Finance and Public Administration Committee

4th Meeting, 2021 (Session 6), Tuesday 14 September 2021

Pre-budget scrutiny 2022-23

1. At this meeting, the Committee will take evidence as part of its pre-budget scrutiny 2022-23 from two panels of witnesses as follows—

Panel 1:

- Councillor Gail Macgregor, Resources Spokesperson, COSLA;
- Alan Russell, Director of Finance at Renfrewshire Council and Chair of Chartered Institute of Public Finance Accountants (CIPFA) Directors of Finance Section; and
- Linda Somerville, Deputy Secretary General, STUC.

Panel 2:

- David Eiser; Senior Knowledge Exchange Fellow, Fraser of Allander Institute;
- Susan Murray, Director, David Hume Institute; and
- Ray Perman, Fellow, Royal Society of Edinburgh.

2. Written submissions from these witnesses are attached at Annexe A. Members should note that a joint submission was received from COSLA, CIPFA and SOLACE (Society of Local Authority Chief Executives).

Recent Developments

UK Spending Review 2021 and Autumn Budget

3. The Chancellor of the Exchequer, on 7 September, launched 'Spending Review 2021' which will conclude on 27 October 2021 alongside an Autumn Budget. The three-year review will set UK government departments' resource and capital budgets for 2022-23 to 2024-25 and the devolved administrations' block grants for the same period (subject to annual adjustments as provided for in the Fiscal Framework).

UK-wide Health and Social Care Levy

4. The Prime Minister wrote to the First Ministers of Scotland, Wales and Northern Ireland and the Deputy First Minister of Northern Ireland on 7 September following the announcement of the introduction of a new UK-wide Health and Social Care Levy. The letter states that “the devolved administrations will benefit from Barnett consequentials from this spending (on the NHS and social care in England) in the usual way.”

5. The letter further states that “combining Barnett funding and UK-wide spending, by 2024-25 Scotland will benefit from an additional £1.1 billion.”

6. The Prime Minister’s letter can be accessed via the following link: Letter_from_the_Prime_Minister_to_the_First_Ministers_of_Scotland__Wales_and_Northern_Ireland_and_Deputy_First_Minister_of_Northern_Ireland.pdf (publishing.service.gov.uk)

Pre-Budget Evidence to the Committee

7. The Committee’s pre-budget scrutiny continues work undertaken by its predecessor Committee in Session 5 on the impact of COVID-19 on the public finances and the Fiscal Framework[1].

8. The Committee issued a call for written views over the summer in which it sought responses on how the Scottish Government’s budget in 2022-23 should address the following questions—

    - How should the Scottish Government's Budget for 2022-23 address the need for a fair and equal recovery from the Covid crisis?

    - How should the Scottish Government’s Budget address the different impacts of the pandemic across age, income and education groups and across places?

    - In 2022-23, it is likely that there will be reduced levels of available Covid-related financial support for the public and private sector. Given this, what should be the priorities for the Scottish Government’s Budget?

    - How should the Scottish Government Budget in 2022-23 address the risks arising from the level and rate of recovery from the pandemic in Scotland relative to the rest of the UK? Please consider any impact on devolved tax receipts and social security benefits in your answer.

    - How has the Fiscal Framework worked in managing response to the crisis?

[1] https://www.parliament.scot/parliamentarybusiness/CurrentCommittees/115076.aspx

- How should learnings from the pandemic inform the forthcoming review of the Fiscal Framework?

9. The call for views closed on 13 August 2021 and a total of 45 responses were received. All submissions can be accessed on the Committee's website via the following link: Published responses for Scotland's public finances in 2022-23 and the impact of Covid-19

10. A summary of written evidence has been produced by the Financial Scrutiny Unit in SPICe and is available on the Committee's website.

11. The Committee previously took evidence to help inform its pre-budget scrutiny from the Scottish Fiscal Commission and the Cabinet Secretary for Finance and the Economy at its meeting on 31 August. The meeting papers and official report are available on the Committee's website: Finance and Public Administration Committee 2nd Meeting, 2021

12. The Committee then took evidence from two panels of witnesses at its meeting on 7 September. The meeting papers and official report are also available on the Committee's website: Finance and Public Administration Committee 3rd Meeting, 2021

Next steps

13. The Committee is expected to hold its final pre-budget scrutiny session with the Cabinet Secretary for Finance and the Economy before October recess. A session with the Auditor General for Scotland on Audit Scotland's 'Tracking the implications of Covid-19 on Scotland's public finances' report, expected to be published mid-September, will also inform this session with the Cabinet Secretary. The Committee is then expected to publish its report on its pre-budget scrutiny in early November.

Finance and Public Administration Committee Clerking Team
September 2021

ANNEXE A

Submission from COSLA, SOLACE and CIPFA Directors of Finance

COSLA *is a Councillor-led, cross-party organisation which champions Councils' vital work to secure the resources and powers they need. COSLA works on Councils' behalf to focus on the challenges and opportunities they face, and to engage positively with Governments and others on policy, funding and legislation. We're here to help councils build better and more equal local communities. To do that we want to empower local decision making and enable Councils to do what works locally.*

SOLACE *is the Society of Local Authority Chief Executives. SOLACE's membership includes all 32 local authority Chief Executives in Scotland, each responsible for leading multi-million pound organisations and thousands of employees, providing a huge range of essential services to the entirety of Scotland's population.*

CIPFA ***Directors of Finance Section*** *works closely with COSLA in leading strategic discussions with Scottish Government around funding and distribution for the essential services and policy areas that Councils deliver on. Members of the Section are those who have responsibility for the overall financial functions across all 32 Local Authorities.*

Introduction

1. COSLA, SOLACE and Directors of Finance Section are pleased to present a joint response to the Finance and Public Administration Committee's call for views on Scotland's public finances in 2022-23 and the impact of COVID-19, as part of its pre-budget scrutiny.

2. We note that the Committee is particularly interested in views on the ongoing fiscal response to the crisis and how to support a fair and equal economic recovery while addressing the financial cost of the pandemic. Our response therefore seeks to address these points from a Local Government perspective.

3. We previously presented evidence to the former Finance and Constitution Committee for its 2021-22 pre-budget scrutiny on the Impact of COVID-19 on the Scottish Government Budget, which can be found here and the follow up letter to the Committee here. Whilst much of what we said then still stands, particularly around the financial challenges to Local Government; how Local Government responded to the Covid crisis; and our views on a Fiscal Framework for Local Government to complement the Scottish and UK Government's Fiscal Framework. That evidence went into some detail on these areas, so in our response to the Committee's questions below, we have sought to highlight key considerations reflecting the current state of play.

Summary of Key Points in the Submission

- There needs to be fair funding in the Scottish Budget to Local Government. Whilst there has been much focus on the role of the NHS in dealing with the pandemic, with the promise of significant levels of investment, this must not come at the expense of critical services which Local Government needs to continue to provide in recovery and tackling poverty and inequality.

- The establishment of a new National Care Service as proposed by the Scottish Government is a distraction from recovery which will take resources, time and capacity away from service delivery at the time we would wish to see a significant investment.

- Local Government needs absolute flexibility to manage funding locally and to respond to need, rather than be pressed into areas of specific spend or to be limited to using funding by an artificial deadline or within a financial year.

- Investment in infrastructure, alongside investment in services, needs to be at the forefront of the Scottish Government's thinking on the Scottish Budget.

- If Local Government is to play its part in achieving net zero emissions, then both revenue and capital funding is needed, alongside policy/ legislative levers to act effectively, integrating carbon reduction into Councils' mainstream service delivery, as well as through dedicated initiatives.

- Targeting resource where the pandemic has hit society hardest is a more effective and value for money use of resource and, where policies are universal, they must be fully funded to enable Local Government to deliver these polices.

- There needs to be a whole system thinking about health and wellbeing, across the public sector. The key social determinants of health of education, housing, employment are all drivers behind long term health and must be invested to improve health outcomes and address health inequality.

- Work on a Local Government Fiscal Framework should tie into reform of the Fiscal Framework system as a whole and should provide a fair and equal basis across the fiscal landscape in Scotland.

1. How should the Scottish Government's Budget for 2022-23 address the need for a fair and equal recovery from the Covid crisis?

Investment is needed to support recovery

4. The Scottish Government's Budget for 2022-23 will need to fully recognise the importance of Local Government services in supporting communities to recover from the Covid crisis and to tackle poverty and inequality. Crucially there will need to be a strong focus on community and economic recovery for which Local Government will need to be resourced to play its part. Councils are major employers in themselves and also play a key role in terms of local economies, commissioning and procuring services, creating jobs and providing employability services to support people into work. The pandemic has starkly exposed and exacerbated the inequalities within our society and, to achieve a fair and equal recovery, significant long-term investment is needed in our communities, focused on addressing these.

5. In order to be able to support community and economic recovery, there needs to be fair funding in the Scottish Budget to Local Government. Whilst there has been much focus on the role of the NHS in dealing with the pandemic, with the promise of significant levels of investment, this must not come at the cost of critical services which Local Government needs to provide in recovery. Recently published research[2], based on English Councils, indicates that cuts in funding for Local Government might in part explain adverse trends which have emerged in life expectancy. Equally, Councils must prioritise areas such as education at the expense of other core Local Government services which also have a key influence on the social determinants of health and have the potential to improve wellbeing and deliver upstream intervention, which ultimately takes the strain off the NHS. Services including leisure and sports facilities; waste collection; homecare and homelessness prevention; and provision of community hubs, offer security to communities and contribute significantly to peoples' daily wellbeing. COSLA together with Public Health Scotland has produced a briefing on the positive contribution of physical activity and sport to Scotland, through a cross policy lens, which stresses the importance of physical activity for wellbeing. The briefing can be found here

6. Demand for social care is likely to increase and potentially change as result of the pandemic as we see more people who may be affected by the long-term health and social impacts of the pandemic. This goes hand in hand with the desire to support people to stay in their own homes, which for those with complex needs is frequently more costly to provide. Alongside this, services such as environmental health, trading standards and local economic development help to ensure safe and growing inclusive economies. Historically these are the services which have faced reduced funding when difficult local

[2] https://www.thelancet.com/journals/lanpub/article/PIIS2468-2667(21)00110-9/fulltext

decisions have had to be made, and there is a real risk that these services will be diminished further if there is not a fair funding settlement for Local Government. A wider view of targeting funding to improve health is therefore required. It is important that this investment is in outcomes rather than creating new structures. The establishment of a new National Care Service, as proposed, is a distraction from recovery which will take resources, time and capacity away from service delivery at the time we would wish to see a significant investment.

