. These will involve the UK government and the devolved governments since a significant proportion of the EU funding is already administered by the devolved governments. Conflicts around these decisions have the potential to disrupt the relationship between different levels of government within the UK.

To motivate the discussion, and to get an idea of the resources involved, we begin by considering the most recent EU budget which shows the magnitude of EU-funded, area-based policies in the UK. In the following section, we examine the choices that the UK Government and devolved governments might make once these financial flows from the EU come to a halt. The final section concludes.

[1] Some of the supporters of Brexit advocated redirecting all UK contributions to the EU (some of which cover the area-based policies) to the NHS. Unfortunately, their claim was based on the gross contribution rather than the net contribution and therefore the argument that the NHS budget could be increased by £350 million per week was fallacious.

The EU budget 2015

The U.K.'s budget with the EU for 2015 is shown in Table 1 below. Annual averages for the 2019-2020 budget round are also listed. These confirm that 2015 was a representative year during the current budget round. The UK's gross contribution to the EU in 2015 was £19.6 billion (£377 million per week). This comprised customs duties, a contribution from VAT receipts, and the largest contribution which related to the size of the UK economy (Gross National Income).

Set against these contributions, £9.2 billion was received from the EU. The largest part was the UK's rebate which was worth £4.9 billion. Area-based policies received £3.5 billion. The largest of these were payments through the Common Agricultural Policy[2] and the Agricultural Fund for Regional Development - £2.5 billion. The Structural Funds (The European Regional Development Fund and the European Social Fund) accounted for a further £1 billion. Thus, excluding the rebate, 80.9 % of the money received by the UK from the EU was allocated to area-based policies. This proportion averaged 83.6% between 2010 and 2014, implying that 2015 was not an outlier relative to recent history.

Distribution of the area-based funds is largely the responsibility of the devolved governments. For example, the Scottish Government is the "formally accredited EU Paying Agency for spending in Scotland and is responsible for all aspects of the administration of the measures"[3]. The Welsh and Northern Irish Assemblies have similar roles. The devolved governments are heavily involved in the distribution of EU funding and are understandably concerned about these roles may change after Brexit. In the next section, we discuss possible scenarios for such roles.

Table 1: U.K.'s Net Financial Position with EU Institutions (£m)

Payments	*2015*	*Average (2010-2014)*	*Receipts*	*2015*	*Average (2010-2014)*
Customs Duties	3,087	2,933	Common Agricultural Policy (Direct Payments)	2,030	2,722
VAT	2715	2,251	European Social Fund (ESF)	556	425
Gross national income	13,791	12,212	European Regional Development Fund (ERDF)	454	630
Total Contribution	19,593	17396	Agricultural Fund for Regional Development (EARDF)	461	467.2
less Rebate	-4,913	-3,479	Other	826	830
less Total Receipts	-4,327	-5,074	**Total Receipts**	4,327	5,074
gives Net Contribution	10,353	8,843			

Source: Office of National Statistics, Pink Book 2016, Table 9.9: UK Official Transactions with Institutions of the EU

[2] Some small parts of the CAP, such as payments for food marketing, capital investment and those linked to numbers of animals are in principle movable, rather than "area-based", but these do not affect the fixed budgets assigned to the devolved territories.
[3] See: http://www.gov.scot/Topics/Government/Finance/spfm/eufunding Para 9.

Issues for the UK Government and the Devolved Governments

The UK government is about to embark on a series of negotiations that are likely to involve the dismantling and/or redesign of existing area-based policies. Whether they will continue into a post-Brexit world will depend first, on whether the UK government is willing to sacrifice them as part of its negotiation strategy, and second, on whether the UK government takes the view that they are an appropriate use of scarce public resources. Obviously, these decisions will be of special interest to the devolved governments.

First consider agriculture. When it enters trade talks with other countries and trading blocs, the UK must decide whether to include agricultural tariffs and subsidies within its negotiation strategy. The first set of negotiations are likely to be between the UK and the EU. The EU is the major destination for UK agricultural exports and the main source of its agricultural imports. In 2014, 61% of UK agricultural exports were sent to the EU and 71% of agricultural imports came from the EU. Therefore, coming to an agreement over agricultural policies with the EU is a high priority.

