Finance and Public Administration Committee

2nd Meeting, 2024 (Session 6), Tuesday 16 January 2024

Scottish Budget 2024-25

Purpose

1. The Committee is invited to take evidence from the Deputy First Minister and Cabinet Secretary for Finance, Shona Robison MSP, in relation to the Scottish Budget 2024-25 and the Scottish Fiscal Commission's December 2023 Economic and Fiscal Forecasts. The Deputy First Minister is accompanied by the following Scottish Government officials—

   - Dr Alison Cumming, Director of Budget and Public Spending, and
   - Dr Andrew Scott, Director of Tax and Revenues, Scottish Government.

Background

2. The Committee has agreed to build on the recommendations in its Pre-Budget 2024-25 Report by focusing its scrutiny of the Scottish Budget 2024-25 on establishing the affordability of the Scottish Government's tax and spending plans and how it has prioritised spending to deliver its three missions of—

   - Equality: Tackling poverty and protecting people from harm
   - Opportunity: A fair, green, and growing economy, and
   - Community: Prioritising our public services.

3. This paper provides background information to support the Committee's evidence session with the Deputy First Minister on the Scottish Budget 2024-25. A background note on the UK context, including key issues raised during recent evidence sessions with the Office for Budget Responsibility (OBR) and the Institute for Fiscal Studies (IFS) on 12 December 2023 is included at Annexe A.

4. The Committee took evidence from the Scottish Fiscal Commission (SFC) on 20 December 2023, and academics, think-tanks and a range of representatives from the public sector, local government, and trade unions, as well as Audit Scotland and Carnegie Scotland, on 9 January 2024.

5. The SPICe briefing on the Scottish Budget 2024-25, which was published on 4 January 2024, provides additional background material.

Scottish Budget 2024-25 and accompanying Economic and Fiscal Forecasts

Forecasts

6. The SFC's Economic and Fiscal Forecasts – December 2023 were published alongside the Scottish Government's Scottish Budget 2024-25 on 19 December 2023.

7. According to the SFC, the outlook for the Scottish economy is largely unchanged since its December 2022 and May 2023 Forecasts, "with a slightly less negative picture for 2023-24 compared to a year ago". It has revised up its forecast of real disposable income per person, however, the drop in living standards of 2.7% between 2021-22 and 2023-24 is "the largest reduction in living standards since Scottish records began in 1998". The SFC forecasts "slow and fragile growth in GDP and real disposable income per person, as the recent rises in interest rates continue to weigh on household incomes and the economy, with inflation also likely to stay higher for longer than we assumed previously".

8. The SFC notes that UK Government funding through the Block Grant has increased by £318m. Total funding in the 2024-25 Scottish Budget is £1.3bn higher than in 2023-24, a rise of 0.9% in real terms. While resource funding is expected to increase by £1.5bn, capital funding is set to fall by £173m in 2024-25. The SFC explains that "most of the increase in resource spending is due to the improved income tax net position". This increase of £1.2bn since the SFC's May 2023 Forecasts is explained as being due to inflation and higher earnings growth resulting in increased income tax revenues. The SFC suggests "we have no strong reasons to believe it is either significantly under or over-estimating Scottish tax revenues", adding "however there are risks and uncertainties" including Real Time Information (RTI) being an "imperfect predictor" of outturn data and lack of information on self-assessment tax revenues. It further notes that there are similar uncertainties in the OBR's forecast of UK income tax revenues.

9. The SFC highlights a reduced expected income tax reconciliation for 2021-22 (to be applied to the 2024-25 Budget). This now stands at -£390m, a reduction from the figure forecasted in May 2023 of -£712m. This, the SFC explains, is partly offset by positive reconciliations for the Block Grant Adjustments of other devolved taxes and social security, with the full reconciliation figure at -£338m. In relation to the Scotland Reserve, the SFC explains that the Scottish Government has set the 2024-25 Budget "with no assumed funding from the Scotland Reserve, as it plans to use all the available balance in the current year (2023-24)". Any underspends arising could, it notes, be added to the Reserve and used in future years.

10. The SFC projects large positive reconciliations for years 2022-23 and 2023-24 as a result of revising up its estimates of the income tax net position for those

years following higher than expected outturn in 2021-22 and higher than expected relative earnings growth in Scotland in 2022-23, alongside policies to raise additional revenues. As set out in the table below, a positive reconciliation for 2022-23 (to be applied to the 2025-26 budget) of £732m is forecast.

Outturn and indicative estimates of income tax reconciliations

Collection Year Applies to Budget for	2021-22 2024-25	2022-23 2025-26	2023-24 2026-27
Reconciliation (£m)	-390	732	502

Source: SFC
Shaded cells refer to outturn available at time of publication.

