Fifth Annual Report on the Implementation of the Scotland Act 2016

Ninth Annual Report on the Implementation and Operation of Part 3 (Financial Provisions) of the Scotland Act 2012

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Introduction

1. This is the ninth annual report on the implementation and operation of Part 3 (Financial Provisions) of the Scotland Act 2012 and the fifth report on the implementation of the Scotland Act 2016.

2. It is intended to inform Parliament of the implementation work that has been carried out on fiscal powers in the Scotland Acts 2012 and 2016 as required by section 33 of the Scotland Act 2012 and paragraph 107 of the Fiscal Framework. The UK Government produces a separate report on the implementation work they have carried out.

3. The Scotland Act 2012 was granted Royal Assent in May 2012 and represented the first transfer of fiscal powers from Westminster to the Scottish Parliament following devolution. These included:

   - The creation of a new Scottish rate of Income Tax;
   - Provisions to introduce a new Scottish tax on land transactions, and to disapply UK Stamp Duty Land Tax in Scotland;
   - Provisions to introduce a new Scottish tax on disposals to landfill, and to disapply UK Landfill Tax in Scotland;
   - Provision for capital borrowing by Scottish Ministers; and
   - The power to create new devolved taxes.

4. The Scotland Act 2016 received Royal Assent in March 2016 and devolved a range of further powers to the Scottish Parliament. These included:

   - Further income tax powers including the power to set rates and bands;
   - Assignment of Value Added Tax;
   - Certain social security benefits;
   - Provisions to introduce a new Scottish tax on the carriage of passengers by air from Scottish airports, and to disapply Air Passenger Duty in Scotland;
   - Provisions to introduce a new Scottish tax on the commercial exploitation of aggregates, and to disapply the UK Aggregates Levy in Scotland;
   - Fines, forfeitures and fixed penalties.

5. This report provides an update on these sections, as well as non-legislative elements in the Fiscal Framework[1] including:

   - Block Grant Adjustments;
   - Administration and implementation costs;

[1] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/503481/fiscal_framework_agreement_25_feb_16_2.pdf

- Policy Spillover effects;
- Borrowing; and
- Scotland Reserve.

6. The report provides an update on all legislative, policy and implementation work that has been carried out since the previous report on 22 April 2020[2] and outlines any forecast administration and implementation costs incurred in 2020-21.

7. Administration costs are the ongoing costs incurred in supporting the delivery of the Scottish Government's responsibilities under the Scotland Acts 2012 and 2016. Implementation costs are one-off costs associated with the initial investment to set up all the necessary systems and other elements required for the delivery of the powers under the Scotland Acts 2012 and 2016, whether through setting up a body or a service, implementing IT systems.

8. The Coronavirus (COVID-19) pandemic has seen significant impacts to work across all areas of government. The Scottish Government has worked with the UK Government and others to transfer additional powers devolved by the 2012 and 2016 Acts in an orderly way to ensure they can be used effectively for the people of Scotland, whilst prioritising its response to COVID-19. This year's report details the implementation work which has been impacted by the pandemic, including the pause of transfer of the remaining social security powers and VAT implementation, as well as the introduction of new benefits and additional support for Scottish citizens such as the extended delivery of Fair Start Scotland employability service.

9. The next report will be published in 2022.

[2] Scotland Acts 2012 and 2016 implementation: annual reports - gov.scot (www.gov.scot)

Fully Devolved Taxes

Costs

Table 1[3]

£m	2018-19	2019-20	2020-2021 (forecast)
Administration	5.1	6.3	5.9
Programme	1.1	0.8	0

10. The above table reflects Revenue Scotland's costs to prepare for, administer, and implement Land and Building Transaction Tax (LBTT), Scottish Landfill Tax (SLfT), Air Departure Tax (ADT), and Aggregates Levy (AL).

Land and Buildings Transaction Tax

The Scotland Act 2012 provided for devolution and powers to introduce a tax on transactions involving interests in land. Land and Buildings Transaction Tax subsequently replaced UK Stamp Duty Land Tax in Scotland from 1 April 2015.

LBTT is a tax applied to residential and commercial lands and building transactions (including commercial leases) where a chargeable interest is acquired. LBTT is administered by Revenue Scotland, with support from Registers of Scotland (ROS).