Nevertheless, the issues surrounding such agreement are Byzantine in their complexity. For example, following Brexit the UK will be leaving a customs union which has a specific tariff schedule for agricultural products. There are also tariff rate quotas (TRQ) agreed with third countries by the EU which set differential tariff rates for imports and exports below and above agreed amounts (quotas). Normally, tariffs are set low for imports below quota and much higher once quota is exceeded. It is not clear how these might be rolled back following Brexit[4], since there is no useful precedent for the breakup of a customs union.

Given that many Brexit supporters advocate completely free trade[5], the UK government is likely to come under pressure to reduce direct payments to farmers. Cogent arguments for reducing agricultural support have been made by Deiter Helm[6]. However, adopting such a policy would mean that even if there were tariff free trade between the UK and EU, UK farmers would be at a competitive disadvantage to their EU counterparts who would continue to receive direct payments from the CAP.

The UK will receive around €27.6 billion from the EU for agricultural and rural support between 2014 and 2020 [7]. These payments cover both the Common Agricultural Policy and the Agricultural Fund for Regional Development. Table 2 below shows the shares that the component parts of the UK will receive from these funds alongside the corresponding population shares.

[4] See: http://capreform.eu/wto-dimensions-of-a-uk-brexit-and-agricultural-trade/
[5] See: http://brexitcentral.com/patrick-minford-unilateral-free-trade-far-attractive-membership-single-market/
[6] See: http://www.dieterhelm.co.uk/natural-capital/environment/agricultural-policy-after-brexit/
[7] House of Commons Library (2016) "Brexit: Impact across Policy Areas", Briefing Paper Number 07213, P55

Table 2: Agriculture Funding and Population Shares for the Component Nations of the UK

	Share of EU agricultural funding (direct aids & EAFRD[8])	Population share
England	58.9%	84%
Scotland	18.5%	8%
Wales	13.8%	5%
Northern Ireland	8.8%	3%

The English economy is much less dependent on agricultural support payments than are the Celtic nations. England's share of EU financial support is substantially lower than its population share. In contrast, Scotland, Wales, and Northern Ireland all receive more than double their population share in agricultural support payments. This reflects the larger relative size of the agriculture industry in the Celtic nations, which is largely driven by the relatively higher landmass per person (particularly in Scotland). Nevertheless, agriculture comprises only a small part of GDP in their respective economies. Even so, abandonment of agricultural support policies would have a more detrimental effect on the budgets of the Celtic nations than in England. The role of CAP payments in supporting the agriculture sector, taking Scotland as an example, is explained in the Box 1.

While CAP payments support farm incomes, the common EU tariffs on agricultural products also protect farming from international competition. Box 2 shows firstly that these tariffs can be relatively large and that they are complex: they are set at a product-by-product level. The UK will no longer have to impose these tariffs if, as expected, it leaves the EU customs union. It may agree tariffs for agricultural products with the EU. It may also seek agreement with other countries where it wishes to form trade partnerships. Failing this, it will fall back on WTO rules for agriculture, which again are complex. Various attempts to liberalise agricultural trade by the WTO have made very slow progress as evidenced by the ability of the EU to charge the very high tariffs shown in Box 2.

The tariff rate quotas pose a particular challenge. These involve importing specified quantities of agricultural products tariff free and then charging a tariff on excess imports. The quantities and rates of tariff vary by product. For example, the EU has agreed with the WTO to import 284,000 tonnes of lamb and mutton tariff free. So if the UK leaves the EU, how much of this tariff-free amount that has been agreed with the WTO should come to the UK? In practice, the UK has imported (mainly from New Zealand) a much larger share of the allowance than its population share within the EU. So should the allocation reflect past patterns of purchase, or some other consideration? These are the sorts of issues that will inevitably impede progress on coming to a trade agreement covering agriculture with the EU.

