OFFICIAL REPORT
AITHISG OIFIGEIL

Finance and Public Administration Committee

Tuesday 5 October 2021

Session 6

The Scottish Parliament
Pàrlamaid na h-Alba

Tuesday 5 October 2021

CONTENTS

FINANCE AND PUBLIC ADMINISTRATION COMMITTEE
7th Meeting 2021, Session 6

CONVENER

*Kenneth Gibson (Cunninghame North) (SNP)

DEPUTY CONVENER

*Daniel Johnson (Edinburgh Southern) (Lab)

COMMITTEE MEMBERS

*Ross Greer (West Scotland) (Green)
*Douglas Lumsden (North East Scotland) (Con)
*John Mason (Glasgow Shettleston) (SNP)
*Liz Smith (Mid Scotland and Fife) (Con)
*Michelle Thomson (Falkirk East) (SNP)

*attended

THE FOLLOWING ALSO PARTICIPATED:

Kate Forbes (Cabinet Secretary for Finance and the Economy)
Douglas McLaren (Scottish Government)
Claire McManus (Scottish Government)

CLERK TO THE COMMITTEE

Joanne McNaughton

LOCATION

The Adam Smith Room (CR1)

Scottish Parliament

Finance and Public Administration Committee

Tuesday 5 October 2021

[The Convener opened the meeting at 10:30]

Pre-budget Scrutiny 2022-23: Public Finances and Impact of Covid-19

The Convener (Kenneth Gibson): Good morning and welcome to the seventh meeting in 2021 of the Finance and Public Administration Committee.

For agenda item 1, we will take evidence from the Cabinet Secretary for Finance and the Economy in what is our final pre-budget scrutiny session. Unfortunately, the cabinet secretary is unable to be with us in person as she recently tested positive for Covid-19. I hope that she is recovering well and that she has not been too badly affected by the virus. Members will have received a paper from the clerks along with private briefings from our budget adviser and the Scottish Parliament information centre's financial scrutiny unit.

I welcome to the meeting Kate Forbes, Cabinet Secretary for Finance and the Economy, who is joined by the following Scottish Government officials: Douglas McLaren, deputy director, budget, pay and pensions; and Claire McManus, fiscal framework team leader. I intend to allow 90 minutes for the session.

Before I open it up to questions from the committee, I invite Ms Forbes to make a short opening statement.

The Cabinet Secretary for Finance and the Economy (Kate Forbes): Thank you for the invitation to join the committee, convener. I am sorry once again not to be with you in person. I hope that the committee has not started to draw any conclusions from the fact that I seem to have to self-isolate only when I have a Finance and Public Administration Committee evidence session. I also thank the committee for its engagement to date with regard to the budget timetable.

I know that you asked for very brief opening remarks, convener, but I wonder whether I can make some comments that will be helpful to the committee's scrutiny. I am grateful that, in agreeing 9 December as the date, we have duly balanced the time to develop our budget proposals with the time for due scrutiny. As the committee knows, our position is as ever contingent on our settlement from the Treasury on 27 October, but this year at least we should have firmer and fuller information than we have had for the two previous budget processes. The timing of the United Kingdom spending review and the autumn budget seems to be a return to the pre-Brexit and pre-Covid cycle, but as yet I do not have any insights into whether that means that the Treasury plans an update in the spring.

With this budget, the fiscal framework and the wider devolution settlement will continue to be tested with the related volatilities having increased and the levers and the flexibilities remaining constrained. That applies as much to our in-year management, with the UK Government repeatedly indicating consequential funding of "up to" a provisional amount that is subject to confirmation later in the year, by which time the moment or the need for that funding has often passed. As I have always said, additional funding is generally welcome when it comes, but what I want to emphasise is that the arrangements for confirming the funding generally fall short of what is required, especially during a real-time pandemic response.

I will continue to engage positively with the UK Government as we recover from Covid. I had a meeting with the new Chief Secretary to the Treasury last month, and in the coming days I am due to attend a finance quadrilateral that is focused on the spending review. We will, of course, take our strategic lead from the programme for government, and the budget will reflect and fund the Government's priorities. Moreover, as indicated in our recent correspondence, we are continuing to carry out preparatory work on a multiyear resource spending review, and we plan to publish a framework for consultation around the time of the budget.

Finally, I will be pleased to answer the committee's questions on the fiscal framework outturn report, the publication of which fulfils the Government's commitment to transparency in the operation of the fiscal framework and provides the Parliament with information to support its scrutiny. That report shows a total provisional reconciliation of -£14.8 million that will apply to the 2022-23 Scottish budget, with the final reconciliation confirmed once the final outturn data are published later this year.

I look forward to the committee's questions.

The Convener: Thank you very much for that opening statement. In time-honoured fashion, I will start with some questions before I go round the table.

The committee received 46 submissions in response to its call for evidence, and the cabinet secretary will not be surprised to learn that, although there were myriad calls from organisations for additional expenditure, the same organisations were much more coy about exactly how much they were calling for and, indeed, whom the Scottish Government would or should ask to pay for that expenditure. Often the responses suggested that any benefits from such expenditure would be long term but the costs would be much more immediate.

We have also had Labour politicians seeking a quadrupling of the Scottish child payment at a cost of £272 million a year and Conservatives suggesting that the Scottish Government could, if it so wished, pick up the tab for the £20-a-week cut in universal credit at a cost of £461 million a year. My simple question is this: how much room does the Scottish Government have for manoeuvre and what are its priorities in the coming year?

Kate Forbes: That is an important context-setting question because, as I said the last time I appeared before the committee, next year's budget feels like one of the most challenging in devolution. I think that every finance secretary has said that since the beginning of devolution, but next year's budget is particularly challenging for three reasons.

First, the costs of mitigating Covid continue, as do the associated volatility and uncertainty. Therefore, we need to manage those when it comes to self-isolation payments or the national health service. Secondly, we are trying to remobilise all our public services. Remobilising the health service, social care and the justice system requires financial support, as does economic recovery.

Over and above that, the final challenge is the funding settlement that we are receiving. Although they were significantly less, there were still Covid consequentials this year. I think it highly unlikely that we will see such additional funding from the United Kingdom Government to deal with the additional pressures next year. Indeed, the UK Government is already pulling back significantly, with the removal of the £20-a-week uplift to universal credit and the end of the furlough scheme.

All in all, the cost and the need will continue but the funding that is available to us will significantly decrease.

You asked what the Scottish Government's priorities are. Our priorities are set out in the programme for government. They are simply to continue to support families in need who are dealing with the consequences of Covid and some of the inequalities that it has exacerbated, to remobilise our public services and to drive economic recovery. Those are our three main priorities.

You talked about the Scottish child payment. The First Minister said in the programme for government that we would double the payment to £20 as soon as possible. We will outline plans in the budget for how we will do that.

The Convener: I am tempted to come back on that last comment, but I will move on, because I want to touch on a number of issues so that colleagues can expand on them.

The committee often gets suggestions that local government should be provided with more flexibility to, for example, raise revenue on its own. Indeed, we received such suggestions this year. Has the Scottish Government identified any additional revenue streams that it could adopt or could devolve to local government? Will it encourage local government and other bodies to develop their own revenue streams, given the current financial situation?

Kate Forbes: As you can imagine, over the past few years in particular, local government has looked extensively at ways of generating income. For the most part, local authorities have developed their own schemes. We saw that impact acutely during Covid, when some local authorities were more exposed to income reduction than others. You will recall that I put in place funding to cover the fact that some local authorities were no longer generating income during Covid.