11. The SFC notes that increases in public sector pay "have a significant effect on Scottish Government spending", with 2023-24 pay estimated[1] to account for over £25 bn of resource expenditure across the devolved public sector, including local government (over half of the resource budget). In the absence of the Scottish Government's pay policy for 2024-25, the SFC has assumed average devolved public sector pay growth of 4.5%. It states that "given the information we have on funding, assumptions about pay and the size of the total pay bill, and assumptions about the size of the reserved public sector in Scotland, this implies a fall in Scotland's public sector employment from 2023-24 onwards".

12. In the medium-term, the SFC expects total funding (resource and capital) to increase by 4% in real terms between 2023-24 and 2028-29, however capital funding is expected to fall by 20% in real terms over the same period. The SFC however highlights that—

> "Policymakers need to plan for the potential for funding from 2025-26 onwards to look quite different from the picture presented here. Due to the various funding sources and forecasts used, the outlook for the Scottish Budget is always somewhat uncertain but the high inflation environment is increasing the risk of large changes in funding. We note the current funding outlook from 2025-26 onwards has two particular elements of uncertainty: there is the risk the income tax net position provides a less positive contribution to funding than is currently projected, and at the same time UK Government spending could be higher than currently planned, increasing funding available to the Scottish Government."

Scottish Budget 2024-25

13. In her foreword to the Scottish Budget 2024-25, the Deputy First Minister explained that "in setting this budget the Scottish Government has adopted a values-based approach focused on our three missions" of Equality, Opportunity and Community. She goes on to say that—

[1] Estimates from the Scottish Government.

"We have been compelled to take painful and difficult decisions in order to prioritise funding in the areas which have the greatest impact on the quality of life for the people of Scotland. We make no apology for deploying the levers available to us to deliver on our values – protecting people and optimising services".

14. The Budget 2024-25 sets out the Scottish Government's plans for taxation, including—

- increasing the Starter and Basic rate income tax bands by inflation to £14,876 and £26,561 respectively. These rates, along with intermediate and higher and top rates, will remain unchanged,
- introducing a new 45p Advanced rate band for those earning over £75,000,
- increasing the Top rate of tax from 47p to 48p, paid by those earning more than £125,140,
- making available an additional £144 million of funding to councils who agree to fully fund a council tax freeze,
- maintaining residential Land and Buildings Transaction Tax rates and bands at their current levels, and continuing first-time buyer relief and 6% additional dwelling supplement rate,
- introducing legislation to increase, from 1 April 2024, the standard rate of Scottish Landfill Tax to £103.70 per tonne and the lower rate to £3.30 per tonne, in line with planned UK Landfill Tax increases, and
- in relation to Non-Domestic Rates (NDR), freezing the Basic Property Rate charged to properties with a rateable value of up to and including £51,000, at 49.8p, and increase the other rates by inflation. NDR reliefs are also maintained, and 100% relief will be offered to island hospitality businesses, capped at £110,000.

15. The SFC forecasts the Scottish Government's policy announcements introducing a new additional tax band and increasing the top rate of income tax by 1p to raise £82m, after taking account of assumed behavioural changes. Revenues, it notes, would be £118m higher without this behavioural response. It explains that "increased income tax rates may lead to some taxpayers changing their behaviour, for example, increasing contributions into a pension scheme, reducing their working hours, leaving Scotland or more aggressively pursuing tax avoidance or evasion". Income tax behavioural responses are "highly uncertain" and "to an extent, the behavioural response in Scotland to current policy changes is unknowable". However, the SFC suggests that "even if we under or over-estimated the behavioural response by 50%, this would not pose a significant risk to the total Scottish income tax revenues" due to the sums involved.

16. The Scottish Government's spending plans for 2024-25 include—

- allocating £13.2bn to the NHS, an increase of £550m funding for NHS Boards,

- providing £6.3bn to social security payments, an increase of almost £1bn on 2023-24 figures, including increasing the Scottish Child Payment in line with inflation,
- increases to resource funding for policing of £75.7m and capital of £7.2m to improve estate, fleet, and technology, and to the Scottish Fire and Rescue Service of £13.6m resource and £10.3m capital to improve facilities,
- increasing the budget for the Crown Office & Procurator Fiscal Service from £198.7m to £223m,
- increasing the total Scottish Prison Service budget from £540.7m in 2023-24 to £648.2m,
- funding the £12 per hour living wage for adult and children's social care and early learning and childcare workers,
- investing £358m to help people install clean heating systems and make their homes more energy efficient,
- investing £66.9m to "kickstart our commitment of up to £500 million to anchor a new offshore wind supply chain in Scotland",
- spending nearly £2.5bn on public transport and increasing active travel funding to £220m,
- continuing to deliver free school meals for all children in Primary 1-5, and funding local authorities with £1.5m to cancel school meal debt, and
- increasing arts and culture funding by £15.8m.

17. The SFC highlights the Wellbeing, Economy, Fair Work and Energy, Rural Affairs, Land Reform and Islands, and Finance portfolios as facing real terms spending reductions. Within the Education and Skills portfolio, notable funding reductions include to the Scottish Funding Council, skills, and tuition fees.