Key developments

11. In response to COVID-19, the Scottish Government temporarily increased the nil rate band for LBTT for residential property transactions from £145,000 to £250,000, for transactions where the effective date is between 15 July 2020 and 31 March 2021 (inclusive).

12. In addition, the Coronavirus (Scotland) (No.2) Act increased by 18 months to 36 months the period in which certain buyers can sell a previous main residence and then go on to reclaim their payment of the Additional Dwelling Supplement (ADS).

Outturn for 2019-2020

13. Revenue Scotland's Annual Devolved Taxes Accounts[4], published on 25 November 2020, reported total LBTT receipts in 2019-2020 of £597 million compared to £554 million in 2018-2019.

[3] Source: Revenue Scotland Annual Report & Accounts - Resources
[4] Revenue Scotland - Annual Report and Accounts 2019-20 - Devolved Taxes Accounts.pdf

Rates and bands

14. The previous Annual Implementation Report published in April 2020 set out the rates and bands for LBTT announced by the Scottish Government in Scottish Budget 2020-21, and the addition from 7 February 2020 of a third tax band on non-residential leases where the Net Present Value (NPV) of rental income is above £2 million.

15. In July 2020, legislation[5] introduced in response to COVID-19 temporarily increased the nil rate band for residential LBTT from £145,000 to £250,000 for residential property transactions where the effective date is between 15 July 2020 and 31 March 2021 (inclusive).

16. The legislation, intended to help support the property market in 2020-21, came into force with effect from 15 July 2020 and was approved by the Scottish Parliament on 26 August 2020, following consideration by the Finance and Constitution Committee on 19 August 2020.

17. No changes to rates and bands were announced in the Scottish Budget 2021-22. The Scottish Government has, however, confirmed that the ceiling of the nil rate band for residential property transactions will return as planned to £145,000 for transactions with an effective date from 1 April 2021.

18. Residential and non-residential LBTT rates, before and after the end of the temporary change to the increased nil rate band are outlined in Table 2 below.

[5] The Land and Buildings Transaction Tax (Tax Rates and Tax Bands) (Scotland) Amendment (No. 2) (Coronavirus) Order 2020

Table 2

Residential transactions			**Non-residential transactions**		**Non-residential leases**	
Purchase price	**LBTT rate from 15 July 2020 to 31 March 2021**	**LBTT rate from 01 April 2021**	**Purchase price**	**LBTT rate**	**Net present value of rent payable**	**LBTT rate**
Up to £145,000	0%	0%	Up to £150,000	0%	Up to £150,000	0%
£145,001 to £250,000	0%	2%	£150,001 to £250,000	1%	£150,001 to £2 million	1%
£250,001 to £325,000	5%	5%	Over £250'000	5%	Over £2 million	2%
£325,001 to £750,000	10%	10%				
Over £750'000	12%	12%				

19. The LBTT Additional Dwelling Supplement remains at four per cent of the total price of the property for all relevant transactions above £40,000, and will be charged in addition to the residential conveyance rates and bands.

Legislation

20. In addition to the legislation to amend LBTT rates and bands highlighted above, provisions in the Coronavirus (Scotland) (No.2) Act also amended the arrangements for the ADS for certain transactions.

21. In recognition that some people purchase a new main residence prior to selling their previous one, provisions in the LBTT legislation provide that the ADS can be reclaimed if: (i) the buyer pays the ADS when purchasing a new main residence; and (ii) sells a qualifying previous main residence within 18 months of that transaction. The Coronavirus (Scotland) (No.2) Act extended this period to 36 months for buyers who paid the ADS in relation to a transaction within an effective date prior to 25 March 2020 and who were still within their 18 month window on that date (transactions with an effective date between 24 September 2018 and 24 March 2020).

22. This Act also provided a power for Scottish Ministers to amend, by order, the period of 36 months or the relevant period of transactions, where they are satisfied that this is appropriate for a reason related to COVID-19. These delegated powers have not been used at the time of this report being published.

23. The provisions were early expired on 29 September 2020 through expiry regulations. However, the provisions permanently amended schedule 2A of the Land and Buildings Transaction (Scotland) Act 2013. Expiry of the provisions within the Coronavirus (Scotland) (No.2) Act 2020 does not affect this, including with regard to the delegated powers provided.

Scottish Landfill Tax

Scottish Landfill Tax was introduced on 1 April 2015, replacing UK Landfill Tax. It is a tax on the disposal of waste to landfill, charged by weight on the basis of two rates: a standard rate, and a lower rate for less polluting materials.