Flexibility to respond effectively to ongoing impacts of COVID

7. Whilst the funding provided by the Scottish Government to address the impact of Covid is welcomed, this funding is largely one off and does not address the underlying need for the continuing resourcing of core services delivered by Local Government. Fundamentally, there needs to be a recognition that the crisis is far from over and, for many people, as support like furlough comes to an end and Universal Credit is limited to pre-Covid levels, inequality and lack of opportunity will increase. There is a very real risk that the sorts of financial intervention seen during the pandemic to support low-income households will not be replicated, whilst the crisis will be ongoing for many people.

8. We are yet to see to what extent there will be a rise in unemployment and the potentially disproportionate effect on levels in Scotland. With the substantial packages of financial inclusion support set to come to an end, the question is what will be there to respond to the ongoing crisis? COSLA believes that this is not the time to switch from crisis management, as a crisis response “mode” will be required for several years to come. For instance, additional funding for the Scottish Welfare Fund during 2020-21 is not set to continue for 2021-22 and beyond, at a time when the Fund is likely to come under significant pressure from those needing support during the recovery phase. At the same time Local Government needs to invest in preventative activities if we are to address matters such as inequalities over the longer term. Councils currently have to call on reserves to deal with the ongoing crisis, however this is one off funding and there needs to be thinking about responding to crisis over a longer term. Further comments are made about Councils’ reserves under question 4.

9. Local Government needs absolute flexibility to manage funding locally and to respond to need, rather than be pressed into areas of specific spend or to be limited to using funding by an artificial deadline or within financial year. The outcomes that were jointly agreed in the National Performance Framework (NPF) should govern how well Local Government’s performance is measured and a much greater focus on how Local Government is achieving over 60% of priorities in the NPF, rather than the current landscape of siloed pots of national funding, with micro-management of each. A more strategic approach is also required to enable Local Government to address the inequalities with our communities in a holistic manner. Ministerial engagement must demonstrate respect for Local Government and for Ministers to trust Councils to get on and do the work they were democratically elected to do.

Investment is needed in infrastructure

10. Investment in infrastructure, alongside investment in services, needs to be at the forefront of the Scottish Government's thinking on the Scottish Budget. Local Government has experienced significant reductions in its Capital settlement over the last 2 financial years and, in its five-year Capital Spending Review, the Scottish Government is indicating that the currently reduced position for Local Government will be broadly maintained. This fails to recognise that Local Government is facing serious Capital budget challenges which are exacerbated by the pandemic, with the continued provision of modern and well-maintained amenities such as community and leisure facilities under serious threat. This is exacerbated by cost increases of building materials and expected higher national standards, for example in building affordable housing. There is evidence to demonstrate that the quality of housing and overcrowding has a direct impacts on peoples' health and wellbeing – household size has been found to be factor in both infection and mortality rates[3] during the pandemic.

11. It should be stressed that investment in infrastructure also requires ongoing and sustainable revenue funding to operate and maintain facilities which communities depend upon into the future.

Investment is needed in addressing the impacts of climate change

12. Local Government has a key locus in transition to a low carbon economy and combating the adverse impacts of climate change. This applies to Local Government's own estate, such as modernising buildings and vehicles, where greater investment is needed. It applies equally across all areas of Local Government intervention including heat, transport, planning, education, economic development, place and waste. Local Government needs the resources and policy/legislative levers to act effectively, integrating carbon reduction into their mainstream service delivery, as well as through dedicated initiatives. Critically if Local Government is to play its part in achieving net zero emissions, then revenue funding together with capital investment is needed. The recent report by the IPCC[4] evidences starkly how urgent the problem is, if significant changes and investment in infrastructure are not implemented at rapid pace, global warming will be greater and even more damaging.

2. How should the Scottish Government's Budget address the different impacts of the pandemic across age, income and education groups and across places?

[3] https://www.health.org.uk/publications/reports/unequal-pandemic-fairer-recovery pg.27
[4] https://www.ipcc.ch/report/ar6/wg1/

Place-based inclusive approaches are needed

13. The Covid pandemic has had a whole range of impacts on communities which require different approaches to address. Impacts have been felt across the whole of our communities, but these impacts have not been felt equally across or within them. Key impacts have been on children and young people's education; mental health; and poverty and inequality. In order to deliver the different recovery measures across communities, Councils will look to use well established place-based approaches. These range from improving places and place-based regeneration, such as bringing buildings back into use in town centres and improving the wider public realm, to supporting and working with communities to make places more liveable. This is often directly linked to social care and community care – building resilience and services within communities which enable people to stay within their own homes and communities and experience better outcomes. However, Councils will need to be resourced to do this and to be able to tailor solutions to individual and community circumstances.

14. Responses need to be developed around a whole family approach, so funding should allow flexibility for this and not be, for example, siloed by age. There are some very real examples in employability with, for instance, the Young Person Guarantee not currently being treated as part of the wider No One Left Behind approach to employability (which COSLA is jointly signed up to). Additionally, stripping out services and budgets, for example adult socal care, children's services and criminal justice, risks destabilising the whole system and will cause disruption, when the focus should be on improving outcomes and addressing the inequality embedded in our society.

Targeted support works better then universalism

15. Recent Scottish Government policy announcements, including those set out in the SNP manifesto's "100-day commitments", have tended to favour universalism (free school meals, free music tuition, abolition of curricular charges, free bus for under 22s). Very often these are prescriptive pots of specific policy-related funding which tend not to recognise place and the needs of individuals. COSLA would argue that, particularly while it is limited, targeting resource where the pandemic has hit society hardest is a more effective and value for money use of resource and that, where policies are universal, they must be fully funded to enable Local Government to deliver these polices.

16. Furthermore, Social Care reform must focus on what needs to be delivered and not the structures to deliver this. The wider contributors to improving health must also be recognised within this context including housing, education, employment and a resilient community which can support people. The impact of the pandemic on older people in care has been disproportionately severe. However, this stems just as much from historic under-investment in adult social care as it does from the disproportionate impact of Covid on older vulnerable people. The Independent Review of

Adult Social Care estimated that investment of an additional £436m would be required to address unmet need of those who do not currently have access to social care who would benefit, compared to the level of access in 2009/10. This unmet need exists despite a real-terms increase in expenditure by Councils and Integrated Joint Boards of 7% since 2009/10.

17. Councils continue to deliver a wide range of care services; however, these are very often constrained by lack of resources, often with difficult choices being made after assessment of care needs, focusing on higher priority cases only and which may mean the desired service is not available. The burden of unpaid care, and its disproportionate reliance and impact on women is a very real issue that requires attention – more women have been furloughed, reduced hours or stopped working due to increased care requirements caused by the pandemic. This will have significant long-term economic impacts and is likely increase inequality further.

3. In 2022-23, it is likely that there will be reduced levels of available Covid-related financial support for the public and private sector. Given this, what should be the priorities for the Scottish Government's Budget?

18. The funding which has been provided for responding to the Covid pandemic has been critical to ensure people and businesses have been supported during a time of unprecedented crisis. Councils have been at the forefront of delivering these supports. With the right level of resources, Councils are equally well placed to deliver on economic recovery and people and place focussed recovery. What is required, however, is that Local Government is provided with the necessary tools, with a greater focus on partnership and collaboration and flexibility to use fiscal tools, without central direction. Local Government needs stability and certainty to the resources it requires to support communities and deliver essential services. There needs to be a greater focus on longer-term strategic issues for Local Government Finance, to ensure that Councils' key role in recovery can be maximised and leveraged to address the increased inequality within our society.

19. There needs to be whole system thinking about health and wellbeing, not just funding for NHS, something which COSLA has long called for. The key social determinants of health of education, housing, employment are all drivers behind long term health and must be invested to improve health outcomes and address health inequality. Continuing with the current inflexible approach mitigates against the ability to tailor solutions locally or allow for investment and innovation where it is needed. As an example, a Council has cited that it had funding to address period poverty, however as this was ring-fenced the Council was unable to be flexible and use part of the funding to combat domestic abuse, despite these issues both affecting women and girls from lower income

households and being interrelated.

20. Similarly, Councils have a key role in creating ‘net zero places’ and driving and facilitating change in their local areas. Any action on climate change is inextricably linked to the natural environment, human health and wellbeing, and the economy. Councils have powers and are looking at measures like low emission zones, however these come at a financial cost in order to enforce measures.

4. How should the Scottish Government Budget in 2022- 23 address the risks arising from the level and rate of recovery from the pandemic in Scotland relative to the rest of the UK? Please consider any impact on devolved tax receipts and social security benefits in your answer.

21. There are significant risks that widening health inequalities, increased levels of poverty and, specifically, child poverty, will be felt to a greater extent in Scotland relative to parts of the rest of the UK. The Poverty and Inequality Commission’s Report[5] to the Scottish Government in June 2021 stated that child poverty rates are at best stagnating and may actually be beginning to rise. These concerning statistics are emerging even before the full impacts of the pandemic are felt. There will need to be significantly greater action needed to meet child poverty targets. Local authorities will play a leading role in seeking to address child poverty and will look to work collaboratively with the Scottish Government and partners. Taking children’s services into a National Care Service will disrupt well established partnerships and key approaches to tackling child poverty as well as impact on the delivery of The Promise. As a key part of this there is an opportunity to look again at how the fiscal framework including devolved taxes can support recovery, focussing on inequality and child poverty.

22. There is a question over how well targeted and affordable the currently devolved social security powers are. For instance, the £10 Scottish Child Payment, which includes low-income criteria, is an example of an intervention that addresses a symptom of poverty but not the cause. Councils have substantial local knowledge of what interventions can work best to support financial inclusion, so the devolved powers should seek to utilise that close knowledge of needs within communities.

23. Alongside the devolved taxes and social security powers which the Scottish Government controls, there is a question around Council Tax. Reform or even replacement of Council Tax to make it a fairer tax, or to have a fairer alternative, have been ‘on and off’ the political agenda for some considerable

[5] https://povertyinequality.scot/publication/poverty-and-inequality-commission-child-poverty-scrutiny-report-2020-21-report-to-scottish-government/

time. How revenue is raised is just as important to addressing inequality and ensure a human rights- based approach, as how it is spent. There is no question that a more progressive local tax would introduce greater fairness and equality into the system of tax revenue to fund Local Government services. However even a reformed local tax may not make it more local. Currently Council Tax is a nationally controlled tax in all but name, with the Scottish Government having re-introduced a Council Tax freeze for 2021/22, having capped the levels of increase in recent years to 3%. Council Tax Reduction is also nationally controlled, unlike in England; however, it provides a vital lifeline to low-income households. An outcome of responding to the risks to how recovery will fare in Scotland relative to the rest of the UK, should therefore be to look again at Council Tax reform including Council Tax Reduction. This should take account of Local Government's ability to raise revenue locally and to use local taxation to respond to local needs.