18. In relation to the Scottish Government's capital budget, the Scottish Government notes that, while its £6.25m capital budget will "continue to be invested across a range of high priority areas to help maintain high-quality public services and achieve a just transition to a net zero economy …, delivering on our medium-term capital ambitions will not be easy". It indicates that this is a larger cut than it had modelled for and "means that it will take longer to deliver all our planned capital projects and programmes – unless the UK Government changes course and increases its investment in capital programmes". The Scottish Government explains that it plans to borrow the new maximum of £458m for capital in 2024-25 set out in the recently updated Fiscal Framework and will consider accessing alternative sources of capital borrowing in future.

19. The SPICe briefing on the Scottish Budget 2024-25 states that—

> "The wider reductions to the capital budget are also seen in the Affordable Housing Supply Programme (AHSP) budget. This is being reduced by 27% in real terms in 2024-25. It is unclear how this will affect the Scottish Government's commitment to complete 110,000 affordable homes by 2032 and to invest £3.5 billion in the AHSP this parliamentary term."

Evidence on 20 December 2023

20. During evidence to the Committee on 20 December 2023, the SFC suggested that “because Scotland’s tax system is now really quite progressive, for every 1% by which earnings grow faster in Scotland than they do in the rest of the UK, net tax revenue will go up by £250m” and £25m more than in the rest of the UK. This, it explained, “means that we get all the strong effects of both any earnings growth and any differential earnings growth in Scotland compared with the rest of the UK”. The SFC went on to say that “promoting earnings growth is therefore a very powerful way of driving up tax revenue in Scotland”, and so “the more we can get earnings to grow faster in Scotland, the more we can get tax revenues to grow”.

21. In relation to the fall in capital funding, the SFC explained that “the key factor that drives the fall in capital is the block grant”, and while the Scottish Government “might do some borrowing around the edges, … the big money comes mostly from the block grant”. The SFC stated that—

> “Speaking as economists, we feel that, if capital investment is spent wisely, it can have a huge impact on the economy. It connects communities and means that businesses can become more productive and that connectivity both within the UK and outside it can be better. Therefore, all the evidence points to capital investment being a really important part of economic growth in the long run”.

22. The SFC explained its approach to examining the potential impacts of behavioural change relating to income tax differentials in Scotland and rUK—

> “We do our best to come up with a behavioural estimate of what we think the tax policy will raise as people respond to an individual tax decision. If you are fortunate enough to be in the £100,000 to £125,000 bracket, and you are losing the personal allowance and facing a marginal tax rate of nearly 70 per cent, do you put more money into your pension or not? Those are the types of things that we are trying to capture. We are not looking, in that context, at the effect on the long-term structural growth rate of Scotland’s economy.”

23. On multi-year funding, the SFC highlighted that it “can make multi-year forecasts for revenues by using the UK Government’s broad-brush statements about the block grant”. However, “the Scottish Government’s argument would be that, while there is uncertainty about the net tax position and about what the UK Government might do, it can do a budget for only one year”. The SFC goes on to comment that “as the independent fiscal institution, we find that disappointing and think that the Scottish Government should set out multi-year spending plans”.

24. Asked about the proposed increases to social security spending, the SFC noted that—

> "It is always worth bearing in mind that social security spending is essentially demand led. Once the Government has set all the policies for how people can apply for social security and the levels of remuneration that they get depending on their conditions, the amount that it ends up spending on social security is not under the Government's control. That depends on the number of people who choose to apply for and get social security. You cannot change that number from one year to the next in the same way that you can decide to cut spending on housing or education. Once the Government has set its social security policies, then, essentially, the spending is out of its hands for quite a number of years until it introduces new reforms."

Evidence on 9 January 2024

25. At its evidence session on 9 January 2024[2], the Committee heard concerns from witnesses that the Scottish Government has not sufficiently prioritised spending in the Scottish Budget 2024-25 to deliver on its three missions of Equality, Opportunity and Community. The Joseph Rowntree Foundation (JRF) suggested that, while protecting schemes such as the Scottish Child Payment is welcome, there is "a significant risk, with the huge cuts for affordable housing in particular, that this Budget could lead to a rise in poverty".

26. Professor David Bell argued that this "was not a great budget in terms of [the] 'Opportunity'" mission and "ostensibly it doesn't look like the budget particularly favours economic growth", a view shared by the Fraser of Allander Institute (FAI). For example, they suggested that reduced budgets for the Scottish Funding Council, tuition fees, the Scottish National Investment Bank (SNIB) and Enterprise Agencies, as well as the reduced capital budget, could impact on inward investment, business growth, and the ability to develop skills in 'green' and high-wage jobs and to retrain people back into the workplace. Potential impacts on delivery of the National Strategy for Economic Transformation are also unclear. Colleges Scotland reiterated that investment in colleges is needed to grow the economy, while the Federation of Small Businesses (FSB) said it would have liked to have seen "at least some of" the business reliefs being offered at a UK level passed on to Scottish businesses.