[8] The Common Agricultural Policy (CAP) comprises direct aids (e.g. the Single Farm Payment) to farmers and the European Agricultural Fund for Rural Development (EAFRD), which is intended to stimulate economic, social and environmental development in rural communities.

Box 1: Importance of CAP payments to Scottish Agriculture

This box illustrates the importance of CEP payments to Scotland's agricultural sector. Table 3 is drawn from the Scottish input output tables 2013. It contrasts the size of transactions involving the agricultural sector with those for the Scottish economy as a whole.

Table 3: Agriculture and All Industries Output in Scotland 2013

	Agriculture	All Industries
Total domestic consumption	863.2	60,922.5
Imports from rest of UK	731.0	28,476.4
Imports from rest of world	281.8	16,587.8
Total intermediate consumption at basic prices	1,876.0	105,986.7
Taxes less subsidies on products	46.5	4,575.6
Taxes less subsidies on production	-556.2	1,478.5
Compensation of employees	345.8	69,497.5
Gross operating surplus	1,352.0	51,425.7
Gross value added	1,141.6	122,401.8
Total output at basic prices	3,064.1	232,964.1

Total sales of Scotland agriculture industry in 2013 just exceeded £3 billion. Around £1 billion of these sales were imports, with three quarters of these coming from the rest of the UK and the remainder from the rest of the world. The sector paid out £863 million to suppliers, such as machinery and animal feed (total domestic consumption). It also paid £346 million in wages (compensation of employees). Profits on sales £1.35 billion (gross operating surplus). The total contribution to Gross Value Added (GVA) comprised these profits along with the wages earned by farm workers. However, profits were artificially boosted by CAP subsidies of £556 million. After deducting these, the overall contribution of agriculture to the Scottish economy is £1.1 billion, equivalent to 0.93% Scotland's total Gross Value Added[1]. Clearly Scottish agriculture is heavily dependent on CAP payments which makes up a significant proportion of its total income.

The right-hand column shows the equivalent figures for the Scottish economy as a whole. Clearly, they are of a much larger magnitude, reflecting the small size of the agricultural sector. They also show that, rather than being civilised, these other sectors jointly contribute around £1.5 billion in taxes. Finally, the share of wages in GVA is much larger outside the agriculture sector. Partly due to its high capital intensity, and partly due to its relatively low wages, compensation of employees accounts for 30% in the agriculture sector but 57% of total Scottish GVA.

Box 2: Current EU Agricultural Tariffs

Tariffs are charged on most agricultural products that enter the EU. Table XX below shows examples of such tariffs. These tariffs protect EU agricultural producers (including those in the UK) from external competition. Table 4 illustrates, some tariffs are extremely high and offer very significant protection to EU producers. As part of the Brexit negotiations, the UK and EU will have to agree tariffs for agricultural trade between the UK and EU. The UK will also have to agree agricultural tariffs (if any) when it makes trade agreements with other countries.

Note that the CETA agreement between the EU and Canada involved significant reduction in tariffs, but retention of direct payments to farmers within the EU through the CAP. This outcome was not popular which Canadian farmers. Although the Canadian farming industry is subsidised, its level of subsidy is low compared with the EU. The OECD values the support given to Canadian farmers at around 0.38% of GDP which compares with 0.7% of GDP for the EU. Therefore, Canadian farmers must compete against more heavily subsidised European farm products, but given that the population of Canada is less than 1/14th that of the EU, its bargaining position is less strong.

Table 4: Current EU Tariff Rates on a Sample of Agricultural Products

Product	Tariff Rate	Effective Ad Valorem Rate
Fresh/chilled cattle carcasses	12.8% +€176.8/100kg	84%
Frozen beef, boneless	12.8% + €303.4/100kg	87%
Milk and cream, fat content 3-6%	€21.8/100kg	74%
Seed potatoes		4.5%
Fresh/chilled lettuce		10.4%
Barley	€93/tonne	53%
Oats	€89/tonne	30%

Source: Horizon Market Intelligence (2016), "What Might Brexit Mean for UK Trade in Agricultural Products?", October