5. How has the Fiscal Framework worked in managing response to the crisis?

24. The Fiscal Framework has ensured that consequential funding under the Barnett formula has flowed to Scotland. However very often funding came at short notice, both from the UK Government and then following Scottish Government decisions on utilising the consequential funding. Transparency was an issue throughout the process – and there was often a lack of early and effective engagement with Local Government. Little opportunity was afforded to consider whether funding could have been used more effectively to support those who needed it most. As we moved through 2020/21 and into 2021/22, the Scottish Government became much more willing to provide Covid funding as general revenue grant, with only very light touch reporting, which has been welcomed. COSLA would argue that this sets a good precedent for funding recovery, whereby Councils are able to use discretion and be flexible in responding to the range of local needs.

25. However, much funding was awarded very late in the financial year. COSLA wrote to the Local Government and Communities Committee on 3rd March to put on record the impact that this would have and the position in relation to Councils reserves, which can be found on our website. This set out clearly the reasons why Councils hold reserves, what Councils could and could not do to utilise reserves to offset the financial pressures caused by Covid; and that reserves would necessarily increase due to the late notification of a considerable portion of Scottish Government Covid funding. Equally, following the Scottish Election and the Scottish Government's delivery of the "100-day commitments", this has unfortunately seen a reversal in approach in the way Scottish Government chooses to fund some Local Government services. This has resulted in a number of different funding pots each of which are micromanaged and disjointed in their policy aims and delivery, such as removal of fees for instrumental music tuition and play parks refurbishment, both of which have historically been up to local discretion. Added to this is a shift toward universality over targeted funding, such as lifting instrumental music

tuition fees, where Councils were already targeting free tuition to children of low-income families.

26. Whilst reserves are high in relation to Covid monies carried forward, this is not a substitute for core recurring funding. There is a risk that the level of reserves is interpreted as less funding being required - this is not the case. Local Government will be dealing with the legacy of the pandemic in years to come and resource will continue to be required for this.

27. Local Government had a primary role in supporting businesses and communities (business grants; pandemic payments etc), the funding for which came from UK consequentials passed on by the Scottish Government, with around £1.3bn of support provided during 2020 and a further £1.2bn since the start of 2021. Whilst Councils have primarily acted in an ‘agency’ role on behalf of the Scottish Government in delivering these supports, Council officers have nonetheless been closely involved in co-design, often with short notice following Ministers’ announcements. This has required considerable effort by Council staff to bring about delivery of much needed support to businesses and communities with the minimum delay. Earlier dialogue and engagement would have helped to deliver these supports more effectively, with the result that a huge extra effort was therefore required.

6. How should learnings from the pandemic inform the forthcoming review of the Fiscal Framework?

Longer term certainty is required at all levels

28. The devolution of tax powers to the Scottish Parliament has introduced a higher level of risk and uncertainty around the assumptions required to deliver a Budget. The nature of the current UK Fiscal Framework, by which the Scottish block grant is adjusted for the retention of devolved taxes in Scotland, means that these risks can only remain at a Scottish Government level. Fundamentally the relative difference in earnings growth and the composition of taxpayers in Scotland compared to the rest of the UK, which is a key feature of the current block grant adjustment mechanism, suggests an inherent unfairness in Scotland’s disfavour. For instance, for 2020/21 Scottish income tax policy generated just £46m more than the deduction for the BGA, with around half of Scottish taxpayers receiving higher tax bills, with no additional spending power for the Scottish Budget. Effectively the Scottish economy needs to outperform the UK as a whole, in order for tax policies (aimed at increasing revenues) to provide maximum benefit to Scotland.

29. The existing arrangements are also influenced by uncertainty in estimates of tax revenues caused by the timing of the UK and Scottish Budgets, which has tended to discourage the Scottish Government from setting multi-year budgets. The lack of multi-year budgets has knock-on impacts on the effectiveness of the whole public sector to plan and implement systematic changes aimed at tacking inequalities and improving outcomes across

Scotland.

30. Fundamentally there needs to be a re-setting of relationships across the UK Government, Scottish Government and Local Government, such that there is greater focus on what can be achieved over the longer term for our communities. This is not achieved through being the recipients of one-year financial settlements. The ability to plan and think outwith 1-5 year time horizons is needed, with all spheres of Government playing an effective and equal part.

Recognition of the whole fiscal landscape in Scotland is needed

31. The forthcoming review of the UK Fiscal Framework should address the relative disbenefits to Scotland by taking greater cognisance of the structural differences in the Scottish and UK economies and to encourage greater innovation in tax policy, rather than mitigating against this. The current Framework does not recognise the interplay between Scottish and local fiscal powers and needs to take account of the whole fiscal landscape, including local fiscal empowerment. Work on a Local Government Fiscal Framework should tie into reform of the Fiscal Framework system as a whole and should provide a fair and equal basis across the fiscal landscape in Scotland.

32. As an example, the Scottish Government is likely to seek increased borrowing powers as part of the review of the Fiscal Framework, with a loosening of conditionality. However, at the same time Local Government finds that it is being hampered in seeking to maximise flexibility in how it accounts for its own Capital borrowing. Local Government proposals for a more flexible approach to the longer- term accounting treatment of Local Government assets (service concession approach), which was offered to assist Councils in the short term to help manage the financial impacts of Covid. With the Scottish Government wishing to tie in these proposals with a wider review of Local Government Capital accounting, this acts counter to Local Government’s ability to use local fiscal flexibility.

33. This is not merely an accounting exercise- it has genuine implications for funding Local Government services into the future, whereby Councils have argued that extending the reach of the service concession regulation over the medium to longer term is both in accordance with good accounting practice and gives greater fiscal ability to finance the delivery of local services. Any changes in this area which removed statutory mitigation will impact on what Councils can afford to invest in even if transitional arrangements are put in place. Councils take a long-term view of what is affordable to invest in and it is imperative that at this critical time that the capacity to invest in assets is not eradicated as a result of an optional change in accounting practice. This is linked to the need for Councils to play an active role in economic recovery and be able to invest in assets, deliver on net zero and create employment opportunities.

Submission from the Scottish Trades Union Congress (STUC)

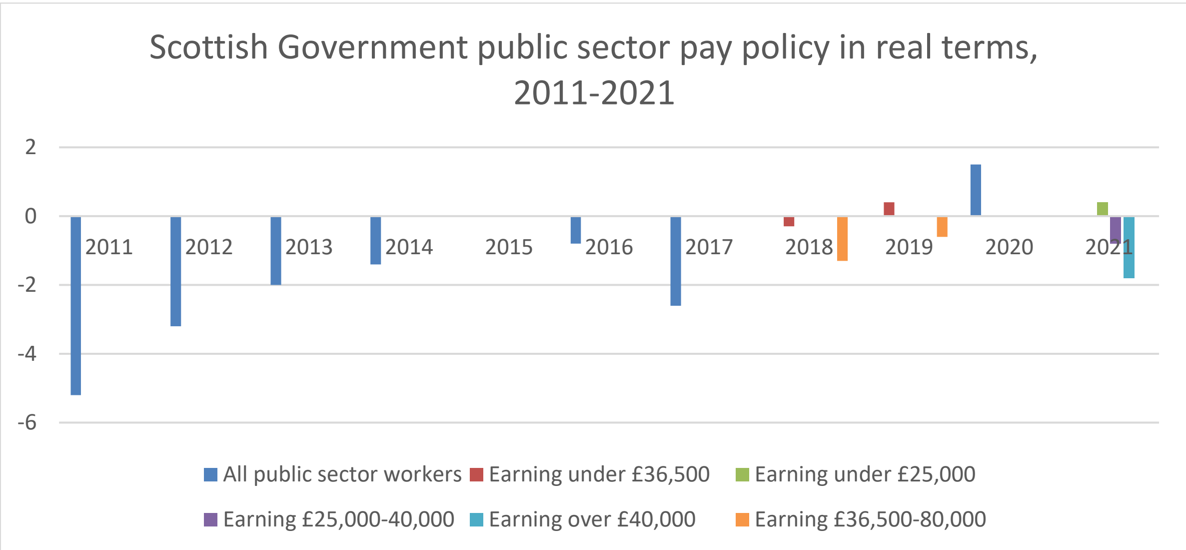
How should the Scottish Government's Budget for 2022-23 address the need for a fair and equal recovery from the Covid crisis?

The Budget must take action on pay, action on care and action for jobs.

Action on Pay

The people that have kept our society going over the last 18 months are not hedge fund managers or millionaires. They are cleaners, carers, nurses, supermarket workers, cleansing workers, delivery workers and postal workers. They are low-paid, predominantly women, keyworkers who have risked their health and wellbeing to keep us safe, and continue to do so.

Half of Scotland's keyworkers are in the public sector and yet, since 2011, public sector pay policy has lagged behind inflation. The table below, produced in March this year, shows public sector pay policy in real terms.



Author's Analysis based on public sector pay policy and RPI inflation. Note: 2021 inflation is forecast not actual. Local Authority settlements may differ, given Local Government funding has been disproportionately cut during this period.

Cumulatively, Scotland's public sector workers have seen a real term loss in wages of 15%. For the typical public sector worker, this is equivalent to a loss of more than £4,000 over the last decade.[i] Restorative pay settlements would not only help properly valued keyworkers but they would also:

- **Reduce the gender pay gap**. Women are twice as likely to be key workers than men.[ii]
- **Reduce in-work and child poverty**. As well as being relatively low earners, many keyworkers work part-time and live in single-parent households – risk factors associated with both in-work poverty and child poverty.
- **Support inclusive growth.** Low-earners spend more in the local economy than high-earners and a high proportion of key workers live in Scotland's more rural, remote areas and deprived areas.[iii]
- **Raise revenue**. An estimated 40% of the cost of a public sector pay increase would be recouped in tax revenue.[iv]
- **Support family resilience**. 46% of key workers with children have a partner who is in non-key work.[v]
- **Support equality**. Black and minority ethnic (BME) employees are more likely than white employees to be key workers.[vi]

Action on Care

The Independent Review of Adult Social Care by Derek Feeley called for 660 million of further investment into the social care system. The dedication and hard work of social care staff needs to be matched with nationally agreed terms and conditions that value the skills of the workforce. This can only be achieved through investment by the Scottish Government and collective bargaining with the trade unions who represent care workers.

Improving pay and conditions through collective bargaining and creating a National Care Service that sits within the public and not for profit sectors, must be a priority for the Scottish Parliament.

Action for Jobs

We need investment in good quality jobs as part of a green recovery.