27. Professor Bell referred to the role that SNIB can play in relation to net zero and the implications of funding cuts to the organisation. He suggested "in of itself, the bank cannot push us directly towards net zero—we need private sector investment—and with the directive that it has to support investments in that policy area, the bank can support that kind of investment". He went on to say that "I suspect that the cut might slow down more speculative investments in new technologies that could accelerate the move towards net zero", adding "perhaps there are alternative funding mechanisms, but thus far the SNIB seems to be the one institution that is very clearly aimed at that particular issue".

[2] The Committee heard evidence from Professor David Bell, Fraser of Allander Institute and the Joseph Rowntree Foundation, as well as representatives from Audit Scotland, Carnegie Scotland, Colleges Scotland, Federation of Small Businesses, Glasgow City Council, GMB Union, NatureScot, and Scottish Council for Voluntary Organisations.

28. Carnegie UK said it was unclear whether the National Outcomes were 'built-in' at the outset of developing this budget, rather than being added at the end of the process. It suggested that properly aligning spending decisions to National Outcomes would help to better ensure delivery of the Scottish Government's key priorities. Carnegie UK further highlighted the benefits of involving the public in informing spending decisions. More broadly, witnesses felt that greater transparency and explanation of the Scottish Government's spending decisions, including why it is prioritising some areas of spend and deprioritising others, would be helpful.

29. Professor Bell explained that the extent of the reductions to the capital budget announced in the UK Government's Autumn Statement "came as a surprise", while FAI noted that, even before these cuts, the Scottish Government was not on track to deliver all its planned capital projects. Colleges Scotland suggested that the impact of capital budget reductions on the college sector is particularly pronounced compared to universities which have the ability to raise revenues. Concerns were raised regarding the impact of capital budget reductions on the net zero budget, with JRF suggesting that more focus is needed on building new energy efficient homes, while supporting fuel-poor households particularly in rural areas.

30. Witnesses discussed the Scottish Government's decision to freeze council tax, the extent to which this is a progressive policy, the impact on local authority spend, and whether that revenue could have been better spent on other priorities, such as further increases to the Scottish Child Payment to help meet child poverty targets. Council tax reform was highlighted as a priority by the JRF and other witnesses.

31. The impact of the significant planned uplift in social security spend on other areas of the resource budget was explored by witnesses. The JRF favours this approach to welfare over that of the UK Government, while Professor Bell noted that the level of spend was expected at the time the policy was set. Spending on preventative approaches could, witnesses reiterated, help avoid increased spending later down the line, including on benefits.

32. Witnesses explored the absence of multi-year spending plans, with the SCVO arguing that this has a significant impact on planning the delivery of services and staffing levels and, in some cases, threatens the future viability of the bodies themselves. Glasgow City Council (GCC) suggested that certainty and transparency is important regarding budgets, an issue echoed by the SCVO and Colleges Scotland, which both said they are unclear from the figures in the Scottish Budget 2024-25 about the level of funding they can expect to receive. NatureScot had similar views, arguing that some certainty in the medium-term would also help to support relationships with its partners and those bodies it funds.

33. It was suggested that an 'honest conversation' is needed about how public services should be delivered and reformed. The GMB Union highlighted that public bodies have been reforming for some time, while GCC noted that,

without proper reform, some local authorities could follow some counterparts in England in being declared bankrupt. Witnesses noted that some reforms would require funds upfront. Audit Scotland highlighted that the Auditor General for Scotland continues to have an interest in fiscal sustainability and public service reform, as well as ensuring that spending can be tracked. On public sector pay, the GMB Union highlighted that recent pay increases have “barely kept up with inflation”, and that “decent” pay settlements are therefore required in this budget.

34. On addressing economic inactivity, Professor Bell argued that effective policy action must be based on accurate data, however the ONS Labour Force Survey, which traditionally provides this information, is no longer reliable. He explained the “main problem has been that the sample size of the Labour Force Survey has halved over the years and there is a question about how representative it is and therefore how you have to weight it”. He noted that administrative data from HMRC now “seems to be telling a different story from what the Labour Force Survey is saying and that’s a problem”. FAI further highlighted that “we have no sub-UK data at the moment being published by the ONS and that is because the survey has such a low response rate as a whole that they can’t really rely on it for UK-wide numbers let alone sub-UK results”. FAI concluded therefore that “we don’t really know the level of inactivity in Scotland”.

The Committee’s Pre-Budget 2024-25 Scrutiny

Background

35. The Committee’s Pre-Budget 2024-25 Report on the Sustainability of Scotland’s Public Finances was published on 6 November 2023. The Report set out the Committee’s concerns regarding the Scottish Government’s lack of long-term financial planning, affordability in decision-making, and the absence of an overall strategic purpose and objectives for its public service reform programme. The Scottish Government’s response was provided on 19 December 2023.