CAP subsidies provide a significant share of UK agricultural income. If the UK government could negotiate tariff free access to EU agricultural markets, but did not maintain the CAP, many agricultural businesses would founder. However, free trade discussions with other countries will almost certainly include consideration of tariffs and subsidies to agriculture. The EU has one of the most protected agricultural sectors among WTO members. If the UK wishes to do trade deals with other WTO members, then they will wish to see a reduction the protections offered to UK agriculture. The outcome will depend on the relative bargaining strength of the UK and these other countries, but it is unrealistic to assume that agreements will be reached without the UK making concessions. These may involve reductions in support for agriculture if concessions made elsewhere would provide greater benefit to the UK economy. Reducing tariffs on agricultural products and subsidies to farming will likely benefit UK consumers by reducing food prices. But it is likely to cause some significant restructuring of UK agriculture, with producers seeking to raise productivity using more intensive methods. It will likely also lead to withdrawals of marginal producers from the sector.

This will be felt particularly keenly in the devolved authorities who will strongly object to having to deal with the negative consequences of trade agreements over which they have little influence.

The Celtic nations are more dependent than England on EU agricultural support. The same is true for the Structural Funds. This is illustrated in Table 5, which gives estimates of annual CAP and Structural Fund spending for each UK nation during the 2014-2020 budget round. Northern Ireland is particularly dependent on CAP funding – receiving five times more CAP spending per head than England. Wales receives three time more CAP spending per head than England, but 6.5 times more Structural Fund spending per head. Should the UK government choose to withdraw from these area-based policies, the effects would be felt most acutely in Wales and Northern Ireland.

The Celtic nations are also more dependent on the Structural Funds than is England. Their effectiveness is open to debate. A recent review by the Department for Business Innovation and Skills argued that, in relation to the Structural Funds:

> *"at an aggregate level, both in the UK and across the EU, the evidence is inconclusive as to whether the funds have been effective in achieving their objectives. There are several compelling reasons for this, particularly in relation to the structural and cohesion funds."*[9]

The lack of compelling evidence is attributed to: (a) lack of reliable data; (b) difficulty of establishing the counterfactual; (c) measurement problems arising from distinguishing effects among the plethora of interventions occurring simultaneously; (d) relatively small scale of the funding in relation both to overall public spending and GDP; (e) differences in evaluation methodologies leading to potentially different conclusions. Analysis of the effectiveness of the Structural Funds using the Quest DSGE model, which was developed by the EU, gives negative multipliers for the UK, implying that the combination of Structural Fund spending and the UK's contribution to the EU has a negative effect on GDP.[10]

This suggests that the argument that the Structural Funds offer the best possible use of scarce public resources does not have strong empirical justification. Nevertheless, there will be strong political pressure for their retention

Table 5: Average Annual Spending on CAP and on Structural Funds (2014-2020 budget round)

	England	Northern Ireland	Scotland	Wales
CAP total spending (£m)	2,184	317	614	353
CAP spending per capita (£)	31	145	96	96
Structural Funds total spending (£m)	735	54	95	255
Structural Funds spending per capita (£)	13	30	18	83

Source: Centre for European Reform

This message is reinforced by the Centre for European Reform's estimates of the net payments to the EU by country. These add estimates of contribution by country to the spending data from Table 6. Given their higher levels of income, it is not surprising that Table 5 shows England and Scotland making net contributions to the EU, while Northern Ireland and Wales are in deficit on their EU accounts. The bulk of the net payment to the EU is made by England (£8bn), while Scotland

[9] Source: Department for Business Innovation and Skills (2014), 'Review of the Balance of Competences between the United Kingdom and the European Union: Cohesion Policy', para 3.18

[10] Varga, J., & in't Veld, J. (2011). A model-based analysis of the impact of Cohesion Policy expenditure 2000–06: Simulations with the QUEST III endogenous R&D model. Economic Modelling, 28(1), 647-663.

contributes £337m per year. In contrast, Northern Ireland receives £171m, while Wales, which voted to leave the EU, receives an average payment of £276m per year.