While furlough has helped stave off mass unemployment, the number of people claiming unemployment related benefits and youth unemployment remain up, and overall working hours significantly down, on pre-pandemic levels. STUC research published in April estimates the cost of youth unemployment could be £2.4 - £3 billion in lost wages for Scotland's young people.[vii] Alongside the Youth Guarantee, the Scottish Government should invest in public sector job creation schemes and green apprenticeships.

We also need to ensure that jobs created are good quality jobs. Companies are using covid as a pretext to attack terms and conditions, including through the insidious use of fire and re-hire practices. Any Government support should be contingent on providing good quality, unionised jobs.

At the same time as we face a jobs crisis, we face a climate crisis. Over the next ten years Scotland will need to change how we produce our energy, construct our buildings, transport our people, manufacture our products, grow our food, and process our waste. There may be a lack of jobs, but there is no shortage of work to be done.

STUC research shows up to 367,000 green jobs could be created but this requires a policy programme based on large sums of public investment, much greater levels of public ownership and an industrial strategy for a Just Transition.[viii] Poor policy choices could see less than 131,000 jobs being created. Rather than simply providing pots of funding, we need a street-by-street home retrofitting programme, funded nationally but directly delivered by local authorities; a publicly-owned energy company that designs, builds and generates renewable energy; and our buses need to be taken back into public control with free bus travel piloted in our major cities. We also need to massively expand publicly owned housing and protect private renters with rent controls.

How should the Scottish Government's Budget address the different impacts of the pandemic across age, income and education groups and across places?

Age

It is hard to underestimate the cost of youth unemployment. An average 18-21 year old in Scotland who's unemployed for a year is estimated to lose £57,000-£77,000 over the following 20 years.[ix] That's equivalent to billions of pounds in lost earnings for Scotland's young people. Alongside the Youth Guarantee, the Scottish Government should invest in local authority-led public works programmes and green apprenticeships.

Income

We know that lowest earners have been hardest hit by the pandemic.[x] Meanwhile, STUC research published in April shows that Scotland's fund management sector, high-income households and property owners are the big winners from covid-19 and that a significant proportion of Scottish Government financial support has flowed to banks, landlords and utility companies.[xi] The Scottish Budget must ensure its tax, investment and social security measures tackle, rather than facilitate, economic inequality.

The STUC does not believe freezing income tax for the duration of the Scottish Parliament is a sensible economic policy. It is clear that high earners have done well out of the pandemic and there is a need for additional investment in public services. Compared to Scotland, total tax revenue is much higher Nordic countries and they are both more equal and more productive than Scotland. Sweden and Denmark collect at least 10% more of GDP in taxation each year than the UK.

While council tax is regressive and should be replaced, a council tax freeze is not effective at helping those on the lowest incomes (as most are protected by the council tax reduction scheme). In cash terms, it benefits those on higher incomes most, and undermines Local Authorities.

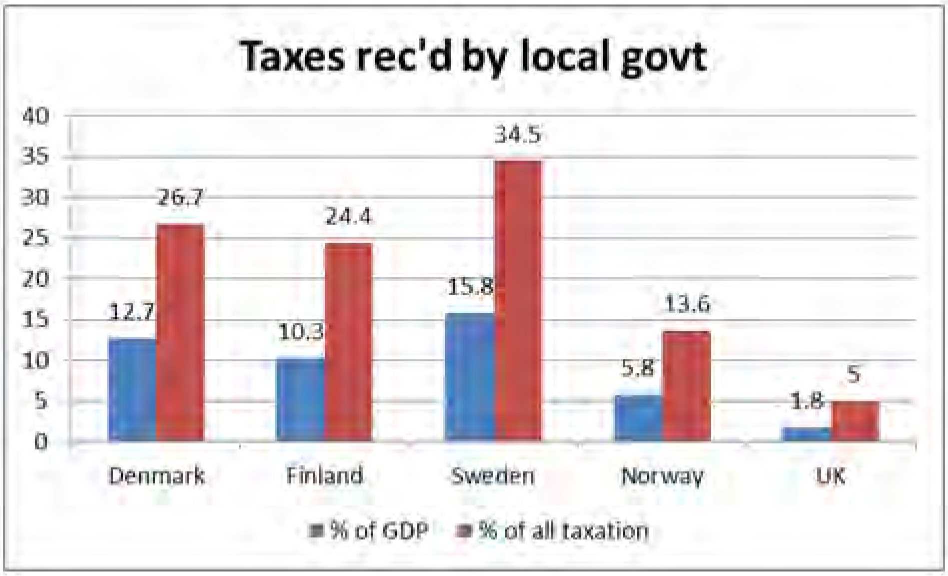
In the medium to long term, progressively increasing the overall tax take of Central and Local Government (and using the additional revenue wisely, e.g. investing in public sector pay, childcare, social security and low-carbon infrastructure) should be a goal of policy. As the Nordics economic performance shows, there is no trade-off between high levels of tax and economic dynamism. In recent years organisations like the IMF have been highlighting that higher taxes can reduce inequality without impeding economic growth.[xii]

Places

To address the decline of regional town centres, and to ensure wealth does not flow out of our communities, we should draw on the concept of community wealth building. While community wealth building is gaining political support, the real test is whether this is accompanied by financial support and the devolution of power.

The balance of funding for public services through local government has shifted from approximately 50% being raised directly by local authorities and 50% coming from national government, to 85% of funding coming from central government and 15% being raised directly by local authorities.[xiii]

This disempowers local authorities and undermines democratic accountability. The Nordic countries raise far more locally in tax, as detailed in the table below.



Compiled by STUC from Eurostat data (2012)[xiv]

In 2022-23, it is likely that there will be reduced levels of available Covid-related financial support for the public and private sector. Given this, what should be the priorities for the Scottish Government's Budget?

The priority should be an investment-led recovery which tackles inequality, supports public services and tackles climate change. While immediate covid-related financial support may decrease, additional funding from the UK Government as well as revenue raising by the Scottish Government will therefore be required to ensure we stimulate sustainable and inclusive economic activity.

Having said this, there are a number of current spending commitments where the STUC would question if public money is being spent in an efficient manner.

The STUC do not believe that blanket tax cuts for business through rates relief are an efficient way of creating jobs or promoting fair work. In many ways blanket tax cuts for business are the antithesis of a Fair Work First approach. Funding goes to companies that lay-off staff, or that fire and re-hire staff, in the same way as it goes to those who recognise unions and are genuinely doing their best to support workers at this time.

Economic development and business support – which the STUC fully support – should be strategic and aligned to fair work conditions. An IPPR report for STUC highlighted the potential for a Fair Work Supplement, with employers who do not meet fair work criteria, paying a supplement on their business rate bills.[xv] At a minimum we should be ensuring that rates relief is conditional on providing fair work.

In relation to the public sector, there is a clear need for restorative pay settlements. Nearly half of Scotland's keyworkers are employed in the public sector and it is in the gift of the Scottish Government to make a significant investment which will make a tangible difference to keyworker pay. These workers have seen real term wage cuts over the last decade and increasing their pay would narrow the gender pay gap, reduce child poverty, boost local economies, and support inclusive growth from the bottom up.

In addition, a priority for social security is to double the child payment. While the UK Government must scrap its planned and unjust £20 Universal Credit cut, the Scottish Government also has an opportunity to loosen the grip of poverty on people's lives through this simple and cost-effective measure.

How should the Scottish Government Budget in 2022-23 address the risks arising from the level and rate of recovery from the pandemic in Scotland relative to the rest of the UK? Please consider any impact on devolved tax receipts and social security benefits in your answer.

How has the Fiscal Framework worked in managing response to the crisis?

How should learnings from the pandemic inform the forthcoming review of the Fiscal Framework?

During the period of the negotiation between the Scottish and UK Governments the STUC highlighted the potential risks surrounding the formula adopted to calculate the block grant adjustment to compensate for the devolution of to the Scottish Parliament.[xvi] Neither a calculation based on relative population or relative tax receipts would prevent a gradual but cumulative negative effect on the Scottish Budget. Neither method achieved the principles for tax devolution and block grant adjustment laid down by the Smith Commission. The final agreed model (indexation against relevant UK tax receipts) did achieve the aim of neither violating these principles nor being systemically detrimental to Scottish Budget.

It should be noted that the STUC's position rested on certain assumptions about economic and population growth which pre-dated both Brexit and the pandemic. However it seems likely that the best and fairest option for the Scottish Budget would be the retention of the current mechanism for calculating the block grant relative to tax receipts.

In addition, given the need for a green and fair recovery which addresses the immediate economic crisis, tackles climate change and reduces inequality, there is a clear need for greater borrowing powers for the Scottish Parliament as a matter of urgency.

Submission from Fraser of Allander Institute

1. How should the Scottish government's budget for 2022-23 address the need for a fair and equal recovery from the Covid crisis?

It is widely recognised that the Covid pandemic has had very uneven health, financial and other economic impacts. Some households and some businesses have suffered declines in income or turnover. Some have seen opportunities for employment and learning significantly constrained relative to expectations before the pandemic. There remain significant uncertainties about how many of those affected by the pandemic will find those effects are temporary, and how many will be impacted permanently.

In this context, what constitutes a 'fair and equal' recovery is a somewhat subjective question.

In the context of the 2022/23 budget and supporting documentation, the government should: articulate clearly its objectives for recovery and how it will assess fairness in this context; draw on up-to-date evidence of the impacts of the pandemic and the progress of the recovery, recognising the range of outcomes and groups that are relevant to this; draw on this evidence to support the policy prioritisation process; articulate the anticipated contribution of those policies towards its aspirations for a 'fair and equal' recovery.

In this context, the subject committees at parliament can play an important role in scrutinising the governments evidence base and rationale for policy decisions during the pre-budget scrutiny process.

2. How should the Scottish Government's Budget address the different impacts of the pandemic across age, income and education groups and across places?

The pandemic has undoubtedly had uneven impacts across society, both in terms of health and economic impacts. The impacts of the pandemic interact with underlying pressures to create an extremely challenging environment.

On the one hand, the ongoing uncertainty around the degree of permanence of some of the pandemic impacts creates a need for ongoing monitoring and flexibility around budgetary plans. On the other hand, where the broad scale of the policy challenge is understood – the challenges for enabling the health and education recoveries for example – policy and funding must be informed by clear long-term strategy and vision.

In making its budget plans, the government needs to clearly articulate the outcomes that it anticipates its policies will have for different groups, and assess whether its interventions are the most effective means of delivering those outcomes.

3. In 2022-23, it is likely that there will be reduced levels of available Covid-related financial support for the public and private sector. Given this, what should be the priorities for the Scottish Government's Budget?

In 2020/21 the Scottish budget received £9.5bn of Covid-related resource consequentials (of which £0.9bn were confirmed in February and have been deferred into 2021/22). In 2021/22 the Scottish budget has so far received £2.5bn of Covid-related resource consequentials (on top of the £0.9bn deferred).