Multi-year outlook

36. In its 2023 MTFS, the Scottish Government had committed to publishing refreshed multi-year spending envelopes alongside the 2024-25 Budget. In its Pre-Budget 2024-25 Report, the Committee recommended that this should include sufficient detail to enable meaningful parliamentary scrutiny and to allow public bodies to plan ahead. The Committee also said it would examine this information along with the updated Infrastructure Investment Plan expected to be published as part of budget scrutiny. However, the Scottish Government has only published single-year spending plans for 2024-25. It explains this is because “the nature of the Autumn Statement and the Office for Budget Responsibility’s forecasts make future prospects more volatile, and it could be misleading to plan too far ahead across the board”. It plans to “revisit the multi-

year outlook" in its next MTFS in May 2024. Commenting, the SFC noted "in our role as the independent fiscal institution for Scotland we encourage the Scottish Government to plan its budgets over both the short, medium and long term", an approach it suggests is even more important against a backdrop of uncertainty.

37. There is no mention in the budget document of the expected updated Infrastructure Investment Plan.

Alignment with three missions

38. The Report recommended that "the Scottish Government explicitly sets out in the Scottish Budget 2024-25 if there are "any areas of spending it has assessed as not meeting its three missions test and where funding will, as a result, be reduced or ceased entirely". The Scottish Government's response states that the published portfolio allocations will reflect where investment has been sustained and prioritised. However, while the figures provided in the Scottish Budget show where funding has been reduced or ended, there is little explanation of why these decisions have been taken.

Transparency and accountability

39. The Scottish Government has responded favourably to the Committee's recommendation that, to support transparency, it should adopt a similar approach to that of the UK Government and the SFC in comparing its Budget plans for spending with the latest estimates or outturns from the previous year's spend. While this information is not provided within the budget document itself, the Scottish Government states that it "recognises the need to provide this information and will set out the requested detail in an additional on-line publication in January 2024".

40. The Committee asked the First Minister to ensure that Cabinet Secretaries regularly report to Parliament on progress against the outcomes they are expected to achieve as set out in his mandate letters and sought clarity on how he will hold Cabinet Secretaries to account if these outcomes are not achieved. The response confirms that "the Scottish Government will report routinely, regularly and transparently on our performance", and that "Ministers will continue to provide updates on delivery as part of their ongoing engagement with the Scottish Parliament on progress in their portfolios". It remains unclear how Cabinet Secretaries will be held to account by the First Minister if progress is not made on the outcomes.

Tax Advisory Group

41. The Committee welcomed establishment of the Tax Advisory Group (TAG)[3] as announced by the Scottish Government in the MTFS in May 2023. Outcomes

[3] Information on the Group and its membership can be found here: [Advisory group on tax strategy - gov.scot (www.gov.scot)](https://www.gov.scot).

from the TAG were to "feed into the Scottish Budget 2024-25"[4]. The Committee saw this as a step towards the creation of a clear strategy for taxation in Scotland" and concluded that "it is imperative that this work progresses at pace".

42. The budget document does not explain if and how the TAG's work has fed into the Scottish Government's tax policies announced as part of the Scottish Budget 2024-25. The Scottish Government explains that its strategy for taxation will be published alongside the 2024 MTFS and will "focus on building on the principles and objectives that underpin the Scottish Approach to Taxation, which were set out in our Framework for Tax in 2021".

Fiscal sustainability, productivity, and affordability

43. The Committee recommended that the Scottish Government produces a full response to the SFC's Fiscal Sustainability Report setting out the actions it will take to start addressing the longer-term challenges ahead.

44. The Scottish Government's response is silent on this recommendation.

45. In response to the Committee's request for details of the progress made in delivering those actions in the National Strategy for Economic Transformation that will help increase productivity, wage growth and labour market participation, the Scottish Government identifies the rollout of some programmes and refers to its NSET Annual Progress Report. In response to the Committee's concerns around affordability not being a key factor in the Scottish Government's decision-making, the Government restates its approach to setting the budget.

Taxonomy approach

46. In its Pre-Budget 2024-25 Report, the Committee welcomed that an enhanced taxonomy approach to identify and categorise all spending lines across the Scottish Budget with regards to their climate impact[5] would, for the first time, include resource as well as capital. This Taxonomy was published as Annex J to the 2024-25 Budget and highlights that—

> "… around 9% of budget spend is positively aligned with the delivery of the Scottish Government's climate objectives [and] 2% is negatively aligned, primarily delivering road and livestock investments which support emission generating activity. The vast majority of spend, 72%, is neutral delivering on core objectives which generate relatively little emissions domestically but may have higher emissions when evaluated in consumption terms; this is

[4] An update on the development of a longer-term tax strategy will be published alongside the May 2024 MTFS.
[5] Further information on this can be found in this Joint Letter from the Deputy First Minister and Cabinet Secretary for Net Zero, Energy and Transport to the FPA Committee, 18 November 2022.

primarily healthcare and social funding. Local government funding (around 16% of the total) is excluded from the taxonomy assessment”.[6]

47. The Scottish Government assesses 75% of resource spend as neutral and 51% of capital, with ‘negative high’ at 1% in resource and 7% in capital. It explains that adopting this taxonomy approach “represents an overall proportional improvement in future budget reporting”. The Scottish Government adds however that, “because the taxonomy is new and different in approach to previous years, analysis of 2024-25 does not include a comparison to previous years: instead, it aims to set a provisional baseline from which to learn”.