On additional taxation powers, prior to the pandemic, we were in discussion with local government about a number of different local taxes, including the tourism levy, on which members, the Parliament and people beyond the Parliament have different views. We were considering the most comprehensive devolution of additional tax-raising powers to local authorities since the advent of devolution. Covid has put a temporary stop to some of that.

However, I am sympathetic to allowing additional fiscal flexibilities for local government. If we call for fiscal flexibilities for the Scottish Government, it is only right that those be passed on to local authorities. We have managed to secure some temporary additional fiscal flexibilities for local government; in fact, we have been more successful in securing temporary fiscal flexibilities for local government during the pandemic with the support of the Treasury than we have been for ourselves. I am very happy to continue to explore with local government what additional powers it needs, but I stress that different authorities have different balances of income from different taxes, other fees, charges or income, or from the Scottish

Government. That is how it should be. Local authorities should be able to tailor their income generation approach to local circumstances.

The Convener: Obviously, significant multibillion-pound consequentials have been received from the UK Government since the start of the pandemic. How much of that is still available to allocate? Is there any risk of a clawback? Has there been a guarantee of consequentials from the UK health and social care levy and when will they be delivered?

Kate Forbes: Again, that is an important question. Last year, we had a guarantee. Where money was announced, it was guaranteed to come. However, prior to the pandemic, the way in which the UK Government funded the Scottish Government was by making announcements and confirming the funding at key points in the financial year.

On our funding position, we have allocated £980 million of the £1 billion of Covid consequentials in the budget revision, which I imagine the committee will take evidence on over the next month. The Minister for Public Finance, Planning and Community Wealth will lead on that. On top of that, we have drawn down £168 million of balances from the Scotland reserve to support the health service and farming in particular. The balance that is left for formal allocation following the budget revision, which the committee will take evidence on, is £328 million, of which £250 million relates to capital and financial transactions that are being deployed across a range of pressures for capital budgets, such as in health, transport, energy and education.

Obviously, there is a difference between funding that is allocated formally through the budget revision and our on-going internal budget management in the Scottish Government. Every single penny has been earmarked or allocated, and the money is supporting our in-year budget position. Where we have not formally allocated funding, we will do so once we have had reassurances from the UK Government at the supplementary estimate.

In short, I cannot confidently allocate every penny without the Barnett guarantee until that funding has been formally guaranteed for me by the UK Government. We expect the Treasury to provide an update on additional funding for 2021-22 alongside the spending review in late October. Formal confirmation from the UK Government often happens in the days after the spending review. We will be in discussion with it to get that formal confirmation of our spending so that we can ensure that the Parliament, through the budget revision, has a formal allocation of every penny.

The Convener: I am going to ask a couple of questions about the impact on economic growth of issues that are currently prominent in the news; in fact, I saw the Prime Minister answering questions on them in the news this morning.

In the hour prior to the meeting, we had a significant discussion about skills shortages with our budget adviser. Skills shortages are acute in many sectors, and there is huge divergence across Scotland—we acknowledge that. What additional resources will the Scottish Government invest to address those shortages? Which sectors are being prioritised? Is there a focus on geographic areas of the economy? In some areas, there is a surplus labour pool whereas there is a chronic shortage of labour in other areas. In economics, there is always the question whether the people should be moved to the jobs or the jobs to the people. What is the Scottish Government's view on that, given that, when we consider the demographic future of Scotland, even over the next decade, we see that some local authorities will have significant population growth? For example, there is projected growth of 8 per cent for Midlothian, whereas there is a projected 4 per cent reduction for the Western Isles. What is the Scottish Government's approach to that key issue?

10:45

Kate Forbes: I should say at the outset that we of course track Scotland's economic performance very closely, not only because of its implications for our revenue position but because it is important that we track our performance in relation to that of the rest of the UK, given the operation of the fiscal framework.

Although Scotland's gross domestic product is still below pre-pandemic levels, it is gradually recovering and it is continuing to broadly track that of the UK as a whole. As you said, convener, the pace of recovery is different across not just geographies but sectors, and it is clear that some sectors are more exposed to the bottlenecks in supply chain and recruitment. Food and drink, for example, which is a particularly important Scottish industry, is facing severe challenges as a result of rising prices and labour market shortages.

The Scottish Government stands ready to do whatever we need to do and can do. That includes close engagement with the UK Government. Richard Lochhead is leading on the labour market shortages and is working hand in glove with industry to intervene where we can. One of the most obvious interventions that we can make is in the skills system.

However, I strongly emphasise that I do not believe that the shortages and challenges that we are talking about can in any way be resolved through the Scottish Government's budget alone. We have a role to play, and we play it and take our responsibilities seriously, but it is well documented that the acute labour shortages that we face right now are largely to do with immigration policy, over which we have no control.

We can intervene. Some of those interventions might look small, but we are doing what we can, for example by funding a marketing campaign to try to recruit more people to the hospitality industry. I am sure that industry will say that that is small fry compared to what it really needs, which is the ability to access visas and bring in far more people to work in the sectors that we are talking about.

The same goes for supply chains. We engage closely with our UK Government counterparts—I have regular meetings—not least on the challenges to do with gas prices and the CO_2 shortage, which has been temporarily fixed but not resolved for the long term. Those are acute issues.

I guess that what I am trying to say is that, where we can intervene, we absolutely will do, but I do not think that anyone is suggesting that the Scottish Government can resolve the issues. Certainly, from a budget perspective, financial support will go only so far: the issues are much bigger.

The Convener: Immigration is a factor, but surely we must do more to upskill the 4 to 5 per cent of the population who are currently unemployed at a time when there is a huge number of vacancies in the economy. I am keen for the Scottish Government to do more to address the issue.

You mentioned gas. The Scottish Government has a national collaborative framework for the supply of natural gas, which means that there has been no increase in the wholesale cost of gas since April 2021 and that there will be no increase during this financial year. First, what is the impact on the Scottish Government likely to be next year? I imagine that the framework will have to be renegotiated in view of prices and that the impact will be significant. Secondly, what impact will there be on the private sector, particularly fuel-intensive industries? I have a number of such industries in my constituency—I am sure that that is the case for other members. What, if anything, can the Scottish Government do to assist with the issue?

Kate Forbes: You talked about the reskilling that is required, which is vital. It will not help in the short term, but we need to ensure that the money goes to the people who most need it.

On energy costs and fuel shortages, we engage closely with industry, as I said. I guess that the big tool that I have at my disposal right now, and on which I am giving you evidence, is the budget. Industry figures repeatedly tell us that they are not looking for financial support. They want to be able to trade. The economy is recovering, trade is available and markets are there, but industry cannot meet demand. The difficulty is with supply, not with demand. When it comes to prices, energy costs and shortages, in our close engagement with industry leaders, they repeatedly tell us that the solutions lie not in financial grants but in enabling them to access the adequate and affordable supplies that they need.

We will repeatedly engage with the UK Government, but I do not have any unallocated budget this year to meet the shortages in full. We have neither the consequential funding for that nor the headroom to provide additional financial support.

The Convener: I have a couple more questions before we open out to other members of the committee.

What was the level of engagement with the UK Government prior to its announcement that it will set out a multiyear spending review, given the impact that that will have on Scotland's finances?

Kate Forbes: I hope to be able to build a constructive relationship with the new Chief Secretary to the Treasury. I had a good first conversation with him just over a week ago. I am due to see him on 14 October for a quadrilateral meeting about the spending review and I may be able to answer the question better after that meeting. I am happy to provide the committee with an outline of that meeting and an update about how it goes.