Currently, the UK Government's spending plans for 2022/23 imply there will be no spending specifically badged as being Covid-related. As a result, the Scottish Government's allocation will fall to zero. Even if we assume that all of the direct costs associated with mitigating the immediate health and economic costs of Covid have disappeared by 2022/23 (e.g. on vaccination and test and trace programmes, on grants and subsidies to businesses to offset losses or additional costs, and on NDR reliefs for the leisure and hospitality sector), this nonetheless represents a substantial drop in spending power.

In reality, Covid-19 will continue to have an indirect impact on budgetary pressures in 2022/23 even if the direct threat of the virus itself has dissipated. Covid is likely to have legacy issues on the health budget (backlogs for elective care, potentially legacy issues around long Covid or mental health, etc.), as well as for skills and employability services, and education too. These legacy issues will overlap with the underlying pressures on budgets that pre-existed Covid (demographic change, etc.)

Under current UK Government plans, we can anticipate that the underlying block grant will increase by at least around two per cent in real terms in 2022/23. It is quite likely that the UK Government will announce additional spending on top of this before the start of the 2022/23 year. Nonetheless, the budget outlook looks set to be extremely tight given the multidimensional nature of the recovery on top of the pre-existing spending pressures.

How the government chooses to prioritise its budget across different dimensions of recovery – economic and labour market recovery, health recovery, education recovery, public service recovery – will need to be informed by evidence both of where pressures are emerging and where existing policies are working well (or less well), as well as by longer-term strategic analysis to identify key pressure points and mitigating actions.

In terms of the immediate future, there remain substantial uncertainties around the fall out from the pandemic. We don't yet know for example how the labour market will adapt to structural change (i.e. changes in the balance of goods and services consumed), and what this will imply for different types of training, skills or employability interventions. We don’t know quite how the legacy of Covid will play out in different parts of the NHS. Over the next few months before the 2022/23 budget is drafted, the government will need to closely monitor the progress of the recovery across the different dimensions, and use this evidence to inform its prioritisation. And there will need to be a relentless focus on value for money from the balance of interventions supported. There is the potential in all of this for subject committees to play a proactive role monitoring these issues too in order to inform and influence the budgetary response.

4. How should the Scottish Government's Budget address the risks arising from the level and rate of recovery from the pandemic in Scotland relative to the rest of the UK?

There are two ways in which this risk might play out.

The first is if, at the time the budget is set, forecasters perceive that the economic recovery is, or is likely to, happen more slowly in Scotland than in rUK. If this is the case, Scottish tax revenues may be forecast to grow more slowly than the corresponding block grant adjustments, constraining the resources available to the Scottish Government when the budget is set.

There is no strong evidence so far that the pandemic has affected economic activity in Scotland disproportionately than in rUK, and there is no strong evidence yet that the Scottish economy is recovering less quickly than rUK, when measured by output (GDP) or indicators of the labour market, such as employment or earnings. So at the moment, the risk that forecasts make a very significant impact on the budget in 2022/23 seems low.

[The technical conditions for a Scotland-specific economic shock were triggered in January 2021. In this context, it might appear strange to say that Scotland has not been disproportionately affected by the pandemic. However, the conditions for a Scotland- specific economic shock have been triggered by a relatively small difference in the forecast timing of the recovery in Scotland (made by the SFC in January) relative to the forecast timing of the recovery in the UK as a whole (made by the OBR in November and March). Despite this triggering of the conditions for a Scotland-specific economic shock, the underlying data on the economy and labour market is moving in a similar pattern in Scotland as in rUK.]

The second way that this risk might play out is if, after the 2022/23 budget has been set, new evidence emerges to suggest that recovery in Scotland is happening more slowly than in rUK. If this occurs, then outturn revenues in Scotland in 2022/23 may be lower than forecast, whilst social security spending may be higher than forecast.

In truth there is little the government can do to mitigate the risks of forecast error. If there is error associated with budget forecasts, the government will need to hope that it can accommodate those errors within its existing borrowing and Scotland Reserve powers. To the extent that the income tax reconciliation applying to the 2022/23 budget is only £34million, and with borrowing limits temporarily boosted to £600m per annum as a result of the triggering of the Scotland-specific economic shock conditions, the risk that the government will not be able to address forecast errors in 2022/23 with its existing budget management tools is extremely low.

In summary, there is a risk that the economic recovery happens more slowly in Scotland than in rUK, and if this happens there could be budgetary consequences. If a divergence is forecast at the time of the budget, this could constrain the resources available to the government; if the divergence emerges after the budget is set, divergence can be managed through borrowing and other cash management powers. At the moment however, the risk that divergence in speed of recovery make a material difference to the budget seem low. The spending plans of the UK Government are a more material consideration to determining the size of budget envelope.

5. How has the Fiscal Framework worked in managing the response to the crisis?

The fiscal framework has largely worked as it was meant to during the Covid-19 crisis, although with one important ad hoc change to the normal rules made by the UK Government.

The basic principle of the fiscal framework is that the Scottish budget is protected against the risk of fiscal shocks that impact the whole of the UK in similar ways. Covid- 19 has, by and large, had similar health and economic effects across the UK.

Additional spending by the UK Government – on health, business support grants, NDR reliefs, supporting transport providers, and so on – has generated Barnett consequentials for the Scottish budget, enabling the Scottish Government to allocate these resources in line with its priorities. At the same time, lower than anticipated revenues from income tax and LBTT in Scotland will largely be offset by reduced ‘block grant adjustments’, given similar revenue falls for the equivalent rUK taxes.

Hence the fiscal framework has worked as it was meant to during the crisis because it has insured the Scottish budget against the risk of the UK-wide spending and revenue shocks that Covid has caused.

The UK Government did however make one important ad hoc adjustment to the normal operation of the framework. This was the introduction of the ‘funding guarantees’ in July 2020, in response to a suggestion from Kate Forbes. These were minimum guaranteed increases in the devolved governments’ block grants for the 2020/21 financial year. These guarantees meant that the devolved governments could make financial plans in the knowledge that they would receive at least these minimum grant uplifts, even if the UK government’s eventual spending would have implied a lower allocation under the traditional Barnett formula approach (although if this eventually did arise, the guarantees could be deemed unfair to England).

In combination, the huge consequential sums allocated through the Barnett Formula together with the use of funding guarantees, averted funding crises for any of the UK's devolved governments, and largely averted major intergovernmental tensions over funding arrangements during the pandemic. If the pandemic had had disproportionate health or economic impacts in one or other UK territory, then tensions around funding could have become more acute. The sheer scale of funding allocated also negated the urgent need for the Scottish Government to gain access to additional borrowing powers during the pandemic itself.

A perennial problem with the fiscal framework however, and one that has become more evident during the pandemic, is the lack of any effective mechanisms for intergovernmental communication and coordination. At times the Scottish Government has had to make budgetary plans whilst being 'in the dark' about UK Government policy (and hence the level of resource that might subsequently flow to it). At other times the Scottish Government has had to react at short-notice to unexpected changes in UK Government policy that might impact Scotland.

6. How should learnings from the pandemic inform the forthcoming review of the Fiscal Framework?

In many respects the pandemic has not fundamentally altered the issues that the Fiscal Framework will need to cover. These issues include:

> Budget management tools to deal with forecast error. Before the pandemic, there was a strong case for saying that adequacy of the Scottish Government's budget management tools needed to be reviewed. Separate analysis by both the Scottish Government and Scottish Fiscal Commission suggests that the revenue borrowing limit of £300 million is likely to be exceeded reasonably frequently. Meanwhile the annual drawdown limit from the Scotland Reserve of £250 million represents only a slight increase on what was permissible with the 'Budget Exchange' mechanism that existing pre Scotland Act 2016. The pandemic has not materially altered the evidence or arguments here.
>
> Block Grant Adjustments. It is anticipated that the Fiscal Framework Review will provide an opportunity for the two governments to revisit their 2016 disputes around BGA mechanisms. The pandemic has not materially altered the evidence or arguments here.
>
> Inter-governmental communication and coordination. There is very limited communication or coordination between the UK and devolved governments on issues such as tax policy, even where policy decisions can have knock-on impacts for devolved governments. The pandemic did reinforce the challenges that these issues can create (e.g. decisions on stamp duty land tax or Non Domestic Rates in England can influence the resources available to the Scottish Government and have impacts on the Scottish economy).

Additional fiscal powers. The Scottish Government's preference is for the review to be wide in scope, exploring the feasibility of devolving new powers over taxation and borrowing. The UK Government's preference is for the review to be narrower in scope, focussed on technical aspects of the existing fiscal framework. The pandemic has not materially altered the nature of the debate here.

The nature of funding guarantees. Perhaps one issue that the pandemic has brought onto the table is the issue of funding guarantees. As noted above, these were introduced by the UK Government in July 2020 to bring further certainty to the Scottish Government's funding outlook and were an important part of the pandemic response. However, the UK Government has no plans to continue the use of the guarantees beyond 2020/21. The Scottish Government may argue for their continuation, but the UK Government is likely to be reticent to do so for reasons of taxpayer equity across the UK.

Thus there are relatively few 'learnings' from the pandemic that might inform the review, but this reflects in part the fact that, as explained above, major funding issues were averted as a result of the magnitude of resources allocated, and the fact that the health and economic impacts of the pandemic were fairly symmetric across the UK. However the review might also usefully consider how the fiscal framework would deal with a future health or economic shock that did affect one part of the UK disproportionately more than others.

The Fiscal Framework Review is scheduled to take place in the first half of 2022, following an independent report in the second half of 2021. To date the governments have made little progress agreeing the scope of either the review or the independent report.

Submission from David Hume Institute

1. How should the Scottish Government's budget for 2022-23 address the need for a fair and equal recovery from the Covid crisis?

Prioritisation – the Scottish Government's Budget for 2022-23 should publish how it has prioritised for a fair and equal recovery to enable people to understand its decision making.

Publicly transparent methodology - the Scottish Government needs to be clear on the underlying evidence for prioritisation choices, based on impact and outcomes intended. There needs to be explicit recognition of the trade-offs in the budget between 2022-23 deliverables, and investments in subsequent financial years needed for supporting transformational change.

Scotland already has statutory outcomes in place in the National Performance Framework (NPF). The NPF is aligned to the globally adopted United Nations Sustainable Development Goals (UNSDGs). Budget priorities should be directly linked to the progress for all of the NPF which should be tracked regularly. The budget should be clear on the interdependencies between different investment priorities and look for efficiencies across budget boundaries.