48. The SPICe Spotlight Blog on the Scottish Budget 2024-25 notes that “these ‘enhancements’ do not tackle the big challenges in understanding how this spending will contribute to meeting Scotland’s climate targets”. It adds that “we do not know what outcomes will be achieved by this spending – do the current allocations of negative spending set Scotland on a path to meet the emission reduction targets, to what degree is ‘positive’ spending offset by ‘negative’ [spend], and how will spending decisions in 2024-25 contribute to emissions in future years?”. The blog goes on to conclude that “unfortunately, this new taxonomy does little to increase the ability of parliament to understand or scrutinise the impact of the Budget on Scotland’s climate”.

National outcomes

49. The Committee in its Pre-Budget 2024-25 Report indicated that it looks forward to leading the Scottish Parliament’s scrutiny of the proposals for revised National Outcomes in 2024. It further asked the Scottish Government to provide an update on progress towards “developing an approach centred around multi-year programmes, the associated outcomes and the annual spend profiles attached”, including an overall timetable for completion of this work.

50. In response, the Scottish Government explained that “this approach is embedded across Scottish Government activity rather than being addressed as a single workstream [and] as such, Scottish Ministers expect all programmes in the Scottish Government to:

- have clear objectives linked to the delivery and achievement of outcomes,
- deliver value for money, and
- have closely tracked spend and regular reporting.

51. The Scottish Budget 2024-25 itself sets out for the first time the national outcomes (primary and secondary) that spend in certain portfolio areas is intended to contribute. These are repeated in the Scottish Government’s Equality and Fairer Scotland Budget Statement 2024-25, which also includes for the first time a ‘case study’ approach using a sample of eight budget lines as case studies, such as employability, primary care dental services, and social security. Commenting on the Statement, the SPICe briefing on the Scottish Budget 2024-25 published on 4 January 2024 suggests “it is hard to

[6] Carbon Assessment of the Scottish Budget 2024-25.

understand how the trade-offs inherent in budget setting have been shaped by equalities issues, and therefore how much of a priority tackling inequality is", adding "the sheer volume of information [265 pages] can make scrutinising it more challenging".

Public Service Reform

52. Recommendations from the Committee's inquiry into the Scottish Government's Public Service Reform Programme were included in its Pre-Budget 2024-25 Report. The Committee expressed concerns "that the focus of the Scottish Government's public service reform programme has, since May 2022, changed multiple times, as have the timescales for publishing further detail on what the programme will entail". It therefore made recommendations aimed "to bring much needed impetus, focus and direction to the Scottish Government's Reform Programme to ensure successful outcomes can be achieved at a much quicker pace".

53. The Scottish Government committed in its 2023 MTFS to providing six-monthly updates on the Programme to coincide with the Scottish Budget (usually published in December) and the MTFS in May each year. The Committee asked that the Scottish Government's first six-monthly update to the Committee includes the following information—

- a clear vision and strategic purpose for what it wants to achieve with the programme, including how it will provide leadership and oversight to support public bodies to deliver on this vision.
- the financial strategy to accompany the reform programme that was committed to by the then Deputy First Minister in March 2023.
- details of each workstream under the programme, milestones for their delivery and clear measurements of success, and
- an explanation of how the programme will impact on delivery of the national outcomes.

54. The Scottish Government's first update was provided alongside its response to the Pre-Budget 2024-25 Report on 19 December. It states that the scale of the financial challenges necessitates delivering efficiencies and making more effective use of resources to deliver services and improve outcomes, and that strategic change is needed longer-term to reduce demand, reduce costs and improve outcomes. The update sets out its "key aims and principles for a 10-year programme of public service reform, and the actions we need to take in the next 1-2 years to respond to our immediate budget challenges, and to build the platform for ongoing change". Four new workstreams have been established—

- **Convening**: agreeing a common vision across the public sector for achieving sustainable public services and establishing the infrastructure that enables progress to be made.

- **Saving**: identifying where clear and quantifiable, cashable savings, can be made, setting out targets for reducing/avoiding costs through efficiencies and supporting a longer-term approach to reformed services.
- **Enabling**: creating the conditions for systemic reform, removing barriers to change and establishing ways that the public can see, understand, and influence the changes, and
- **Aligning**: driving policy coherence and consistency across significant policy led reforms that will shape the future service landscape.

