

# Finance and Public Administration Committee

## Medium Term Financial Strategy Review

### Correspondence from the Convener to the Cabinet Secretary for Finance and the Economy of 23 February 2022

Dear Cabinet Secretary

#### Medium Term Financial Strategy: content review

This letter sets out the Committee's findings and recommendations arising from our review of the content of the Scottish Government's Medium-Term Financial Strategy (MTFS).

As you know, introduction of an MTFS as a "means of focussing on the longer-term sustainability of Scotland's public finances" was a recommendation of the Budget Process Review Group (BPRG) in 2017. To be published annually following the UK Spring Statement and at least four weeks before summer recess, the document was intended to be a key aspect of the Parliament's all-year budget process.

The Committee's work in this area is in response to the Legacy Expert Panel's report to our predecessor Committee that a review of the content of the MTFS should take place early in the new session. It echoes the BPRG's recommendation, repeated in the Budget Process Session 6 Agreement between the Committee and the Scottish Government, that the content of the MTFS should be kept under review as it develops over time.

We recognise that the fourth MTFS published in December 2021 did not fall within the cycle anticipated by the BPRG. That said, it provided an opportunity for the Committee to seek views to inform the content of the next MTFS, which is to be published in May/June 2022 for the first time alongside, and to be informed by, a resource spending review. In our focussed review, the Committee explored with committees and experts whether the MTFS:

- meets the intended BPRG objectives,
- contains the elements envisaged by the BPRG, and
- provides committees with a hook for scrutiny of the medium-term priorities for, and risks to, the Budget.

#### Evidence gathered

Given the focussed nature of this work and publication of the MTFS coming alongside both the Scottish Budget 2022-23 and a Framework for a Resource

Spending Review in early December, responses to our targeted call for views were limited. We received five substantive responses: four from committees and one from the Auditor General for Scotland (AGS). We heard informally from seven other committees that they had not undertaken any scrutiny of the December 2021 MTFS, in part due to time constraints and, for some, the challenges in using the MTFS to inform scrutiny of specific portfolios areas.

We note that not all four iterations of the MTFS to date have fallen within the intended budget scrutiny cycle, due to the timing of UK and Scottish budgets in the intervening years, the lack of multi-year spending reviews, and parliamentary elections. This, the Committee accepts, has led to some challenges in embedding the MTFS as a key aspect of the budget process. Indeed, the Education Committee suggested in its response to this Committee that it would not be able to assess the adequacy of the MTFS until publication of the fifth iteration in May/June 2022, within the context of the resource spending review to be published around the same time.

The BPRG envisioned that the Committee should conduct a review of the budget process later this session, following the Fiscal Framework Review, and it is the Committee's intention to include a more in-depth examination of the MTFS as part of that work. In the meantime, we set out here a small number of specific recommendations that we consider would enhance the level of information provided in the MTFS and better support parliamentary scrutiny, for inclusion in the next iteration in May/June 2022.

As a starting point for our review, we revisited the BPRG recommendations, which stated that the MTFS should set out the Scottish Government's expectations and broad financial plans and projections for at least the next five years. We note that the MTFS is intended to capture an overview of existing policies, so these can be understood in formulating detailed budget proposals later in the budget cycle. It further aims to enable parliamentary committees to consider the overall fiscal context and financial implications of existing government policies over a five year-period. While anticipating that the MTFS would evolve over time, the BPRG recommended that the Scottish Government should work towards it including the following four elements

- forecast revenue and demand-led expenditure estimates from SFC and their effect on Scotland's public finances,
- broad financial plans for the next five years
- clear policies and principles for using, managing and controlling the new financial powers, and
- scenario plans, based on economic forecasts and financial information in order to assess the potential impact of different scenarios on the budget.

The BPRG states that "where the Scottish Government makes a policy announcement that has significant financial consequences, the anticipated implications of this for the MTFS could also be set out for each year of the MTFS" and that it should also include an "overall assessment of long-term sustainability of existing policy".

On the basis of submissions received, this letter highlights two main areas where further improvement is needed. Firstly, we heard that the MTFs does not provide sufficient focus on how significant policy decisions are to be resourced over the period of the MTFs, which limits the ability of committees to use the document to examine the implications for their portfolio areas over a number of years.