The continued connection to the UNSDGs is important for providing a common language to collaborate with other organisations and governments around the world - including in other parts of the UK which have also committed to delivering them.

Within the overall NPF assessment, the focus should be on those hardest hit by Covid-19. Government should set out where the pandemic's impact has had the most impact on increasing poverty and reducing fair work opportunities. All budgetary measures taken should ensure that these improve beyond the pre- pandemic level quickly, with target dates.

To support longer term recovery, it is critical to move away from single year budgets. This would be a significant public benefit to all publicly-funded services, third sector organisations and businesses more generally to publish provisional spending plans for future years, and to provide details of the assumptions and projections about revenue which underpin these. This will help longer term planning for service improvement, investment and productivity across Scotland. The benefit of this approach would be to allow all organisations to make their own indicative plans, more easily work on medium term projects with others and collectively boost both productivity and outcomes for Scotland. We recognise it increases political risk, but would encourage all to support such transparency positively.

2. How should the Scottish Government's budget address the different impacts of the pandemic across age, income and education groups and across places?

The pandemic has exacerbated both economic and social inequality across Scotland. It has set back progress on reducing poverty and inequality. World Economic Forum Global Gender Gap Index (March 2021) highlights the risk of gender equality being set back a generation by the pandemic.

Scotland's Gender Equality Index (December 2020) provides a pre-pandemic baseline. The pandemic has had a detrimental impact on gender equality, especially women's employment levels. The next update, due to be published in December 2023, will be a key metric on tracking progress.

The David Hume Institute's research conducted in partnership with the Children's Parliament and the Scottish Youth Parliament showed that young people's top 4 priorities are climate change, digital inequality, inclusion and poverty. The budget must have clarity on investment in 2022-23 for climate transition to net zero; delivering planned expenditure on broadband accessibility and digital inclusion; setting how expenditure will directly influence the reduction in poverty and promote greater inclusion.

The Scottish Government must continue to support work to improve Scotland's Places. This includes Scotland's internationally recognised Place Standard tool and the Place Principle.

The David Hume Institute's commissioned report from Professor Duncan Maclennan argues for devolving resources by putting more power in the hands of local communities. The report discusses the balance of responsibility between central and local government. The key point is that taxation policy should be decided to achieve the best long-term outcomes and evidenced in how they meet the NPF targets.

Indications of spending beyond 2022-23 in a multi-year framework are likely to maximise projects where the pay-back extends beyond the current fiscal year.

Through the David Hume Institute's Action Project we heard from businesses in remote areas of Scotland about their local ecosystem and how they supported each other. They identified less with business sectors and more with other businesses locally. Examples included working together to support local employment to develop and retain skills in the area. The budget should recognise that targeted regional funding can be as important as sectoral support for developing employment and retaining skills in communities.

3. In 2022-23, it is likely that there will be reduced levels of available Covid-related financial support for the public and private sector. Given this, what should be the priorities for the Scottish Government’s budget?

Prioritisation is key. At a time of multiple challenges and tight public finances, hard choices are almost certainly going to involve choosing to stop spending money on services or initiatives that are achieving public good, and are valued by their recipients or stakeholders in order to start or increase spending on other areas that are now judged a higher priority.

As well as transparent prioritisation, people told us through The Action Project they wanted a focus on climate action; faster delivery of digital infrastructure especially in rural communities and to give those most excluded support to engage actively.

4. How should the Scottish Government's budget address the risks arising from the level and rate of recovery from the pandemic in Scotland relative to the rest of the UK?

The Scottish Government has a track record of creative employment support, for instance when the Future Jobs Fund was withdrawn establishing Community Jobs Scotland. The scheme has a track record of positive destinations alongside feedback from organisations and young people that paid employment is a game-changer. At a time when tax receipts will be crucial, prioritising support for jobs where skills can be developed, rather than skills development alone, will be critical.

The Young Persons’ Guarantee had a positive impact during the pandemic. Analysis of the outcomes will help determine whether elements of it can be retained in future years.

There have been dramatic changes in the labour market in Scotland as a result of the pandemic and EU-exit. The budget will need to invest in communities with a view to retaining and developing the skills of those who live there, as well as attracting new skills to support existing and emerging jobs, particularly those supporting decarbonisation.

Prioritise increasing equality - there are widely documented potential benefits to the Scottish economy through higher levels of equality, for example through increasing tax take.

The budget should build on Scotland's comparative advantage in addressing climate change and transitioning to net zero by delivering on the agreed outcomes from COP 26.

EU funding schemes are finishing and are being replaced with a range of UK and Scottish Government led funding. Government will need to be transparent about the change, where this may leave gaps in funding and how this will or could be addressed.

The Scottish Government should continue to prioritise support for rural communities and economies to avoid rural depopulation.

One of the UK Government's replacement policies for EU funds is the new UK wide £220 million Community Renewal Fund (CRF). The CRF allocates funding directly to local initiatives but encouraged larger bids (over £500,000+) and bids score higher when endorsed by the constituency MP. With the short turnaround times for the CRF deadlines, this made it harder for small community organisations to bid for funding.

There may be projects that don't meet CRF requirements that could be valuable for the Scottish Government to support.

The timing of the UK budget to inform the Scottish budget should be set to remove the uncertainty seen in 2019-20 and 2021-22 to reduce the level of risk in the Scottish spending plans. The Scottish Parliament should seek assurances this will be the case to enable the benefits from the multi-year approach highlighted above to be achieved.

5. How has the Fiscal Framework worked in managing the response to the crisis?

The Fiscal Framework is complicated and it is not always immediately clear exactly how Scotland will be impacted in a rapidly changing external context. The intricacies of the framework were discussed at two previous David Hume Institute events with Professor Graeme Roy and with the Scottish Fiscal Commission

The current Fiscal Framework allows for some adaptation to Scottish needs, for example in social security. Through the Fiscal Framework, the option for Universal Credit (UC) claimants in Scotland to choose to be paid more frequently or have housing benefit paid directly to landlords has made a significant difference to some individuals. With 82% of UC claimants (184,150 people) choosing more frequent payments (MFP) since October 2017, and 33% (75,030 people) have taken up direct payment to landlords for housing costs as a way to help manage money and reduce housing insecurity. With poverty increasing, retaining these Scottish adaptations is likely to help many people.

The Fiscal Framework also enabled the different approaches to covid business support grants in Scotland. Reviewing how effective these have been against policy objectives will be important in understanding if they are tools that can be deployed in future circumstances.

6. How should learnings from the pandemic inform the forthcoming review of the Fiscal Framework?

The Fiscal Framework limits the Scottish Government's ability to manage spending (and saving) across financial years. More flexibility could help commitments to multi- year spending plans as discussed in the Institute's recent paper on multi-year budgeting.

We support a review to learn about how the Fiscal Framework has worked during the pandemic and whether Covid has meant that the Framework needs amending in some way.

The loss of significant European Funding as a result of EU-exit also needs to inform the review of the Fiscal Framework. New direct spend in Scotland from Whitehall departments (e.g. MHCLG previously DCLG) expanding their focus and teams into Scotland must also be considered.

Understanding the interactions between devolved and reserved taxes through the fiscal framework is important so people and businesses can plan ahead. For instance, choices on Scottish income tax, have to take account income tax rates and bands elsewhere in the UK and the potential for higher earners to move out of Scotland. For those taxpayers who may stay in Scotland but have more flexibility in how they structure their personal finances, the interaction of Scottish Income Tax with income tax on savings and dividends, corporation tax and capital gains tax must also be considered. It is important the review of the Fiscal Framework considers these interactions.

Submission from Royal Society of Edinburgh

Summary

- The pandemic has significantly altered spending priorities, leading to high levels of public spending to address challenges within the health care system and support the economy. The scale of public expenditure during the pandemic will increase UK public sector debt to its highest peacetime level. This increased level of debt, combined with a probable decrease in tax receipts, will place significant pressure on the UK and Scottish budgets.

- There are several risks that the Scottish Budget may need to address; notably, there is still a risk of a fourth wave of the pandemic, which, if it occurs, will lead to further increases in public spending. Other risks include high levels of inflation beyond 2%, impacts from adverse weather conditions due to climate change, falling tax receipts due to businesses failing and rising unemployment as furlough ends.

- The pandemic has led to vast backlogs and challenges within the health care system; the backlog in appointments and diagnosis will need particular attention in the short term. However, equal or more attention may have to be given to the social care sector, as this is where the pandemic has exposed some of the greatest weaknesses. This will be a key spending priority for the Scottish Government, but it's unclear what demands this will place on the Scottish Budget in the short-medium term. Another key spending priority will be education to ensure that any lost education resulting from the pandemic is addressed.

- Despite the pressures that health and education will place on the Scottish Budget, the Scottish Government should not lose sight of its aspirations to recover by improving growth, achieving net-zero, and establishing economy focused on wellbeing. Key aspects of a wellbeing economy are access to a high standard of employment which offers the minimum of a living wage, skills development, and low inequality. The RSE believes that a spending priority will be to support the economy through investing in early-stage companies (spinouts and start-ups), which are crucial to job creation, and aiming to fulfil the recommendations presented in the Social Renewal and Economic Recovery reports.

- Our previous responses noted that the fiscal framework offers significant flexibilities and provisions to support the Scottish Budget. In the lead up to the renegotiation of the fiscal framework, the state of intergovernmental relations has declined. The RSE has previously recommended that intergovernmental relations be improved by creating an Independent Secretariat, which would help enhance the structure, formality and

relationships of intergovernmental relations rather than create new mechanisms. A similar proposal has been put forward by the Dunlop Review and the joint review of intergovernmental relations by the UK Government and devolved administrations. The RSE is concerned that new initiatives from the UK Government, including the Shared Prosperity Fund, Levelling Up Fund, and Community Renewal Fund will bypass the devolved administrations. To ensure that such funds are as successful as possible, it will be crucially important that there is coordination and cooperation across the governments of the UK.

Introduction

1. The Royal Society of Edinburgh (RSE), Scotland's National Academy, welcomes the opportunity to respond to the Scottish Parliament Finance and Public Administration Committee inquiry on the Scottish Budget 2022/23. We enjoyed a strong working relationship with the previous Scottish Parliament Finance and Constitution Committee and look forward to working with the newly formed committee for the 2021-26 parliamentary term.

2. As Scotland's National Academy, the RSE has consistently provided comment and advice on Scottish public finances and constitutional affairs. Our work includes responses to the former Scottish Parliament Finance and Constitution Committee last year on the impact of the Covid-19 pandemic on the Scottish Budget and the fiscal framework.[6] [7] Additionally, the RSE has provided advice and comment on constitutional affairs to the UK Government[8] and committees within the House of Commons[9] and House of Lords[10]; these responses will be of interest to this committee.