55. The update provides actions under each of the workstreams and sets out the progress it will make in Years 1 to 3. Over the next three months, it indicates that it will agree a shared approach, working with local government, the public and third sectors "to align, enable and deliver", and require all Scottish Government portfolios to set out their savings and reform plans by the end of the financial year "in line with the principles in this document and set out clear savings targets to public bodies".[7] Portfolios and public bodies will be asked to "follow a cascade of options in delivering savings, taking all opportunities to increase the efficiency with which they deliver their functions, taking all opportunities to offer services in different ways, considering reclassification/alignment/merger of bodies or function, and reducing service only where these options are exhausted".

56. The Committee had set out in its Pre-Budget 2024-25 Report its concerns regarding the confusion that still appeared to exist in relation to the Scottish Government's policy on public sector headcount and workforce levels. In its response, the Scottish Government states that—

> "… expenditure on public sector pay increases in the past two years is now greater than the growth in our resource Block Grant funding from the UK Government. As a result of the ongoing fiscal challenges and uncertainty over UK Government funding and inflation levels the next phase of this work will focus on working with our Trade Union partners to deliver reforms to put our public sector workforce on a sustainable footing. We intend to set out the pay metrics for 2024-25 following the Spring UK Budget.[8]"

57. The update indicates that the Scottish Government will "establish enabling environment for workforce reform, including support for voluntary severance". It does not include, as requested by the Committee, the financial strategy to accompany the reform programme that was committed to by the then Deputy First Minister in March 2023.

[7] The update recognises there are some bodies and core services (such as the NHS, Police and Fire, Social Security Scotland, Colleges and some very small bodies), "which will require specific approaches based on their existing reform plans and service pressures".
[8] The UK Government has announced that its Spring Budget will take place on 6 March 2024. This is likely to be after the Scottish Government's Budget Bill is passed.

Next steps

58. The Committee expects to publish a report of its scrutiny of the Scottish Budget 2024-25 at the end of January 2024.

Committee Clerking Team
January 2024

The Scottish Budget 2024-25: UK context

UK Government's Autumn Statement

1. The Chancellor of the Exchequer, The Rt Hon Jeremy Hunt MP, labelled his Autumn Statement on 22 November 2023 as an "autumn statement for growth", highlighting that the package includes "110 growth measures". The Chancellor explained his announcements are focused on five areas: reducing debt; cutting tax and rewarding hard work; backing British business; building domestic and sustainable energy and delivering world-class education". He indicated that, due to "difficult decisions we have taken in the last year", the fiscal situation now allowed him to deliver a package of tax cuts to support growth.

2. Key tax measures announced include reduced national insurance contributions, permanent full expensing of plant and machinery investment costs[9], extending business rates relief for retail, hospitality and leisure sectors in England, an alcohol duty freeze until 1 August 2024, and tobacco duty increases. The Chancellor's spending announcements include increases to universal credit in line with inflation (September figures) and the state pension in April 2024 by 8.5% in line with annual earnings growth for May to July 2023. He also increased the national living wage from 1 April 2024 by 9.8% to £11.44 an hour for eligible workers across the UK aged 21 and over and announced £80 million for the expansion of the Levelling Up Partnership programme to Scotland[10].

3. The Chancellor reaffirmed the UK Government's commitment set out in the Spring Budget 2023 that from 2025-26, planned departmental resource spending will continue to grow at 1% a year on average and that public sector capital spending will be frozen in cash terms. The House of Lords Library states in its briefing on the Autumn Statement that these spending targets restated by the Chancellor for 2025-26 onwards "imply real terms spending reductions for 'unprotected' departments". It highlights OBR estimates that the spending of unprotected departments would need to fall by 2.3% a year in real terms from 2025-26, increasing to 4.1% a year, should the UK Government continue with its ambition to increase defence spending to 2.5% of GDP and return overseas development assistance to its 0.7% of gross national income target.

4. The Chancellor stated that the Scottish Government is receiving £545 million in additional funding "as a result of decisions at the Autumn Statement".

[9] This was due to end in April 2026.
[10] For Na h-Eileanan an Iar, Argyll and Bute, Dundee, and the Scottish Borders. He stated that the UK Government will consider how to extend this programme further and will work in partnership with the Scottish Government "with the intention of delivering an extension to the Investment Zones programme in Scotland".

OBR's Economic and Fiscal Outlook – November 2023

5. The OBR published its 'Economic and fiscal outlook: November 2023 alongside the UK Autumn Statement. These five-year forecasts highlight that—

- The economy recovered more fully from the pandemic and weathered the energy price shock better than anticipated.
- Inflation is expected to remain higher for longer, taking until the second quarter of 2025 to return to the 2% Bank of England target, more than a year later than forecast in March.
- This domestically driven inflation increases nominal tax revenues compared to the OBR's March forecasts, however "it also raises the cost of welfare benefits, and higher interest rates raise the cost of servicing the Government's debts".
- The Chancellor meets his target to get debt falling as a share of GDP in five years' time "by an enhanced margin of £13 billion, but mainly thanks to the rolling nature of the rule giving him an extra year to get there".
- The tax burden rises in each of the next five years to a post-war high of 38% of GDP.
- The OBR has revised down its estimate of the medium-term potential growth rate of the economy to 1.6% from 1.8% in March, "largely driven by a weaker forecast for average hours per worker, which we now expect to fall in the medium term, rather than holding flat".
- Unemployment is forecast to rise to 1.6 million people (4.6% of the labour force) in the second quarter of 2025, around 85,000 people higher, and a year later, than expected in March.
- Living standards[11] are forecast to be 3% lower in 2024-25 than their pre-pandemic level.

