



Written views from the OECD to the Scottish Parliament’s Finance and Public Administration Committee on the Scottish Fiscal Commission’s first Fiscal Sustainability Report

Introduction

The OECD is pleased to provide written views on the Scottish Fiscal Commission’s (SFC’s) first Fiscal Sustainability Report. The views expressed are based on best practices drawn from OECD Member country experiences. Our submission is also informed by the OECD’s long and extensive involvement in this area, including the annual meetings of the *OECD Working Party of Parliamentary Budget Officials and Independent Fiscal Institutions (IFIs)*.

The OECD welcomes the Scottish Fiscal Commission’s first Fiscal Sustainability Report. The majority of OECD IFIs undertaken this type of assessment (74% of national IFIs and 50% of subnational IFIs) ([OECD, 2021](#)). In undertaking the [OECD Review of the Scottish Fiscal Commission](#) (2019), the OECD heard from a variety of stakeholders that there was a lack of analysis on fiscal risks and long-term fiscal sustainability in Scotland. In light of this, the OECD recommended that:

“... the Scottish Fiscal Commission should consider expanding its work on fiscal risks, with a view to developing long-term sustainability analysis in future.”

The independent Budget Process Review Group in Scotland had also previously recommended that budget scrutiny should have a long-term outlook and focus more on prioritisation, addressing fiscal constraints and the impact of increasing demand for public services ([Scottish Government, 2017](#)). The SFC’s first Fiscal Sustainability Report helps respond to these concerns.

Long-term fiscal sustainability has been a recurring theme at meetings of the *OECD Working Party*, and the OECD has published [Benchmarks for Long-Term Fiscal Sustainability Analysis](#) (2017) to support IFIs in undertaking this work. This publication was a first attempt to identify and classify a complete and comprehensive set of benchmark practices for IFI long-term fiscal sustainability analysis in OECD countries. These are used to provide the following high-level assessment of the SFC’s first Fiscal Sustainability Report.

High-level assessment of the SFC’s first Fiscal Sustainability Report

The SFC is not legally mandated to publish a Report on Fiscal Sustainability, but is doing so on its own initiative. This rests on the SFC’s ability to produce reports on a discretionary basis in relation to any “fiscal factors” it considers appropriate. Around two in five long-term fiscal sustainability reports by OECD IFIs are also self-initiated ([OECD, 2021](#)). In other OECD countries, the IFI is legally required to

publish long-term fiscal sustainability analysis, with this function being included in the IFIs enabling legislation. This can help ensure that the work is adequately resourced and also helps guarantee a certain frequency of reporting.

Overall, the OECD finds that analysis in the SFC's Fiscal Sustainability Report is in line with good practice by other OECD IFIs. Specifically:

- The Report identifies the “annual budget gap” as the key indicator of fiscal sustainability, an indicator that is clear and easily understandable.
- The analysis includes separate projections for spending and funding. Further decomposition of the projections for spending and funding into their main component parts helps promote awareness of the major cost drivers for expenditure as well as key factors that will impact tax revenues and other funding streams.
- The SFC plans to publish a report at least once in each five-year Parliamentary session. While there is not an established standard across OECD countries for the frequency of publication, common practice suggests reports should be published in intervals of five years or less, to effectively contribute to public and political discussion on this subject.
- Good practice is for the time horizon to assess fiscal sustainability over a period of 30 years or longer, with most analysis in OECD countries spanning 30-50 years. In line with this, the SFC's report spans 50 years.
- Key assumptions underlying the projections in the SFC's report are made explicit, and forward projections seem to be based on “realistic” assumptions.
- Scenario and sensitivity analysis is widely practiced by IFIs in long-term fiscal sustainability reporting. The SFC analysis provides a baseline projection, as well as one based on an alternative scenario where the United Kingdom Government responds to long-term fiscal pressures.

Because the SFC's Fiscal Sustainability Report is a voluntary publication, the resources dedicated to it – and thus the depth of analysis - may vary over time. If the SFC has sufficient resources to further develop its Fiscal Sustainability Report in the future, it may wish to consider incorporating leading practices from similar analysis in other OECD countries. For example:

- In addition to budgetary and economic analyses long-term sustainability analysis, the SFC may wish to include analyses of the distributional impacts of various long-term fiscal scenarios. This might include highlighting the distributional implications of fiscal policy for different age cohorts. For example, one of the aspects assessed by the Slovak Council for Budget Responsibility (CBR) in connection with the long-term sustainability of public finances is intergenerational fairness. The CBR quantifies the net contribution to/receipt from public finances of individual age cohorts. For this purpose, generational accounts are used, allowing the CBR to estimate the magnitude of fiscal expenditure or revenues for individual age cohorts during their lifetime.
- Presenting the fiscal implications of other potential fiscal pressures, including natural resource depletion, trade or technology changes that may affect the economy, or climate change. This could be part of a larger report on fiscal sustainability that also identifies fiscal risks. For example, the United Kingdom Office for Budget Responsibility (OBR) has recently combined its two biennial reports on long-term fiscal sustainability and fiscal risks into a

single annual report on Fiscal Risks and Sustainability. The most recent report includes an assessment of the fiscal risks from higher medium-term fossil fuel prices and potential fiscal implications of long-term changes in energy supply and demand, taking account of the UK's decarbonisation objectives ([OBR, 2022](#)). The SFC has already indicated that "In other years we intend to publish papers looking at the fiscal sustainability in more specific areas, such as climate change, health and child poverty" ([SFC, 2023](#)).

- Highlighting how different tax and spend policies can affect the economy. For example, the United States Congressional Budget Office (CBO) estimates the macroeconomic and budgetary effects of various fiscal policies, to illustrate how federal tax and spending policies can affect the economy. The CBO examines how economic growth is affected by policy through many channels, including marginal tax rates on labour and capital income, transfer payments to working-age people, and federal investment.
- Highlighting the long-term fiscal costs of past and possible future policy changes. For example, both the CBO and the Korean National Assembly Budget Office (NABO) estimate scenarios to highlight policy options to obtain a hypothetical fiscal objective along various fiscal paths and scenarios. In Korea, NABO presents a menu of revenue and spending options disaggregated by functional area and time horizon. By highlighting various "paths" to sustainable finances, IFIs can illustrate to parliamentarians and stakeholders the opportunity costs of delayed fiscal policy action.
- Featuring broader international comparison. The SFC's report draws comparisons with similar analysis undertaken by the United Kingdom OBR. A broader range of international comparisons could provide helpful context for readers to interpret forecast inputs and the reasonableness of analysis included in long-term fiscal sustainability reports.
- Presenting a more detailed overview of the public finances at the local authority level of government. Long-term fiscal sustainability analysis encompassing central and subnational levels of government provides essential context for a debate on budgetary choices. For example, Canada's Parliamentary Budget Officer separately assesses the fiscal sustainability of Canada's federal government, subnational governments and public pension plans.