3. This response was facilitated through an RSE working group, which included members of our Economy and Enterprise Committee[11] and RSE Fellows with expertise in economics, finance, and constitutional affairs. In responding to the inquiry, we have addressed our comments under the following main headings: *The Impact of Covid on the Budget and Future Challenges, Spending Priorities and Revenue Raising, and Fiscal Framework and Intergovernmental Relations.*

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[6] Royal Society of Edinburgh, (2020). 'Impact of COVID-19 on Public Finances and the Fiscal Framework'. URL: https://www.rse.org.uk/advice-papers/impact-of-covid-19-on-public-finances-and-the-fiscal-framework/
[7] Royal Society of Edinburgh, (2020). 'Budget 2021/22: Supporting the COVID-19 Recovery – Scotland's Taxes and Fiscal Framework' URL: https://www.rse.org.uk/advice-papers/budget-2021-22-supporting-the-covid-19-recovery-scotlands-taxes-and-fiscal-framework/
[8] Royal Society of Edinburgh, (2020). 'UK Internal Market'. URL: https://www.rse.org.uk/advice- papers/uk-internal-market/
[9] Royal Society of Edinburgh, (2020). 'Scotland and Coronavirus'. URL: https://www.rse.org.uk/advice-papers/coronavirus-and-scotland/
[10] Royal Society of Edinburgh, (2021). 'Future Governance of the UK'. URL: https://www.rse.org.uk/advice-papers/future-governance-of-the-uk/
[11] https://www.rse.org.uk/policy/standing-committees/economy-enterprise/

General Comments

4. The pandemic has created significant uncertainty, and there is a lack of data around key statistics, making it difficult to respond directly to the questions in the inquiry. At the time of writing, we do not know the timing of the UK Spending Review or the Scottish Budget or the prevailing circumstances at the time of these announcements. For example, a fourth coronavirus wave would likely keep public spending high, but if cases continue to decline, the Chancellor may have more latitude to contain public spending and hence reduce the rate of growth of borrowing. Furthermore, there is a lack of data around the impact of Covid-19 on tax revenues, business growth, and the labour market. While there is some information on the immediate impact, there is a lack of clarity on key statistics, including the level of business debt and the ability to pay it back, which may affect public finances.

5. Before the pandemic, an asymmetric tax system was established as Scotland and Wales had specific arrangements on fiscal policy resulting from different political experiences and spending priorities. This means that an increase in spending within England has different consequences for the devolved administrations via the Barnett Formula. However, during the pandemic, with a public health and economic emergency, spending across England happened quickly to cope with pressures on the system and this spending was not passed on to the devolved administrations via the Barnett Formula. Funds were provided to the devolved administrations via a 'Barnett Guarantee', which ensured that principles of the Barnett Formula were preserved.

The Impact of COVID on the budget

Immediate Impact

6. In our previous response[12], the RSE noted a problem with income tax estimations identified before the pandemic. Income tax revenue forecasts from the Scottish Fiscal Commission[13] were overly optimistic, as revealed in the UK Budget in 2019. However, the Scottish Government decided not to adjust the budget in 2019/20 but to carry forward adjustments to future budgets. Therefore, there remains a potential shortfall of around £500m, which will need to be accounted for in future budgets, and this will be on top of further public finance pressures resulting from the pandemic.

[12] Royal Society of Edinburgh, (2020). 'Impact of COVID-19 on Public Finances and the Fiscal Framework'. URL: https://www.rse.org.uk/advice-papers/impact-of-covid-19-on-public-finances-and-the-fiscal-framework/

[13] Scottish Fiscal Commission, (2020). 'Scotland's Economic and Fiscal Forecasts'. URL: fiscalcommission.scot/forecast/scotlands-economic-and-fiscal-forecasts-february-2020/

7. Over the last year, governments have had to dramatically increase expenditure via borrowing in response to the pandemic. The scale of public expenditure during the pandemic will increase UK public sector debt to its highest peacetime level. This increased level of debt, combined with a probable decrease in tax receipts, will place significant pressure on the UK and Scottish budgets.

8. We understand that the Scottish Fiscal Commission is currently completing its forecast of tax revenues, and this may provide a clearer indication of some of the impacts of Covid-19 on the Scottish Budget.

Current and Future Risks

9. In the short to medium term, several risks may impact the Scottish budget, and the Scottish Government should plan to meet them.

10. Despite the success of the vaccine rollout across the UK, there is still a risk of a fourth wave of the pandemic, which, should it occur, will subsequently increase public spending. If there is a fourth wave, some restrictions are likely to return and continue into 2022. These will reduce the profitability of many businesses, which will be reflected in lower government revenues via income tax and business rates.

11. Furthermore, the Bank of England is forecasting that inflation will rise beyond the 2% target in 2021.[14] The Scottish Government will have to consider the effects of rising wages and increased prices caused either by the pandemic and Brexit.

12. The impact of climate change means that the UK and Scotland will likely experience more adverse weather conditions in future, which could cause severe disruption. Building our resilience to adverse weather conditions and achieving net zero will take time; therefore, in the meantime, there may be impacts on the budget to respond to and repair damage from adverse weather. The risks of adverse weather conditions may add weight to the argument for having a longer time horizon on budgets rather than the current practice of a single year. The RSE has frequently supported the introduction of multi-year budgets, as the current process restricts longer-term prioritisation of expenditure.

   - Throughout the pandemic, significant public resources were used to support the private sector through business support loans and the job retention scheme. The business support loans have led to high levels of debt across the private sector, and as restrictions ease and the pandemic ends, there

[14] https://www.theguardian.com/business/2021/jun/30/bank-of-englands-andy-haldane-warns-of- inflation-rises

may be an expectation for this to be repaid sooner rather than later. However, it is uncertain how many businesses will be able to repay loans quickly or at all. Slow payback or writing off loans could impact public finances in two significant ways:lack of repayment will lead to the government fronting the cost, although most of this cost will fall on the UK Government;

- businesses with high debt levels will have reduced growth prospects, consequently impacting tax and business rate revenue. It is unclear on the level of private-sector debt in Scotland, how this differs from the rest of the UK and how it impacts public finances. The RSE believes that more research needs to be undertaken in this area to understand the potential impact on future budgets.

13. The job retention scheme has been crucial in supporting businesses and the workforce through the pandemic. It still supports many workers and businesses that cannot operate at full capacity due to ongoing restrictions. With the scheme expected to end in September, there is a risk that those still furloughed could lose their jobs. This would result in a rise in unemployment, increasing the need for higher public spending and reducing tax revenues. However, there are reported labour shortages in some sectors, including transport and logistics, hospitality, manufacturing and construction. There is a challenge for the Scottish Government to manage labour shortages and unemployment, particularly where skills (and expectations) are not matched with the available jobs. The Scottish Government working with businesses and training providers, should provide more reskilling and upskilling opportunities to support people to smoothly transition from a declining sector to a growing one.

Spending Priorities and Revenue Raising

Current Circumstances and Challenges

14. Since the beginning of the pandemic, government spending priorities have been focused on supporting the health service and economy. While it is uncertain if there will be a fourth wave of the pandemic, health will likely be the biggest spending priority in the immediate future. At the same time, spending in the economy will be repurposed to focus on recovery.

15. The pandemic has created several backlogs in areas of the public sector which will need to be addressed and present a challenge to the 2022/23 Scottish budget. Notably, there are significant backlogs and challenges in health and social care across the UK and Scotland. The backlog in appointments and diagnosis will need particular attention in the short term. However, equal or more attention may have to be given to the social care sector, as this is where the pandemic has exposed the greatest weaknesses. The Scottish Government has made clear its intention to integrate social care into the health system through establishing a National Care Service and has recently launched a

consultation on this. However, it is currently unclear how much this will demand from the Scottish Budget in the short- medium term. The underlying issue within the care sector is resourcing and attracting suitably skilled people to meet the steadily growing demand for care, which will require additional resources, potentially in the order of billions, direct from the Scottish Government, from fees paid directly by users, or through insurance. Within its pre-budget scrutiny, the Committee should examine the potential costs of social care to the Scottish Budget in the short term and medium-long term.

16. The pandemic has significantly impacted the education sector, with learners missing out on lessons and face-to-face contact with teachers and peers. Alternative assessment models have to be implemented to assess learners' performance. There is a risk that learners may not have acquired the knowledge and skills they would otherwise have gained pre-pandemic. There will be an urgent need to ensure that every learner has the opportunity to access the education they need. This may mean significantly higher spending on education and training than would otherwise be the case. Through its Education Committee[15], the RSE will continue to engage on the Scottish Government's education recovery plans, including reform of Education Scotland and SQA, and implementation of the OECD's recommendations on Curriculum for Excellence.

Future Spending Priorities and Objectives

17. Considering the above comments, the RSE would assume that there are significant constraints placed on future Scottish budgets due to the impact of the pandemic; and this will restrict the ability of the Scottish Government to manoeuvre to support areas the economy which are critical to growth and wellbeing.

18. Despite the pressures that health and education will place on the Scottish Budget, the Scottish Government should not lose sight of its aspirations to recover by improving growth and establishing an economy focused on wellbeing. The OECD defines a wellbeing economy as the '*capacity to create a virtuous circle in which citizens' well-being drives economic prosperity, stability and resilience, and vice- versa, that those good macroeconomic outcomes allow to sustain well-being investments over time.*' There is a need for greater research around what a wellbeing economy in Scotland would look like and the key factors to wellbeing.

19. The RSE believes that a key aspect of a wellbeing economy is high employment levels in jobs that offer a living wage or higher coupled with opportunities for personal and skills development. Research has shown that early- stage companies (start-ups and spinouts) are more likely to create new

[15] https://www.rse.org.uk/policy/standing-committees/education-committee/

jobs than larger, well-established companies. On average, young firms account for about 20% of employment across OECD countries but create almost half of the new jobs.[16] Therefore, given the importance of job creation to recovery and wellbeing, a spending priority could be to invest in innovation and commercialisation.

20. We note that the Scottish Government has changed its approach to funding enterprise via the development of the Scottish National Investment Bank (the Bank). Given that the Bank will focus on providing large funds to businesses and projects, and the enterprise agencies will provide smaller-scale funding, there is a risk of a funding gap within the investment ecosystem between larger and smaller-scale funding that may need to be addressed. The RSE supported the development of the Bank, emphasising that there must be a coherent approach set out in a strategy to support the entire enterprise and innovation ecosystem. The strategy should seek to address any funding gaps in the market from the enterprise agencies to the Bank.

21. Within a coherent strategy, the Bank will have a strong role in economic recovery by focusing on high-level and large-scale investments based on the mission-oriented approach. Focusing on the big challenges such as net-zero, demographics and public health can help crowd investment in these areas and create a supply chain of new companies in Scotland.