Table 6: Average Annual Net Payments by Country to the EU (2014-2020 budget round)

	UK	England	Northern Ireland	Scotland	Wales
Gross Payments (£m)	16,907	14,582	340	1,417	567
Less UK Rebate (£m)	-3,844	-3,271	-102	-299	-172
Net Contribution (£m)	7,985	8,094	-171	337	-276
Net Contribution Per Capita	117	140	-94	64	-90

Source: Centre for European Reform

Clearly UK Government decisions affecting the CAP and the Structural Funds will have significant effects on the devolved governments' budgets. It is possible that the UK government will reduce, or eliminate, agricultural subsidies during trade negotiations. It may do so if it feels that losses in this sector would be compensated by larger gains for other industries. However, closing these sources of funding would be hugely unpopular with the devolved administrations. It would also be problematic because some programs are jointly funded by the EU and the devolved administrations. For example, the Scottish Rural Development Programme is funded jointly by the EU and the Scottish Government.

However, if the UK stopped its contribution to the EU in 2017-18, it could significantly reduce its fiscal deficit. The OBR forecast for the 2017-18 budget deficit is £59bn. The 2017-18 deficit would be reduced by £8 billion if the UK was no longer contributing to the EU budget. Hence, one option for the UK government would be simply to close EU-funded area-based policies following Brexit and use the money saved to reduce the fiscal deficit.

The strategy of reducing financial support for agriculture would be politically unpopular, both with the farming lobby and the devolved governments, but it is also somewhat at odds with the current UK government's political concern for reducing spatial inequalities across the UK. Also, the present Chancellor is less wedded than his predecessor to achieving budget balance. Hence the political desire to continue with such area-based payments, even if the supporting evidence for their efficacy is weak, may outweigh the desire for both fiscal discipline and the efficient use of public funds.

If it decides to continue with some form of area-based funding, the UK government will face a set of issues in deciding how large these funds should be and how they should be allocated and monitored. At present, the allocation of the EU Structural Funds is based on a set of objective rules which define "less developed" regions - those with incomes below 75% of the EU average, "transition" regions - those with incomes between 75% and 90% of the EU average and "more developed" regions - those with incomes greater than 90% of the EU average. The size of such regions within member states determines the overall value of Structural Funds allocated by the EU to that state.

For agriculture, allocations to member states are largely influenced by historical precedent and negotiations that involved the new member states when they acceded to the EU [11]. There are no objective criteria which can be used to justify current levels of CAP support provided to the UK.

Member states can devolve CAP implementation to subnational governments. Thus, England, Scotland, Wales and Northern Ireland have implemented quite different versions of the CAP.

[11] See: http://capreform.eu/agreeing-the-allocation-of-cap-funds-between-member-states/

Scotland and Wales have adopted similar methods for determining CAP payments; Northern Ireland is using a different method, while England has applied yet another approach. This diversity is permissible within current EU CAP regulations.

The allocation of CAP funding within the UK to the devolved governments is determined by negotiation. The outcome is largely driven by historical precedent rather than by objective analysis of farming conditions in the UK nations. Thus, for the 2014-2020 budget round:

> *"The UK government has announced that farmers in England, Northern Ireland, Wales and Scotland will receive the same proportion of the €27.6 billion Common Agricultural Policy (CAP) budget over the next seven years as they currently receive."*[12]

Giving each of the devolved governments the same share of the budget as they received in the previous round is simply taking the line of least resistance. This somewhat arbitrary process for determining the funds allocated to the devolved governments does not seem consistent with a process designed to achieve desired social and economic outcomes at minimum cost to the taxpayer.

If area-based policies continue post-Brexit, how should funding be allocated to the devolved governments? We consider three possible solutions:

1. Use the Barnett formula. Additional funding to cover agriculture, regional development and rural policy would be added to each devolved government's budget. The Barnett formula remains the mainstay of financial support for the devolved governments following the transfer of tax-raising powers to Scotland, Wales and Northern Ireland. Additions to the Barnett-determined block grant to take account of these policies would be relatively straightforward once the total cost of these policies is determined.