6. The OBR further sets out the main changes to AME[12] spending since its March forecasts, including an increase in the Scottish Government's current expenditure by an average of £1.9 billion a year over the forecast, due to higher RDEL[13] spending and tax receipts.

7. During evidence on the OBR's forecasts and the Autumn Statement on 12 December 2023, Richard Hughes, Chair of the OBR noted that the "real spending power of Government departments in England goes down by about £19 billion over the forecast period" due to the Chancellor leaving public service spending plans unchanged in cash terms, despite a higher forecast for inflation". The implication for Scotland, he suggested, is that "if those spending plans are sustained, there will be fewer real increases in Barnett consequentials for Scottish departments because in practice less is being spent in real terms on health, education, transport and other areas where spending is devolved here in Scotland"

[11] As measured by real household disposable income (RHDI) per person.
[12] AME (Annually Managed Expenditure) is largely difficult to forecast public expenditure such as demand-led benefits and tax credits; non-cash costs; and bank holdings and loan repayments. Spending in AME is separate to DEL.
[13] The OBR defines RDEL spending as departmental or day-to-day spending.

8. The Committee’s Pre-Budget 2024-25 Report includes the following conclusion, in light of its continuing interest in the need to grow the tax base and increase productivity levels—

> “The Committee has consistently recommended that more action is needed to increase productivity, wage growth and labour market participation in Scotland and notes the Scottish Government’s response pointing to its National Strategy for Economic Transformation (NSET) as key to addressing these issues. We ask what progress has been made in delivering actions in the NSET that will help increase productivity, wage growth and labour market participation.”

9. In evidence, IFS Deputy Director, Carl Emmerson argued that, to address the UK’s labour market challenges, “first, we need a strategy for getting people who are out of work and are economically inactive into work [and] secondly, we need to know how to help who are in work to progress, and how we can get the productivity gains that can ultimately deliver wage gains”. He added that “we have done the latter particularly badly during the past 15 years”.

10. On UK tax levels and workforce productivity levels, Mr Hughes from the OBR explained to the Committee that—

> “Tax burdens are rising pretty much everywhere in the world, because working populations are shrinking and the numbers of people who are on state pensions or consuming public healthcare are rising. Therefore, if working people are not becoming significantly more productive than they were in the past—we heard in the earlier part of the evidence session that they are not—you need to get more tax out of your working population in order to deliver those pensions and to pay for those services. Working people are less productive than they were in the past. That is the arithmetic that is driving tax burdens higher everywhere.”

11. David Phillips, Associate Director at the IFS, suggested that “rather than just looking at tax rates or tax thresholds, there could be opportunities for a fundamental reform of taxes”, including in relation to property tax both in England and Scotland. He went on to highlight that the data on labour market trends “is being exposed as being quite poor”, with a substantially lower response rate to the Office for National Statistics (ONS) labour force survey leading to inconsistencies between that data and HMRC’s real-time information. For example, “based on the labour force survey, Scotland seems to have had an improvement in its labour force participation and employment relative to the rest of the UK, since before the pandemic …, however HMRC data shows that Scotland has the lowest increase in employment of any region of the UK—2.7% compared with about 4% in both England and Wales and 6% in Northern Ireland”.

12. On the UK Government’s decision to freeze total capital spending, Tom Joseph from the OBR stated that “the Government has not set any detailed spending plans beyond next year [and so] it is not really possible for us to say what the

implications are for public investment in the UK”. He went on to say that “capital spending has increased as a share of GDP over the past few years, but it is expected to fall back down again over the forecast period if it is frozen in cash terms”, adding “if such freezes were to be maintained over a long period, we would expect that to have a negative impact on economic growth over the longer term. Reductions in the capital funding available to the Scottish Government was an issue raised by the Committee in its Pre-Budget 2024-25 Report, when it noted its disappointment in this trend and said it is “particularly concerning during times of financial strain when governments should be investing in infrastructure to stimulate economic growth”.

13. During evidence, Mr Phillips drew the Committee’s attention to the SFC’s previous forecasts of “more claims, more successful claims and longer claims in Scotland’s disability benefits system”, due to the eligibility conditions and how claims are assessed and reassessed. He added if this is the case “that will push up costs”. He went on to say that “the next set of SFC forecasts will give some indication about the extent to which things are coming forward in the first 18 months or so of the roll out of Adult Disability Payment”, including any rises in expenditure and potential implications for the Scottish Budget.