The Convener: I was pleased that you invited me, the deputy convener and the convener of the Social Justice and Social Security Committee to a meeting last week to discuss issues with the fiscal framework. I have one question about that. The fiscal framework has helped us through Covid-19 and the early months of Brexit, but what weaknesses have been identified in the framework and how can it be improved and made more flexible? What engagement has there been with the UK Government on the scope of the review and when it will commence?

Kate Forbes: Your predecessor committee was very helpful in this regard. Its report on the fiscal framework was supported by all parties. The report identified some benefits of the fiscal framework, particularly during a period of volatility, but it also identified some of its shortcomings. We are due to work with the UK Government to commission an independent report on the fiscal framework. I am keen that that report captures all the points that the previous committee and independent stakeholders such as the Fraser of Allander Institute highlighted.

The previous committee's report demonstrates that the arbitrary caps on borrowing for the forecast error and on spending are not keeping pace with inflation, with the size of the budget or with the potential size of the forecast error. The report also suggests that we have limited ability to carry forward and manage the budget across years. Thirdly, there are challenges to managing levels of volatility and risk and we should consider some additional levers to help the Scottish Government manage that. It is a very technical area and I would be grateful if the committee continued considering what it believes should be done with the fiscal framework. The review or the report should not be so narrow that we are not cognisant of what the pandemic has taught us about the operation of Scottish Government finances.

Liz Smith (Mid Scotland and Fife) (Con): Cabinet secretary, you mentioned the programme for government in an answer to the convener. In your speech about the programme for government, when you talked about trying to encourage economic growth, you said that it is the Scottish Government's mission

"to create the best conditions for entrepreneurs to seize the opportunities"—[*Official Report*, 2 June 2021; c 17.]

to increase production and innovation and to create jobs. Obviously, you will have seen statistics from the Scottish Fiscal Commission and, I am sure, will have had advice from your new council of economic advisers, which, I think, is providing some evidence about the period from July to the autumn. Obviously, you are not going to tell us the detail of the budget, and I would not expect that, but where are they trying to focus your attention when it comes to the priorities for that economic growth?

Kate Forbes: There are a number of different points. The first is a real focus on innovation leading to productivity. You will be mindful of that, and, over the past few days, we have heard in the media a lot about UK-wide productivity challenges. There are real challenges when it comes to increasing levels of productivity. Those are being highlighted by population shortages right now. If we live in an environment in which we are unable to access additional labour from outwith the country, it is even more imperative that we invest in innovation and tech and that we improve productivity levels across the country. That point has been repeated for a number of years by the Confederation of British Industry and others. That focus is on how we incentivise innovation and invest in productivity; that includes investing in our people.

That takes me to my second point, which is a real focus on skills—making sure that we have the right skills in the right places for the right jobs. We have seen, post-pandemic—not that we have got through the pandemic—that unemployment is much lower than was originally forecast; however, that means that there are acute labour shortages in certain sectors. We therefore need to make sure that, through the young persons guarantee and our other interventions such as the national transition training fund, we are reskilling people with the right skills—those that are actually required.

Those are two areas that are coming through loud and clear in the conversations that we are having around the advisory council, that I am hearing regularly from business organisations and that I would like to see prioritised in the forthcoming budget.

Liz Smith: That is very helpful indeed. On the reskilling issue, I have heard people such as Sandy Begbie talk about the young persons guarantee from the perspective that, although young people have particular issues at this time, many other issues involve the need to reskill people who have been in the economy, in a job, are perhaps still on furlough but are not necessarily going back to the job that was there before the pandemic. Can I press you a little on what priorities you feel need our attention when it comes to upskilling those who will probably find it very difficult to get back into the labour force?

Kate Forbes: I think that that is a fair point. Although interventions around young people are important, we face real challenges in relation to people who face redundancy or have been made redundant because their industries are changing. That is where the national transition training fund comes in; it seeks to provide funding to particular sectors to help their people transition.

For example, I take you back to the tourism recovery plan. Bear in mind that that was the response to recommendations that were established by the tourism recovery task force, which was composed predominantly of industry leaders. They asked specifically for help for reskilling and retraining. An element of the national transition training fund has therefore gone specifically to help the tourism and hospitality industries reskill and upskill their staff. Obviously, they are facing labour market shortages, so it is really important that the right skills are there.

When it comes to people who are moving between sectors—upskilling not within their sector but between sectors—we also have support in place. Perhaps we need to review that support and make sure that it is fit for purpose, as we progress through the pandemic, to help take people from where they are now to where they want to be. The most obvious example of that would be providing support for people in the oil and gas sector, who have, unfortunately, faced redundancy, not because of decisions made by Governments in this country, but through the global reduction in the demand for oil and gas. That support needs to be made available within and across industries.

I will make a final point before I stop. Through partnership action for continuing employment—PACE—which is the wraparound support for employees who face redundancy, we have specific and targeted training available to help. However, it is a huge challenge to equip people with the skills that they need to transition to a new job or a different job in their industry.

11:00

Liz Smith: I have two more questions. First, you mentioned the tourism sector. A lot of tourism bodies, particularly in Perthshire, tell me that it is difficult to get people to take up jobs that are there, because they do not actually want the jobs, which is different from not having the right skills. If we look at the statistics for employment and unemployment, we can see that a latent workforce is out there but, in many cases, those people do not want the particular jobs that are on offer, and that is different from the skills agenda. What is the Scottish Government doing to address that problem?

Kate Forbes: It is a difficult problem to solve, because we cannot force people into particular occupations, but we can make those jobs more attractive, and there was a real focus on that in the tourism recovery task force's work. Previously, I referenced some of the short term urgent work that we were happy to do with the tourism industry, which was specifically to help recruit to those roles, by presenting tourism as an attractive industry to work in. A lot of the tourism recovery task force's work looked at how to make it a more attractive career option. Rather than assuming that it is just a filler job until people get something else, we need to think about how we make it more attractive. The tourism recovery task force—which, again, is predominantly industry based—had a number of suggestions on how to do that, and we have provided initial support, particularly around skills and training. I know that I am talking about skills and training, but that is also part of the attractive package within the tourism industry because we hope that, if people feel like they are being invested in, they will have a greater sense of loyalty and responsibility to the job. Terms and conditions and pay go alongside that, so trying to ensure that the living wage is being paid is one small example. It is a huge area and, where we can provide support, we will do so, whether that is financial support or working with the industry to implement its recommendations. However, that work is very much industry led and that is important.

Liz Smith: Thank you. My last question is about tax revenues. Obviously, we have heard from many witnesses to the committee that there are demographic issues in relation to Scotland's ageing population, so the working population is being squeezed. With regard to the overall budget, where is the greatest possibility, from a Scottish perspective, for raising tax revenues that, in turn, would help with Government spending?

Kate Forbes: There are two parts to that. First, we need a growing economy to ensure that there are tax revenues. I am a firm believer in the notion that, if businesses are trading well and paying their taxes, we have a secure source of revenue, and that was the reason why we extended non-domestic rates relief for a full year. We could have implemented non-domestic rates halfway through the year, when signs of recovery were obvious, but I wanted to extend relief to a full year in order to maximise the time for industry to recover. As we go into the budget, we will be very cognisant of the need to ensure that our taxation enables businesses to fully recover and fully trade. Clearly, since the pandemic, other challenges have faced business, not least the shortages that have perhaps hindered their ability to trade fully.