   Like existing UK area-based policy interventions, the Barnett formula is not based on objective statistical criteria, such as measures of relative need - an argument made by the Welsh Assembly[13] which feels that the formula fails to take account of levels of deprivation and poverty in Wales. However, its operation has become more transparent. HM Treasury now provides the information on which the Barnett formula block grant is calculated[14]. Nevertheless, HM Treasury still retains control over its design and implementation. Thus, as far as the UK government is concerned, using the Barnett formula to allocating funding for area-based policies would be relatively simple to administer. As indicated earlier, the cost of adopting this mechanism for allocating funding to the devolved governments may be outcomes that do not necessarily constitute optimal use of public funds.

   One potential danger for the devolved governments of "Barnettising" agriculture and regional spending is that if these programmes are cut back in England by the UK government, then the devolved governments will come under pressure to follow suit. Although the devolved governments can spend their Barnett block grant as they wish, failure to follow changes in spending priorities in England will require reducing funding to other spending priorities. The political costs to the devolved governments of reducing spending to

[12] See: https://www.gov.uk/government/news/uk-cap-allocations-announced

[13] See: http://www.assembly.wales/NAfW%20Documents/ki-004.pdf%20-%2002112011/ki-004-English.pdf

[14] See: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/479717/statement_of_funding_2015_print.pdf

match cuts being imposed by the UK government are likely to be less than those incurred by cutting elsewhere in order to maintain spending on agriculture and regional programmes. The latter course of action is likely to be more contested than a spending cut which can use similar action in England as a frame of reference.

2. Base allocations on relevant objective statistical measures. For example, support for infrastructure, SMEs and skills development, currently funded through the ERDF and ESF, could be replaced by a UK fund distributed to the devolved governments using objective criteria agreed by the four constituent nations. Similarly, objective measures might be used to allocate funding to agriculture. However, in both cases to avoid claims of political manipulation, the statistical criteria should be objective and transparent.

   Eligibility criteria for domestic UK government area-based policies do not seem to rely on objective statistical criteria. Recent policy measures include "City Deals", "Devolution Deals" and "Enterprise Zones". Eligibility for these policies depends on dialogue between different levels of government rather than on objective statistical criteria. This is a clear contrast with EU Structural Fund policies where, for example, the highest levels of support are restricted to those areas where GDP per head is less than 75% of the EU average. One obvious danger of distancing area-based policies from objective statistical measures is that they become exposed to political manipulation. Regions may seek to influence outcomes in their own interest when there is no clear mechanism for ranking eligibility for policy intervention.

   This approach might achieve better economic and social outcomes for the UK as a whole than use of the Barnett formula. However, given that it is central to the hybrid tax/grant funding mechanism recently implemented for the devolved governments, those governments which are disadvantaged by this method will complain that it is inconsistent with this new funding structure which has retained the Barnett formula as an essential element in devolved government funding. Further objections may be raised if the UK government decides unilaterally to retain control over the allocations. Even if the mechanism is objective, the devolved governments will argue that they should be consulted about the outcomes.

3. Agree the aggregate level of support for area-based policies and then transfer an equivalent amount of tax revenues to the devolved governments. This would provide the devolved governments with a greater degree of autonomy, but would also transfer revenue risk to these bodies. Thus, for example, rather than provide equivalent funding for the CAP and the Structural Funds to the Scottish government, the UK government might transfer the same value of excise duties. This would transfer responsibility for decisions on agricultural support and economic development to the devolved governments. While this increase in autonomy might be welcomed, the devolved governments would also have to accept additional the revenue risk associated with whatever instrument is used to fund the policy. In addition, the budgets would not be ring fenced and hence open to competition with other devolved government priorities.

However, it is worth reiterating that, specifically in relation to agriculture, the autonomy of devolved governments may be curtailed by decisions made by the UK government in its trade negotiations. For example, the devolved governments could not set up their own version of the CAP if the UK government has agreed to open up UK agriculture to competition by removing tariffs and eliminating farming subsidies. It might choose to do so in order to gain concessions for industries deemed to be more important to the UK's economic prospects. Even if the policy results only in reductions in tariffs, farm incomes are likely will suffer, possibly resulting in increased pressure on devolved governments for compensation.