22. The impact of the pandemic will have been felt differently across the regions of Scotland; for instance, those areas with a higher number of businesses involved in or connected to hospitality and tourism may have been disproportionately impacted compared to other regions. City regions will also be impacted differently, with Glasgow's economy shrinking more than Edinburgh's.[17] Therefore, tailored spending may need to be targeted in different areas across different regions. However, a lack of data on regional economies across Scotland may mean there is a lack of understanding of regional markets and where investment should be targeted. The RSE believes there is a need for a coherent regional policy across Scotland and the UK, which targets investment, and we expand on this in paragraph 32.

23. The pandemic has highlighted and exacerbated inequalities within our society. Reports from advisory groups for the Scottish Government, including the Social Renewal Advisory Board and the Advisory Group for Economic Recovery, recommended that the Scottish Government prioritise policies to reduce inequality. These reports have 20 and 25 recommendations, respectively, ranging from introducing Universal Basic Income to developing a Scottish jobs

[16] OECD, (2020). 'DynEmp: Measuring job creation by start-ups and young firms'. URL: https://www.oecd.org/industry/dynemp.htm
[17] Demos-PWC, (2021). 'Good Growth for Cities'. URL: https://www.pwc.co.uk/industries/government- public-sector/good-growth.html

guarantee. It is assumed that these reports will influence the spending priorities of the Scottish Government. However, given that there are limited resources, a review of the allocation of spending and redistribution of resources may be necessary to fulfil the recommendations of these reports.

24. The RSE fully recognises the difficult decisions the Scottish Government will need to make to address competing demands on limited resources. As we have set out above, health and education will require significant resources to address healthcare backlogs and ensure learners can access the education they need. This severely limits the Scottish Government's ability to manoeuvre and spend significant resources in other policy areas. If policies are to achieve public support, the Scottish Government needs to be transparent about how and why they are deciding spending priorities.

Taxation and Revenue Raising

25. Due to the pressures on the Scottish and UK finances and the need for additional spending to fuel the recovery, governments may need to consider tax rises or new taxes. It has been reported that the UK Government may be considering a rise in National Insurance, and the Scottish Government will need to consider how it reacts to this. If, as suggested, it is used to increase spending on care for the elderly, the Barnett consequentials would deliver extra funding to Scotland.

26. Taxation will have a major impact on addressing the major challenges we face, such as climate change, demands on public health and the need to address structural inequalities. Governments may seek to raise taxes to raise revenue and use them to influence behaviour. The Scottish Government may need to choose how best to raise revenue whilst addressing key challenges, and certain taxes may be increased or new taxes introduced.

27. The RSE understands that the Scottish Government will soon publish its draft Framework for Tax. The framework will seek to embed a more strategic approach to tax policy and how the devolved powers over taxation can help address Scotland's challenges. The framework should present how the Scottish Government could develop new taxes to address economic, social, and environmental challenges.

Fiscal Frameworks and Intergovernmental Relations

28. The fiscal framework is due to be reviewed and renegotiated by the end of 2022. Our previous responses noted that the fiscal framework offers significant flexibilities and provisions to support the Scottish Budget. As a result, the current year's Scottish Budget will be unaffected by any possible reductions in income tax revenue due to the pandemic. For future years, the Scottish Budget is protected from falls in income from tax revenue if these are the same per

head across the UK. Thus, any falls in revenue from income tax due to the pandemic will only impact the Scottish Budget if they are more severe per head in Scotland than in England. It is unclear if there will be a disproportionate impact on taxes in Scotland which will be felt in future Scottish Budgets.

29. The RSE has raised concern around the intention of the UK Government to finance projects via new spending initiatives such as the Shared Prosperity Fund, Levelling Up Fund, and the Community Renewal Fund. These initiatives will bypass the devolved parliaments and governments and mean a direct transfer of money from the UK Government to local authorities and other agencies. For instance, the UK Community Renewal Fund deals directly with local authorities, in which they are expected to compete for a £220m fund. Many local governments have little capacity and expertise to apply for and distribute funds of this scale. In a response to the former Finance and Constitution Committee, we noted that the level of compliance associated with the administration of EU Structural Funds was an issue for local governments.[18] Therefore, it will be important to ensure that new funds from the UK Government take into account capacity limitations within local government and, as such, the bureaucracy associated with the new funds should be kept to a minimum. The RSE would recommend that new funding initiatives of the UK Government are distributed in cooperation with the Scottish Government and its development agencies, and where possible local authorities. If not, there is a risk that funds will not be as successful as hoped, and there will be a lack of coherence as spending may become complex and duplicated.

30. The City Region Deals were a reaction to changing political circumstances but have injected large amounts of money into local communities. In some cases, this has led to local schemes being developed with a lack of coherence and poor management, as found by the Scottish Parliament Local Government and Communities Committee[19] and Audit Scotland[20]. However, the local authorities have established their roles in City Region Deals, and progress has, so far, improved. Progress has been achieved through capacity building to improve spatial and regional development. In developing new initiatives like those listed above, the UK Government should learn from the City Region Deals and work with the Scottish Government and local authorities to ensure they are developed with coherence and are properly managed. If not, there is a chance that these will face the same challenges that the City Region Deals did when they were first established in Scotland.

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[18] Royal Society of Edinburgh, (2019). 'Structural Funds post-Brexit'. URL: https://www.rse.org.uk/advice-papers/rse-response-on-the-funding-of-eu-structural-fund-priorities-in-scotland-post-brexit/

[19] The Local Government and Communities Committee, (2018). 'City Regions – Deal or No Deal?' URL: https://sp-bpr-en-prod-cdnep.azureedge.net/published/LGC/2018/1/8/City-Regions--Deal-or-No-Deal-/LGCS052018R1.pdf

[20] https://www.audit-scotland.gov.uk/news/city-deals-lack-measures-of-success

31. Across the UK and Scotland, a proliferation of new initiatives and bodies involved in economic and social development will further complicate the environment. As mentioned in paragraph 23, there is a pressing need for a coherent regional policy for Scotland and the UK, which presents an understanding of regional economic, social and spatial development. New initiatives need to build on the experience of EU Structural Funds in their design, implementation and evaluation. The UK and Scottish Governments should develop a coherent strategy for regional and spatial development in Scotland.

32. There are examples of the UK and Scottish Governments working well together to deliver large projects, usually where the capacity of the local authority and economic agency cannot deliver on their own. Successful cooperation will lead to increased efficiency and better outcomes.

Intergovernmental Relations

33. As we have said in previous responses linked above, the current intergovernmental experience within the UK may be detrimental to the union itself. As the devolution settlements have evolved and changed, UK Government departments' imperfect knowledge of the role of devolved governments has affected intergovernmental relations. At the same time, political divergences have also contributed to growing mistrust. There is widespread and longstanding recognition that the system of intergovernmental relations is not fit for purpose, especially in light of the implications of Brexit for devolution and the UK's territorial constitution. Furthermore, while provisions may have been needed to secure trade across the UK, parts of the Internal Market Act are likely to further damage intergovernmental relations.

34. The RSE has previously recommended that intergovernmental relations be improved by creating an Independent Secretariat, which would help enhance the structure and formality of intergovernmental relations rather than create new mechanisms. As it is independent, the body would arrange regular meetings of the Joint Ministerial Committees, draft and publish minutes, handle disputes and conduct research. The body should have ring-fenced funding, which would be provided proportionally from each government.

35. The recently published Dunlop Review into UK Government Union Capability[21] presented several recommendations on improving intergovernmental relations, including:

- A new Great Office of State in the UK Government Cabinet.
- A new structure supporting the separate offices of the Secretaries of State for Scotland, Wales and Northern Ireland with a single Permanent Secretary.

[21] Dunlop, A. 2021. 'The Dunlop Review Into UK Government Union Capability'. URL: https://www.gov.uk/government/publications/the-dunlop-review-into-uk-government-union-capability

- A new fund for UK-wide projects, including joint projects with devolved governments.
- A new UK Intergovernmental Council (replacing the Joint Ministerial Committee), supported by an independent secretariat and a new, clear dispute handling process.

36. Additionally, the UK Government and the devolved administrations are jointly reviewing intergovernmental relations[22]. The review is continuing, and proposals include:

- Revised principles
- Replacing the Joint Ministerial Committee with a three-tiered structure incorporating:
    i. portfolio engagement at official and ministerial level engagement on cross-cutting issues, including an Inter-ministerial Standing Committee and a Financial Inter-ministerial Standing Committee; and
    ii. a plenary-style intergovernmental council
- A standing secretariat, operating independently of the administrations
- Revised procedures for dispute avoidance and resolution

37. These reviews and reports are welcomed, and some of their findings and recommendations align with the RSE's earlier representations. There is a weakness with the UK's intergovernmental system, amplified with Brexit. Therefore, improvements to the system are welcome, but they must only be implemented when all four national authorities of the UK agree on them.

[22] https://www.gov.uk/government/publications/progress-update-on-the-review-of-intergovernmental- relations

[i] Calculations based on applying public sector pay policy settlements to the median salary for full-time and part-time public sector employees in 2020 (ONS ASHE data).
[ii] https://www.resolutionfoundation.org/publications/risky-business/
[iii] https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinghours/articles/coronavirusandkeyworkersintheuk/2020-05-15
[iv] https://www.ippr.org/files/publications/pdf/scotlands-missing-pay-growth-march2016.pdf
[v] https://www.ifs.org.uk/publications/14763
[vi] https://www.tuc.org.uk/research-analysis/reports/ps10-minimum-wage-would-benefit-millions-key-workers
[vii] http://www.stuc.org.uk/files/Policy/Reasearch_Briefings/Action_onPay%20Briefing.pdf
[viii] http://www.stuc.org.uk/files/Policy/STUC_Green_Jobs.pdf
[ix] Transition Economics research for STUC.
[x] https://www.resolutionfoundation.org/comment/the-covid-certainty-more-savings-for-the-rich-more-debt-for-the-poor/
[xi] http://www.stuc.org.uk/files/Policy/Research-papers/Who_is_winning_from_covid.pdf
[xii] https://blogs.imf.org/2020/01/07/reduce-inequality-to-create-opportunity/
[xiii] https://www.unison-scotland.org/unison-and-jimmy-reid-foundation-joint-report-into-funding-local-government/
[xiv] http://stucbetterway.blogspot.com/2013/04/scotland-and-nordics-part-1-tax.html
[xv] https://www.ippr.org/files/2019-09/1568730565_local-tax-in-scotland-sept19.pdf
[xvi] http://stucbetterway.blogspot.com/2015/11/fiscal-framework-has-potential-to-make.html?m=1