Secondly, we have to continue to use the mix of tax that we have. We get limited income tax as well as non-domestic rates, which, although a property tax, are often considered as the primary business tax. To be honest, I do not see any huge room for manoeuvre in both just now. We know that, when it comes to income tax, what really matters is our performance relative to the rest of the UK; moreover, we do not have allowances or incentives with it and we have to be mindful of how it interacts with national insurance contributions. As for non-domestic rates, they are a property tax rather than a business tax.

My first answer to your question, therefore, would be economic growth, and my second would be room for manoeuvre on tax policy.

John Mason (Glasgow Shettleston) (SNP): Good morning, cabinet secretary. There are many areas to discuss, but I want to go back to the issue of inflation, which has already been mentioned.

We have had some discussion with our advisers about short-term inflation. That could include, for example, people with savings rushing out to buy the same kind of car, which would leading to a shortage of such cars and prices going up. Presumably, though, that sort of thing would come down. Something like the gas price, however, could stay higher for longer. Moreover, with wages, could a shortage of staff inevitably lead to inflation? If so, what impact would that have on Scotland and the Scottish budget? After all, if hotels and shops start paying higher wages, we will have to pay nurses and everyone else higher wages, too. Do you feel that inflation is a major problem or is it, in fact, quite minor?

Kate Forbes: It is a very significant consideration in our budgeting. You have mentioned a number of the impacts that it can have on our budget, but perhaps the most obvious one relates to pay, given that a significant percentage of our budget is spent on people—for example, the staff in our NHS, local government and public bodies. Public sector pay is therefore an important element of our budget setting; it has certainly been a big focus of previous budgets, and you have to be mindful of inflation when it comes to public sector pay policy. Inflation has other implications, too, but as you will know, it has an impact on costs, and we cannot escape its impact if we are to achieve our policy aims or build the infrastructure that we want to build.

I do not want to put him on the spot, but I wonder whether Dougie McLaren wants to come in on this question.

Douglas McLaren (Scottish Government): I do not have too much to add. We and others look very closely at the Bank of England's outlook, and it has projected a rise in consumer prices index inflation to at least 4 per cent by the end of this calendar year and continuing into the new year. Indeed, as far as public sector pay is concerned, that will be happening at the very time when most if not all workforces will be looking to renegotiate new deals that are fair, sustainable and affordable. With the devolved public sector pay bill being such a significant part of the Scottish Government's resource budget, that is clearly a really important issue for this particular budget.

We will wait and see what if anything the Chancellor of the Exchequer will say later this month about his underlying public sector pay assumptions for the spending review. He might say very little; we might get some insights, and we will of course ask questions. However, the fact is that, with their pay remit cycle, Whitehall departments tend to negotiate their respective pay deals later in the year than we do, so we have to go first with the settlement that we have. As a result, we will be watching things very closely.

John Mason: I move to capital expenditure and borrowing. The fiscal framework outturn report shows that we are increasingly nearing our limit on borrowing, which I think is £3 billion. The forecast is that we will be at 82 per cent of that limit by the end of 2023-24. Will that cause problems? Assuming that the fiscal framework is not revised, which is a separate question, what happens if we hit that limit?

Kate Forbes: The short answer is that we will not hit that limit if we continue on the trajectory that we set out in the medium-term financial strategy, because we cannot. We have to allow for headroom and obviously have to manage our budget in a way that allows for unforeseen circumstances. The medium-term financial strategy set out our approach to borrowing, and clearly the next one will set out that approach as well.

That does not mean, however, that we could not use additional borrowing powers if the cap were higher. I believe that our borrowing powers should be more in line with those of local government, whose prudential borrowing scheme is based on affordability rather than arbitrary caps. The latter do not take into account the changing nature of the challenges or the economic imperatives to invest or not to invest, so the argument is for something that is more akin to the arrangement that local government has rather than arbitrary caps.

John Mason: I am in favour of the prudential framework as well. Do we have any indication from Westminster that it would be willing to discuss that kind of thing when the fiscal framework is reviewed?

Kate Forbes: I hope to discuss it. We are not seeing a huge appetite for change, and I have not had much evidence of such an appetite during the pandemic when we looked for temporary fiscal flexibilities. I think that the discussion is unlikely, but there is an opportunity for civic Scotland—if I can put it like that—on a cross-party basis to come to a position on borrowing that is good for Scottish businesses and the Scottish economy, and is not new, since local government already has it.

The Scottish Fiscal Commission obviously has to judge our projections of capital borrowing, and its most recent report said that they were reasonable.

John Mason: I move to the part of the fiscal framework outturn report on social security. I confess that I find some of it quite complex, but if I understand the figures correctly, the forecast in the 2020 budget was an expenditure of roughly £3.212 billion and the outturn was roughly £3.262 billion—around £49 million more. Many changes have happened—we have not taken on some things quite as quickly as we had hoped, and Covid must have had an impact. Is it too early to say what is happening with the social security system, or do you think that we will struggle to stay within our social security budget?

Kate Forbes: Discussions about the fiscal framework have often focused on the volatility that is inherent in tax forecast, and perhaps we focus less on the inherent volatilities in social security demand. There are two reasons for forecast error in relation to social security: one is that we have been through quite an uncertain 18 months with Covid, so it would make sense that getting a grasp of what demand truly is has been challenging.

Secondly, it is likely, as the SFC's forecast illustrated, that demand for social security will increase. Revenue borrowing for forecast error is capped at £300 million, which needs to cover not only tax volatility but also social security volatility, and we have an obligation to fund social security because it is a demand-led budget.

Therefore, there are two challenges. One is that I have to fund a significant demand-led budget line from a fixed budget and, secondly, the limits on our revenue borrowing for forecast error are quite low to meet the errors that occur. It is an area of concern. We must ensure that we can continue to meet that demand-led budget, which we are obliged to and must meet, but if we do not have any capacity in the revenue borrowing limit we have to fund the forecast error from within our budget.

11:15

John Mason: There is a lot in there that we could explore further. However, I will move on to the other point that I want to raise, which is about the recent national insurance increase at Westminster. I believe that it is to be called the health and social care levy. Are we clear about exactly what Scotland will get from that or how it will work for us?

Kate Forbes: Yes and no. I wrote to the UK Government in the immediate aftermath of the announcement of the health and social care levy to seek clarity on various points. The response that I got did not actually give me any of those answers. The big question remains what we will get in additional consequentials. In the past, when there have been announcements about increased spend on health and social care that have generated consequentials, we have later discovered that those have been netted off against funding that was due to come anyway, so it is not all additional. We know what the UK Government has publicly announced for Scotland, but the big question for 27 October is whether that will all be additional or whether some of it will be netted off against decreases in other health and social care lines, so that it is not, for example, a net additional £1 billion.

John Mason: Thanks.

Ross Greer (West Scotland) (Green): Good morning, cabinet secretary. I was keen to discuss with you the effect of the arbitrary cash-terms limits on the fiscal framework, but you covered that with Mr Mason. Therefore, I will move on to non-domestic rates, which you touched on in your answer to Liz Smith.

The total value of non-domestic rates relief through the various schemes that are on offer in Scotland comes to somewhere in the region of £700 million. That was expanded during the pandemic—for example, to the newspaper industry—for obvious reasons. I think that the decision was twice unanimously supported by Parliament. There is a range of options for non-domestic rates relief; what evaluation has the Government done of the effectiveness of the various schemes?

Kate Forbes: That is a good question. We have commissioned the Fraser of Allander Institute to review the effectiveness of the small business bonus scheme, in particular. That work is on-going. The institute is reviewing how effective the scheme is in meeting its policy objective of helping small businesses. The scheme has a huge role to play, especially in local economies and on our high streets. That is the primary review that is on-going.