These alternative mechanisms for the future of area-based funding are summarised in Table 7 below.

Table 7: Alternative Mechanisms for Implementing Area-based Policies Post-Brexit

Policy Action	**UK government**		**Devolved governments**
	For	Against	
Close down EU area-based policies	Limited evidence that policies achieve social and economic objectives	Redistribution to poorer areas may increase social cohesion	Reduction in budget and policy autonomy likely to be very unpopular
Retain area-based policies: allocate on the basis of objective measures	Transparency increases support for policy. Resources ring-fenced to policy objectives.	May not be most efficient use of public resources	Restriction on autonomy may be resented. Losers regret may be a potent political instrument.
Retain area-based policies: allocate using the Barnett formula	Reasonably transparent allocation. No need to micro-manage policy.	Likely to be even less efficient use of public resources	Greater freedom to design local policies, but funding dependent on UK fiscal stance
Retain area-based policies: assign equivalent tax revenues to the devolved administrations	Transfers risk to the devolved administrations. No need to micromanage.	Reduces fiscal flexibility by narrowing UK government tax base	Increased revenue risk, but greater freedom to design policy

(These are not necessarily exhaustive, but do give an idea of the range of UK government reactions to its withdrawal from EU area-based policies)

Conclusion

This paper has examined potential futures for repatriating EU area-based policies to the UK. These comprise policies affecting agriculture, regional and rural development. They are largely administered, and to some extent designed, by the devolved governments, whose budgets are more dependent on these policies than is the case in England.

Decisions about the future of these policies will partly be dependent on future UK trade negotiations. Agriculture is particularly exposed to such effects. Currently, UK agriculture is highly dependent on subsidy from the CAP. It will only remain competitive with the EU, its main trading partner, if it retains a similar level of subsidy to the CAP and has tariff free access to European markets. However, comprehensive trade negotiations with other countries will inevitably consider tariffs and subsidies relating to agricultural products. Objections will almost certainly be raised to the retention of CAP-like subsidies and the UK negotiators must consider whether to sacrifice these to gain concessions for other, more important, industries. Trade negotiations inevitably involve give-and-take: it is unrealistic to assume that the UK will get everything it wants. And agriculture is in a particularly exposed position in that it is currently protected by sizeable tariffs and an extensive subsidy regime. Reduction in barriers to agricultural imports will likely benefit UK consumers through lower food prices, but it is difficult to see how UK agricultural producers can remain competitive both with the EU and other countries without significant restructuring. This is likely to be strongly opposed both by the powerful agriculture industry lobby groups and by the devolved governments, which are more dependent on the existing system of agricultural subsidies than is the case in England.

As far as the Structural Funds are concerned, there will undoubtedly be strong support for their continuation, particularly from those with a vested interest in these policies. This would involve establishing UK-branded versions of the ESF and ERDF. These are in principle affordable because UK contributions to the EU easily cover their costs. However, given that UK fiscal policy is likely to continue to be tight, the effectiveness of such spending will come under close scrutiny. Some will argue that these policies are an inefficient use of public funds because they are not effective in achieving their objectives. Again, this argument will involve the devolved governments who currently administer these funds. They are likely to resist discontinuing the ESF and ERDF, again raising the potential for conflict with the UK government.

If some aspects of the area-based policies are retained, important decision will have to be made about their structure and administration. Possibilities discussed in the paper include following the EU practice of defining eligibility at the UK level using objective statistical measures; allocating additional funding through the Barnett formula and letting the devolved governments deal with the area-based policies; allowing devolved governments to access additional revenue streams to fund the area-based policies. Each approach has advantages and disadvantages both from a UK government perspective and from the perspectives of the devolved governments. There will be many opportunities for intergovernmental conflict as the debates on their design evolve. And while the objective of achieving the best use of public funds should not be set aside, the potential political costs of inflexibility during intergovernmental negotiations to establish post-Brexit agricultural, regional and rural policies should not be underestimated.