The Health and Sport Committee explained that the first MTFs in May 2018 “had some (limited) portfolio detail”, but “unfortunately subsequent MTFs publications have lacked the level of portfolio detail needed to provide meaningful context for pre-budget scrutiny”. It suggested that, “if future MTFs publications were better aligned to this intention ... , the Committee would find them an extremely useful tool that would be of great assistance to its pre-budget scrutiny”. More specifically, the Local Government, Housing and Planning Committee highlighted the importance of having projections for local government funding over five years, including how shared priorities of national and local government would be supported on a long-term basis and the implications for local authorities and the third sector.

This issue was also highlighted by the AGS, who added that, “in setting out spending plans more clearly, there is a need to link these to overall aims, including the three core priorities of child poverty, climate change, and a stronger, fairer, greener economy. This, he argued, would “better help Parliament and the public to properly understand the implications of fiscal issues for public services, the government’s priorities and expected outcomes from public spending”.

Secondly, there needs to be a more consistent approach to inclusion in the MTFs of evidence that supports the Scottish Government’s conclusions regarding fiscal risks and the overall funding position. We heard for example that detailing the way in which figures for tax revenues, the block grant and other funding streams aggregate to the overall funding position and including a definitive single statement of relevant tax and spending policies in the MTFs, would support more effective Parliamentary scrutiny.

The AGS told the Committee that “the impression given is of selective presentation of the underlying analysis”, which he argued has hampered the ability to identify how the various components build up to the overall picture. While the MTFs includes three high-level scenarios for spending, it states that “there is no reason to believe the three optimistic assumptions used to generate the upside funding scenario will necessarily occur together”. The central scenario is considered most likely but, as the AGS notes, “beyond that there is limited assessment of the likelihood of different scenarios or the confidence levels that actual experience will be within the envelope set out”.

A number of respondents further highlighted the lack of detail on how the Scottish Government plans to respond to the risks identified in the MTFs. The Social Justice and Social Security Committee for example indicated that “although the MTFs lists the broad fiscal risks and general mitigation

approach, it does not set out any further detail on the risks and provide specific actions it will take to mitigate the risk”, a point echoed by the AGS.

## Conclusions

The Committee believes that, in providing a medium-term perspective on Scotland’s public finances, the inclusion of a Medium-Term Financial Strategy, which looks five years ahead, is a helpful addition to the all-year budget process.

In our view, the four elements identified by the Budget Process Review Group to be contained in the MTFS remain as relevant today as back in 2017 when the BPRG reported. We recommend that the Scottish Government places a renewed emphasis on ensuring that these four elements form the basis of, and are properly reflected in, the fifth iteration of the MTFS to be published in May/June 2022.

As we were told in evidence, a lack of portfolio detail, and on this occasion, limited time, has hampered committee scrutiny. We recognise that timing issues along with workload pressures will always be a factor impacting committees’ ability to become involved in the budget process.

However, we cannot help but conclude that the MTFS in its current form does not sufficiently encourage or support meaningful committee scrutiny, in the way originally intended. We further believe that more detailed information is needed to build up an overall picture of Scotland’s medium-term public finances.

We therefore recommend the following improvements to the MTFS:

- Key information should be presented in a consistent way from year-to-year to enable changes to be identified and tracked, provide transparency, support effective parliamentary scrutiny, and promote public understanding.
- A more comprehensive set of tables is needed in the annexes to the MTFS, as noted by the AGS, to enhance transparency and thus aid scrutiny. • Detailed information on spending priorities and future spending trends across portfolios, and cross-cutting issues such as addressing climate change, should be included. As envisaged by the

BPRG, where a policy announcement has significant financial consequences, the anticipated implications should be set out for each year of the MTFS, along with an assessment of the long-term financial sustainability of existing policy. • Data, scenario planning and modelling used to underpin assumptions should be included.

- Detailed information on all fiscal risks should be provided, along with specific actions that the Scottish Government would take to mitigate each of these individual risks. This should include how the Scottish Government plans to address forecast shortfalls, reconciliations and increased demand for social security payments.
- A definitive single statement of relevant tax and spending policies should be factored into the MTFS.

The Committee hopes that these recommendations are useful in embedding the MTFS in the budget process, enabling effective committee scrutiny, and providing a comprehensive overall picture of Scotland's medium-term public finances. They also reflect recommendations arising from our budget scrutiny about the need for greater transparency in all aspects of the budget process, from introduction of the Scottish Budget to publication of the Scottish Government's consolidated accounts, as well as longer-term planning through the MTFS and spending reviews.

We look forward to receiving your response in due course and to considering the next MTFS later this year.

Yours sincerely

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Convener  
Finance and Public Administration Committee