However, we are regularly asked for additional reliefs. We now have reliefs in place for hydro power, new buildings and recently occupied buildings, all of which will have to be reviewed according to their terms. The business growth accelerator, which incentivises new builds, and the fresh start scheme, which incentivises tenants to occupy previously unoccupied buildings, need to be reviewed on their own merits. At every budget period, we consider again whether either those reliefs are the best use of our limited funds, or there is another way to meet the policy aims—which, I think, we all agree on—through other use of the funding. Such regular reviewing is important.

Ross Greer: When is the Fraser of Allander Institute review due to report?

Kate Forbes: That is a good question. I might have to write to you on that. It was originally due a number of months ago, but was delayed because of Covid. We wanted to ensure that the reviewers got access to small businesses and had comprehensive data. If my officials do not know whether we have confirmed an updated timetable, I will get back to you in writing about the latest deadline.

Ross Greer: Excellent. That is appreciated.

You mentioned the regular requests that are made for additional rates relief. That is absolutely the case, but recently there have been more requests than I have noticed in previous years for additional conditions to be placed on rates relief. For example, in its evidence to the committee, the

Scottish Trades Union Congress proposed conditions on fair work and the living wage, and Alcohol Focus Scotland has proposed that a public health condition be levied on licensed premises. Without necessarily commenting on any specific proposals—you are, of course, welcome to do so, if you wish to—will you comment on the principle of additional conditionality on rates relief, particularly given the challenging overall fiscal situation in the coming years?

Kate Forbes: I will answer that in two parts. First, I support the principle of conditionality across all Government spend. We should consider more carefully where we can embed proportionate conditionality; we have committed to do that, as part of the co-operation agreement.

The second part is perhaps more disappointing. I have looked at non-domestic rates through every lens to consider how we can expand conditionality, but doing so is extremely challenging, if not impossible, in places. We place a huge burden on non-domestic rates—which, we should bear in mind, are a property tax—because we have no other form of business taxation in Scotland.

It is difficult to use conditionality in non-domestic rates in any way but through conditions that relate to the property itself, because it is a property tax, not a business tax. Non-domestic rates are based entirely on a property's rental value—what that property might get in the open market—which is applied to the poundage. The tax was not established to take into account income generation, nor was it ever based on employees. The various conditions that we might want to attach to reliefs are almost impossible for a property tax.

That is not to say that we have not considered the possibility. During the pandemic in particular, I was keen to see whether we could attach other conditions. However, the methodology behind non-domestic rates—the way in which rates are collected and the principle that underlies them—means that it is almost impossible to attach conditions that are not specifically related to the property.

People might argue that we should overhaul non-domestic rates and set up a taxation regime that is based on income and other factors. That is a perfectly legitimate argument to make, but because it is a property tax, we look to non-domestic rates to do more than it was set up to do or is capable of doing because it is the only form of semi-business taxation that we have in Scotland.

Ross Greer: That is useful.

The Coronavirus (Scotland) (No 2) Act 2020 included conditions on awarding Covid relief grants to businesses, specifically in relation to tax avoidance. That is timely this week, given the revelations in the Pandora papers. I accept that it is particularly challenging to review the effectiveness of such a measure because we would hope that the net effect would be that businesses that would be caught by it would not bother trying to apply in the first place. However, has any attempt been made to evaluate the impact of attaching a tax-avoidance condition to Government grants?

Kate Forbes: Yes, in short. I note that that applies to non-domestic rates as well, to link in with your previous question. The Barclay review of non-domestic rates specifically talked about what powers we might have in Scotland to crack down on tax avoidance. That was incorporated into a general tax avoidance provision. I am happy to send the committee more information about non-domestic rates in that context.

You will remember that in discussion about tax havens there was a lot of public debate about whether or not the Scottish Government had the power to act. Where we have powers or softer means of cracking down on tax avoidance, we will use them, but the issue is, ultimately, reserved. When it comes to having real teeth that can crack down on tax avoidance, the powers are still reserved to the UK Government.

Ross Greer: Thank you.

Douglas Lumsden (North East Scotland) (Con): Good morning, cabinet secretary.

I was pleased to hear you mention the potential for increased flexibilities for local government in terms of raising revenue. Will you expand on that and say when it might happen? Will it happen as part of the budget process or as part of the local government fiscal framework that is, I think, in development? Could one of the flexibilities be removal of the 3 per cent council tax increase cap?

Kate Forbes: Your question highlights the point that some things can be actioned in budgets from year to year; you asked about council tax. A fuller conversation about the right mix of powers and flexibilities is—I think, rightly—for the fiscal framework discussions, in collaboration with the Convention of Scottish Local Authorities. The discussions have, largely because of Covid, perhaps not moved at the speed at which I think either party would have liked them to move. I am committed to getting them back on track.

Our position on council tax, specifically, will be set out in the upcoming budget. I assure you that that budget will be set only after extensive consultation with COSLA's finance spokesperson, Gail Macgregor.

Douglas Lumsden: May I ask again about the timetable? I raised the issue at COSLA a couple of years ago, but it has not progressed. When might the framework be approved by the Scottish Government and COSLA?

Kate Forbes: There are two parties involved and—as you will be aware—quite a lot of change is afoot for local government over the next year. I think that we can make some progress prior to the local government elections, but I imagine that the matter will be one of the first that will be picked up after the elections. We are committed to working with COSLA to develop a rules-based fiscal framework to support future funding settlements.

The other part of the issue—again, this is not a cop-out—-is that a big ask from local government is for the ability to set multiyear budgets. Along with the need for additional flexibilities, there is a need to know what will be in a budget from year to year. I sincerely hope that the resource spending review that we will set out will allow local government to look three years ahead. [*Inaudible*.]

The Convener: I am sorry; we seem to have lost the cabinet secretary.

Are you back with us, Kate?

Kate Forbes: I am sorry; I did not catch that.

Douglas Lumsden: I am sorry, cabinet secretary. You broke up there, but you are back now.

Kate Forbes: I do not know whether it is just my connection. I am struggling to hear committee members.

Douglas Lumsden: Okay. I will try to move on.

Air passenger duty is mentioned in the fiscal framework outturn report. There was a consultation between March and June. When will there be progress on that, or will that not happen?

Kate Forbes: You will recall that we were all set to devolve air passenger duty when we discovered a pretty major issue to do with subsidy control in relation to the Highlands and Islands air discount scheme. We had extensive conversations with the UK Government about where the matter would sit. We could not expose our finances to any potential liability before the matter was resolved—as it had to be—with the European Union.

In the past six to nine months, however, the fundamental issue has moved slightly because of Brexit. We will want to progress the matter in our discussions on the fiscal framework. Ultimately, the challenge was to resolve the issue of the Highlands and Islands exemption before air passenger duty was devolved.

11:30

Douglas Lumsden: I guess, in that case, that the answer is that air passenger duty will be dealt with in the next fiscal framework.

Kate Forbes: We do not need to wait for that. Conversations are continuing with the UK Government, and we are still fully committed to devolving the duty. There are two points to highlight. The first is that we were making good progress on resolving the Highlands and Islands exemption. Secondly—although I do not want to keep using it as an excuse—the fact is that Covid struck. Many areas that were being progressed at pace prior to Covid are now being picked up again. Because of the wider conversation that we are having on the fiscal framework, it makes sense to have our other conversations in that context.

Douglas Lumsden: Many witnesses have told the committee that meeting our ambitious net zero targets will require a huge amount of investment. Will any commitments that are in place have to be removed to meet the new commitment?

Kate Forbes: Thankfully, as far as our net zero commitments are concerned, two areas are already highly visible. The first is the capital spending review. It was completed last year and published alongside the infrastructure investment plan, and gives a long-term multiyear view of investment in infrastructure. I do not know whether this has come through in the evidence that the committee has received, but one of the primary drivers of the shift to net zero will be investment in low-carbon infrastructure.

We talk at length about the need for a transition in transport; however, that will require public and, indeed, private sector investment in transport systems. The same goes for heating and power. The capital spending review stands prior to this budget, which will action the next year of the capital spending review with regard to investment in low-carbon infrastructure. I also point out that that has been accompanied by a £2 billion low-carbon fund to accelerate investment.

The second area is the programme for government and the co-operation agreement with the Greens, which are quite clear about the shifts that need to be made. The budget is actually just the power behind the programme for government; it enacts the programme with real money, from a challenging settlement.

Douglas Lumsden: Do you see commitments such as the dualling of the A96, for example, having to give way to meet the new commitments?

Kate Forbes: No. As a Highlander who knows the importance of such roads and who has driven up and down the A9 far too often to count, I think that it is really important that we continue to invest in Highland, northern and north-east communities.

Michelle Thomson (Falkirk East) (SNP): I will follow on from the theme of tax avoidance that Ross Greer highlighted.

I understand that there is a historical dispute going back to devolution of further powers in relation to proceeds of crime and £30 million that it was originally assumed would remain with the Scottish Government but which the UK Government now assumes will go back to it. Is that still the case, and can you give us any insight into the discussions that you are having with the UK Government on the matter? Can you also confirm that, if you moved resources from Police Scotland into dealing with more financial crime, none of the benefit of such a move would accrue to the Scottish Government budget?

Kate Forbes: You are right that this is primarily a justice issue and that, ultimately, when it comes to policing such issues, responsibility lies with Her Majesty's Revenue and Customs and with Companies House, which both come under United Kingdom Government competence. Obviously, Police Scotland has a role when it comes to suspected criminality. However, with regard to funding, when something is a reserved matter, it will be funded on a UK-wide basis, which means that consequential funding will not be generated for the Scottish Government.

Please come back to me if I have misunderstood any element of your question.

Michelle Thomson: The point that I am trying to make is that, given the on-going dispute about no detriment, if the Scottish Government were to discover more crime—even if it were able to, which it is not, in many areas—it would not get the benefit of increased proceeds-of-crime funding, because it would all be offset in the overall budget. Is my understanding correct?

Kate Forbes: We currently believe that the application of block-grant adjustments in relation to the revenues of £4 million per annum under the Proceeds of Crime Act 2002 breaches the Smith commission's no-detriment principle. That is because we believe that that funding should come to the Scottish Government.

I have written to the Chief Secretary to the Treasury to try to progress resolution of that issue, and we have agreed that it should be resolved as part of the fiscal framework review. It is still an outstanding issue.

Obviously, this is a highly technical area. Claire McManus might be able to supply some information that I have missed out.

Claire McManus (Scottish Government): I think that the cabinet secretary has covered everything. As Michelle Thomson said, prior to the fiscal framework agreement, there was a £30 million cap on those revenues, which was never breached. That is the basis of the current dispute. As the cabinet secretary said, she has agreed with the Chief Secretary to the Treasury to consider the issue as part of the fiscal framework review.

Michelle Thomson: I will pick up on what Ross Greer said about tax avoidance. The issue is not only tax avoidance; it also involves unintended consequences. We know that there are issues around mini umbrella companies, which we have seen in relation to the pandemic. We also know that there are huge issues with Scottish limited partnerships being used for money laundering. My understanding is that none of those reside under anything that would enable the Scottish Government to do anything about them, even though, clearly, from an international perspective, our international brand as a place to do business is affected if people can freely use very loose arrangements such as Scottish limited partnerships.

Can you confirm that my understanding is correct? Can you also say whether there might be other vehicles, even in the form of soft powers, that could be used in relation to things such as Scottish limited partnerships? The Law Society of Scotland has a view on that.

I appreciate that this is straying into justice areas, so you might wish to decline to answer the question. However, it would be useful if you could give us a sense of your thinking.

Kate Forbes: In short, your characterisation is accurate. We have, where we can, used softer powers to try to crack down on tax avoidance. I would say that since its establishment Revenue Scotland has taken a firm and effective approach to tax avoidance, because it is working collaboratively with other public bodies—for example, it works closely with the Scottish Environment Protection Agency in relation to landfill. The taxes are small in the grand scheme of things, although they are important for the Scottish Government, but the point is that, since the establishment of Revenue Scotland and the development of other devolved taxation, we have taken a much more robust approach to tax avoidance. However, you are right that it is based only on soft powers rather than on actual legislation, because, ultimately, tax avoidance is a reserved matter.

Michelle Thomson: My last question is about the difference between accountability and responsibility. The Scottish Government is accountable for many of the outcomes in the national performance framework, which is very outcome-driven. Our discussion today has been about the areas where the Scottish Government has responsibility, or those where it has no responsibility, despite having accountability for a range of areas.

There is also the reverse situation in which the UK Government is accountable for many areas but is not subject to scrutiny by the Scottish Government or the Scottish Parliament.

If you were to have a choice about the areas in which responsibility was aligned with accountability, which top three areas would you pick, given the considerable short and long-term economic challenges that we have explored today? Which three things would you like to place on record?

Kate Forbes: That is a great question. From a technical perspective, being able to have a wider mix of tax powers would be far more effective for the management of our budget and of the economy. Taking business support as an example, we have just spent time discussing non-domestic rates despite the fact that that is not a business tax but a property tax. It would be good to have a broader mix of tax powers and to have all the powers associated with income tax as well as a wealth tax and perhaps capital gains tax. It would be helpful to understand and have responsibility for the interactions between national insurance contributions and income tax.

My first ask would be to have a far more comprehensive toolbox of tax powers at our disposal, so that we are not basing all our action on a few narrow taxes that cannot bear the weight of what we ask them to do. That is certainly true of income tax and that position is universally shared by tax professionals.

The second thing would be to be able to manage year-on-year volatility in the budget. It is hugely detrimental to have an arbitrary cap of £300 million for forecast error. It reduces our ability to plan ahead and it means that when forecast error exceeds £300 million, as we have seen in previous years, actual money that could otherwise be used for public services must be used to deal with the forecast error. The ability to manage our budget in year and from year to year needs to be considered.

My final point is that we should have a prudential borrowing scheme that is based on affordability. We already have to base capital borrowing decisions on affordability. I have to deal with the revenue consequences of capital borrowing in future years. I know that. The medium-term financial strategy sets out how we manage it. The notion that we would not use borrowing powers prudently if we had them does not bear scrutiny. We have had to do that in part with capital borrowing. All that we are asking for is something similar to the prudential borrowing arrangement that local government has.

Those are the three items on my wish list.

Daniel Johnson (Edinburgh Southern) (Lab): I would like to pick up on some of those points. I am interested in ensuring that we develop the fiscal framework and the budget processes around the block grant, because I believe that that is how we can strengthen the devolution settlement, which is my overarching objective.

I would like to test some of the assumptions and assertions in what you have just asked for. Prudential borrowing makes straightforward sense. Income tax revenues for the Scottish exchequer are approximately £12 billion. Your ability to borrow against the forecast error is around £300 million, which is about 2 per cent of that. The errors in recent forecasts have been a little less than that. Is that a real issue or a notional one? If it is a real issue, will you give some examples of where you have hit your headroom on the borrowing limit? Please bring the issue to life for me.

11:45

Kate Forbes: I might ask officials to comment and give a straight-bat, technical answer, but Scottish Fiscal Commission analysis shows that income tax reconciliations could exceed Scottish Government borrowing limits up to four times every 10 years. That answer may not feel as tangible as you would like. Our own analysis suggests that there is up to a one-in-six chance that funding volatility as a result of income tax forecast error will breach the current limits of our resource borrowing powers, but you must remember that the borrowing limits also have to cover forecast errors for other devolved taxes and social security benefits. We cannot look only at income tax when it comes to forecast errors.

Governments around the world have to manage their budgets within fiscal rules, and that is right and proper. The difficulty for us is that we are dealing with a fixed budget. We still have to take a very prudent approach in how we spend our money, but what we are talking about here is the ability to use our spending power to benefit public services rather than to resolve errors, which are no fault of our own, from previous years.

This year, the reconciliation that applies to the 2021-22 budget is higher than the current borrowing limit—somebody can correct me, but from memory it is about £319 million, which is higher than £300 million. It does not get more tangible than that. The only reason why it has not breached the borrowing limit this year is that a Scotland-specific shock due to a timing difference between our forecast and the UK Government's forecast allowed the resource borrowing limit to be temporarily increased. If anything, this year's position demonstrates why it is essential that we have had that temporary increase, which should perhaps be made permanent.

Does that give you enough of a tangible hook to hang the argument on?

Daniel Johnson: I would like to see the analysis, but I do not dispute the fundamental point. Any forecast will have a margin of error, and when our revenue is based on forecasting, it stands to reason that the borrowing limit should be in line with that margin of error. What I am interested in is the hard analysis of the quantum of that, and how far away the Scottish Government believes the borrowing limits are. You can take it as read that I understand that having a hard nominal limit does not make sense. The question is what the order of magnitude should be.

I will move on to an associated point that is, in a sense, almost more important. You said that you have faced an issue over the past year in understanding, once announcements have been made—forgive the shorthand—when you can bank them. I recognise that this is an exceptional year, but exceptions sometimes come along.

I have two questions. First, how indicative is that of a general issue with funding coming through the block grant, and the predictability of that? Secondly, what is the actual substance of that issue? Is it simply that the Scottish Government takes a cautious approach and wants the ink to dry on the bit of paper before it starts to action the funding, or is it that you do not know that you are definitely going to get the cash from the Treasury until it hits your bank account? I guess that there is a range of possibilities between those two points.

Again, if you have specific examples of where that has caused a problem and the amount of money has been lower than you anticipated, it would be useful to have those on the record.

Kate Forbes: In short, we are not cautious about getting money out to the people and the services that need it as soon as we can, but what has really exacerbated things during the year is the level of volatility. You will forgive me for stating some basics here, but I want to build up my argument.

The fact is that we cannot overspend our budget; at the end of the financial year, I have to bring to Parliament through the outturn statement a budget with no overspending, because the Treasury would not look kindly on us if we overspent. In-year budget management is all about trying to maximise spending power for the services that need it and to meet all the asks. After all, every day in Parliament, there is always another ask for more money.

At the same time that we trying to maximise that spending power, we have to come in on budget. The difficulty is that, during the year, there is volatility. For example, with the UK Government's announcement of health and social spend, we were told that we would get up to £520 million; that will be confirmed in the main estimates, which means that the final confirmed position will probably be known in January, February or March. If all that £520 million gets spent on the important services that it needs to be spent on—and we will spend that money; please do not read into what I am saying some lack of commitment to spending the money that needs to be spent—and we are told in January or February that we will get £400 million in consequentials, because the UK Government equivalent departments have not spent the full amount to generate the full £520 million or because it is recycled funding, I suddenly have a shortfall of £120 million that I need to make up with only a matter of weeks to go before the end of the financial year to ensure that our budget comes in on balance. That is the level of risk that we face.

Knowing that that is the position, we are managing our budget in year on a daily basis to maximise our spending power while at the same being cognisant of the fact that, once the money is spent, it is challenging to make up any shortfall. One actual example was a sum of £25 million for education. The UK Government announced some education funding, which was very welcome, and we passed that money on to education. However, when we saw the May estimates, we discovered that the actual funding was £25 million less. In other words, it was £25 million that I was not going to receive but which I had already passed on. This is not a complaint—it is a request for more levers to manage that kind of volatility and ensure that we come in on balance.

Last year, the Barnett guarantee made it clear that there would be no negative consequentials and that what had been announced would not be clawed back. I therefore had total reassurance that when the £25 million was announced it could be passed on without the fear that the actual sum might be less. The guarantee has been taken away this year, because the UK Government's volatility is such that it cannot predict with any certainty what UK departments will spend. That is why the increased volatility this year has made things very difficult. We manage that volatility internally, but it makes things more challenging and any Government in this role would find huge value in having more tools to manage it.

Daniel Johnson: I guess that with any budget process there will be external and internal volatility, but one of the corollaries of what you are saying is that you would find it useful if the UK Government were more transparent and predictable in the way that it followed through on its spending. If so, is the same true of the Scottish Government? I am thinking in particular of Audit Scotland's recent comments about transparency, and I was interested to see that in its recent report on these matters it said:

> "budget revisions are managed across Government, which means it is not always possible to establish the detail of reprioritisations within directorates."

To my mind, that sounds a little bit like the situation that you have highlighted with regard to the UK Government.

Is tracking budget changes in directorates an issue? Is there an opportunity to improve the systems that you have in place? Audit Scotland made the supposition that the data is there but you cannot report on it. I am thinking of your relationship with the UK Government and your own practice. Is there scope along those lines to improve transparency and disciplines in budget reporting?

Kate Forbes: I am certainly open to suggestions about, and we will give more thought to, how we can be more publicly transparent in the budget. However, a more mature debate about the realities of budgeting is required, because a lot of our budget is demand led. Budgets were demand led for some business support. If, for example, we announced that £50 million was available and only £40 million was spent, which exhausted demand, accusations that the budget was underspent would be made, but that is the nature of demand-led budgets.

Sometimes demand can exceed the budget that is allocated, so we must manage that, and sometimes demand is less than was forecast. Budgets are a moveable feast, and budget revisions—they usually happen twice a year, with the exception of the Covid period, when they have happened three times a year—are just a snapshot in time, and as much certainty as possible is required when we publish them.

You made a point about the UK Government. I am sympathetic to the UK Government's position that you cannot definitely say to the penny how much will be spent over a year at the beginning of a year or even at any point in a year, because who knows what might happen? Fuel shortages might happen or other events might need to be responded to. Budgets will always be slightly moveable feasts. My difficulty is not with budgets being a moveable feast but with having a fixed budget that must balance, which means managing a very volatile situation with very limited levers.

To go back to your question, if we can do more on transparency, I am open to that. If we can build more transparency into the budget revision process, I am open to that. I know that the committee will scrutinise that in the coming weeks, so your feedback from that could inform future budget revisions.

Daniel Johnson: I will just follow that up before I ask my final question. I am speculating about whether more robust, regular and detailed reporting through the year on budgets and spend from the UK and Scottish Governments might help matters. I totally accept that much of Government activity is demand led and that you cannot guarantee absolutely that you will spend a certain amount, but robust reporting and tracking help to manage the situation. That is true in the private sector—a business is dictated by whether customers spend money on its services. I would suggest that that is much less predictable than anything that the Government does. The question is whether such an approach would be an avenue for both Governments to improve things. That explains where I am coming from.

In recent weeks at committee, questions have been raised about outcome-led budgeting and where we are 10 years on from the Christie commission. Given that the medium-term financial strategy is under development prior to its publication, does that provide an opportunity to recast what the Scottish Government intends to do in the medium term on outcomes and objectives? Much of the written and oral evidence that we have received has noted that, unless objectives are baked into how the Government budgets and organises itself, such documents provide only commentary rather than drive change towards the objectives. Will you take such an approach? Can more be done in the MTFS and beyond that to bake objectives into how the Government budgets and organises itself?

12:00

Kate Forbes: If I were to summarise what you are saying, it is that our budget choices need to be aligned to the national performance framework. Sometimes, that will require difficult decisions as to where we put the money. For example, in the big debate about preventative spend, putting more investment upstream to change the outcomes is important. There is an opportunity to do that in a significant way with the resource spending review, because that will be multiyear. Most of the outcomes that we are talking about will not be delivered in the space of a year. For example, changing health and social care outcomes is a multiyear initiative and the resource spending review will allow us to look at how the compounding effect of multiple years delivers that change.

The challenge that I would put to you in return—I cannot recall whether I have spoken about this previously in this committee, or whether it was in the Local Government, Housing and Planning Committee—is that the nature of our debate in Parliament needs to reflect the magnitude of the choices. If we are to spend more money on active travel, it has to come from somewhere. If we want to recycle money from acute healthcare to spend on active travel—I am just using that as an example—we must have a mature debate. It is in that fashion that the Opposition must scrutinise, and the Government must present, where that penny is best spent.

We all know that funding supplies are not unlimited. If we think that it is important to invest in prevention rather than cure, that will require money to be shifted. Every time I stand up to present a budget that displays any reductions at all, those are immediately latched on to and criticised, so we need a mature debate. The Government certainly needs to be pushed by the Opposition to contend with those issues, and the Opposition needs to reflect that, too.

Daniel Johnson: That might be why I was asking questions about medium-term spending plans. I will gently conclude there.

The Convener: Disinvestment is always the key issue in terms of prevention. We will certainly look at that in the months ahead.

I have some short questions to finish off. The first is about the fiscal framework. We have touched a lot on issues about borrowing. Five years ago, when the fiscal framework was agreed at the 11th hour, the budget limits were set in stone. Since then, there has been a 9.2 per cent erosion due to inflation, so I take it that one of the Scottish Government’s asks in the review will be that any limits that are set should be index linked to inflation. Am I right?

Kate Forbes: At the very least, but basing limits on affordability rather than arbitrary caps would be my default position.

The Convener: We have talked about demographics, skills and jobs. The Government has a young person’s guarantee, but it is facing a reduction of 60,000 workers in the 16 to 64 age group between 2020 and 2026. What does the Government do to focus on the 55 to 67 age group, for example. They have a lot of skills and experience, and many of them are very reliable. How will the Government get back some of those people into the workforce or get them retrained?

Kate Forbes: The primary, but not the only, means of reaching that age group is the national transition training fund. That supports people who are unemployed, at risk of redundancy, or in need of upskilling or retraining. There are other schemes, including the no one left behind scheme, which is about supporting people who are furthest from the jobs market—for a whole host of reasons that we could go into—and helping them into work. There are a number of different schemes, but the one that I point you to is the national transition training fund.

The Convener: Finally, the health and social care levy on national insurance will impact on the public sector in Scotland to the tune of around £151 million, with £67 million going on the NHS and £31 million on local government. I believe that the UK Government will guarantee that amount. Have you had a guarantee that those consequentials of £151 million will come through?

Also, what impact will the levy have on the private sector, when it comes to economic and jobs growth in Scotland?

Kate Forbes: The UK Government has announced what money it thinks will be generated and therefore what will come in consequentials, but I encourage the committee to scrutinise what is finally announced, to ensure that the £1 billion—if it is £1 billion—is additional and not netted off elsewhere. That remains my concern, and we will not know the answer to that until 27 October.

It has been well documented that the national insurance increase will have an impact on private and public sector employers, as any increase in taxation will have. There is no doubt of that. Our job is to ensure that the money is used wisely and carefully.

Convener, I promised to provide an update on the small business bonus scheme, in response to Ross Greer’s question. Dougie McLaren says that he is happy to answer the question now, to save writing a letter. That is entirely at your discretion.

The Convener: Okay, but let me continue with my question. I was not asking about the spending for which the national insurance levy is being raised, which is for health and social care; I was asking about the impact of the levy on local government, for example, which collectively will have to pay £31 million to the Treasury. I understand that the UK Government has agreed that it will provide—certainly south of the border—the consequentials in that regard. Has that been guaranteed for Scotland, so that some of that £1 billion that you mentioned does not have to be fired back into local government, police and fire services and so on? That is what I was trying to get at; I apologise if I did not explain that clearly.

Kate Forbes: No, I apologise for not grasping what you were asking. We have had a lot of engagement with the UK Government on those points, and Dougie McLaren might be able to give you a brief update on whether there will be full compensation.

Douglas McLaren: The issue is compensation for the increase in public sector employer contributions, to which you alluded, convener. We have not yet had an assurance and we are trying to test the issue with the Treasury.

The Treasury's prevailing answer to all our questions about the matter is that we will get the detail and updates at the spending review later this month. As things stand, it looks as though what will come through is a consequential funding increase that is related to spend in the Westminster budgets, but the question for us will be whether that truly compensates—in the UK Government's parlance—for the need across public sector employers in Scotland. We do not have an assurance or detail on that yet; we will test it with the Treasury.

The Convener: Thank you. The second part of my question was about the implications of the national insurance increase for economic and employment growth in Scotland.

Kate Forbes: We are still trying to fully comprehend what the impact will be, particularly on economic growth. A lot of our attention has focused on the impact on employees, rather than on employers. Let us consider the example of the hotel on the Isle of Skye that was in the press over the weekend. The owners were lamenting the fact that VAT is increasing, that they cannot secure labour and that prices are increasing across the supply chain. The national insurance increase is clearly another issue for such businesses to contend with, on top of a number of pressures that they are facing.

The Convener: All of which are inflationary pressures.

Dougie McLaren, do you want to come in with your response to Ross Greer?

Douglas McLaren: Yes, thank you, convener. I was checking my notes on the matter. The Barclay review asked for the small business bonus scheme review to be concluded by 2022 and, as the cabinet secretary said, Covid interrupted the process. The Fraser of Allander Institute encountered practical problems, such as the need to get physical access to materials on university premises, but I think that the work is picking up again. We do not have an exact estimated time of arrival, but if I find out more from colleagues or the institute itself and can add anything, I will be happy to update the committee.

The Convener: Thank you for that.

We have exhausted our questions. Cabinet secretary, thank you for answering so many questions so comprehensively. I wish you a speedy recovery. I apologise for the broadcasting glitches, which you valiantly managed to get through; we were able to ask the questions that we wanted to ask.

That ends the public part of the meeting.

12:10

Meeting continued in private until 12:19.

Published in Edinburgh by the Scottish Parliamentary Corporate Body, the Scottish Parliament, Edinburgh, EH99 1SP

All documents are available on
the Scottish Parliament website at:

www.parliament.scot

Information on non-endorsed print suppliers
is available here:

www.parliament.scot/documents

For information on the Scottish Parliament contact
Public Information on:

Telephone: 0131 348 5000
Textphone: 0800 092 7100
Email: sp.info@parliament.scot