Key developments

24. In line with the Scottish Budget 2020-21, the standard and lower rates of SLfT were increased from 1 April 2020.

25. The Scottish Government announced an intention to increase the standard and lower rates of SLfT in Scottish Budget 2021-22, with effect from 1 April 2021.

Outturn

26. Revenue Scotland's Annual Devolved Taxes Accounts, published on 25 November 2020, reported total SLfT receipts in 2019-20 of £119 million compared to £149 million in 2018-19.

Rates

27. As announced in Scottish Budget 2020-21, and confirmed through subsequent legislation[6], the rates of SLfT for 2020-21 are £94.15 per tonne for standard rated waste and £3.00 per tonne for lower rated waste.

[6] As provided for through The Scottish Landfill Tax (Standard Rate and Lower Rate) (No. 2) Order 2020

28. The Scottish Government announced in Scottish Budget 2021-22 proposals to increase the standard rate of SLfT to £96.70 per tonne and the lower rate of SLfT to £3.10 per tonne, with effect from 1 April 2021. Legislation was made and laid in the Scottish Parliament on 19 February to provide for this inflation-based increase, which will ensure consistency with planned Landfill Tax charges in the rest of the UK.[7]

29. No changes have been made to the Scottish Landfill Communities Fund credit rate, which remains at 5.6%.

Legislation

30. Other than the increase to rates outlined above, no new legislative changes have been made to the arrangement for SLfT.

Air Departure Tax

Air Departure Tax is Scotland's planned replacement for Air Passenger Duty, which was devolved by the Scotland Act 2016. The UK and Scottish Governments have agreed that the introduction of Air Departure Tax will be deferred in order to allow for the issues raised with regard to the Highlands and Islands exemption to be resolved.

Key developments

31. The introduction of ADT in Scotland has been deferred to allow the issues raised in relation to the exemption for flights departing from the Highlands and Islands to be resolved.

32. The UK Government will maintain application of Air Passenger Duty in Scotland in the interim. The Scottish Government will engage with HM Treasury (HMT) on their planned consultation on Air Passenger Duty reform to find a solution that remains consistent with the Scottish Government's climate ambitions.

Aggregates Levy

The Scotland Act 2016 provided the Scottish Parliament with the power to legislate for a tax to replace the Aggregates Levy in Scotland. Aggregates Levy is a tax paid on the commercial exploitation of primary aggregates i.e. crushed rock, sand, and gravel.

[7] The Scottish Landfill Tax (Standard Rate and Lower Rate) Order 2021

Key developments

33. In August 2020, the Scottish Government published a report commissioned from the environmental consultancy Eunomia[8]. The report investigated the historical complexities and impact of the Aggregates Levy in the UK and set out illustrative future tax policy options for a Scottish Aggregates Levy, which modelled scenarios and potential impacts.

34. Since publication of the fourth annual implementation report, the Scottish Government has also engaged with the UK Government on its review of the UK Aggregates Levy[9], which was published in July 2020.

35. Following on from this, work will be undertaken to consider policy options and develop the necessary evidence base to support the introduction of a devolved levy in Scotland. It will be for the next Scottish Parliament to consider the legislation that would be required to provide for this.

[8] Scottish Aggregates Levy: evidence review and policy options - gov.scot (www.gov.scot)
[9] Review of the Aggregates Levy - GOV.UK (www.gov.uk)

Scottish Income Tax and VAT assignment

Scottish Income Tax

Since 6 April 2017, the Scottish Parliament has had the power to set the Income Tax rates and bands applicable to Scottish taxpayers on their non-savings and non-dividend income. The rates and bands will be set each year by a Scottish Rate Resolution.

The Scottish Block Grant will be adjusted to reflect the change in funding stream, in the manner set out in the Fiscal Framework agreement[10] between the UK and Scottish Governments on February 2016.

Key developments

36. Income tax outturn data for 2018-19 were published by Her Majesty's Revenue and Customs (HMRC) in September 2020[11]. This was the first outturn that included the new five band Scottish Income Tax System.

37. A National Audit Office (NAO) report published on 22 January 2021[12] confirmed that HMRC have appropriate rules and processes in place to collect and operate Scottish Income Tax. Audit Scotland endorsed this approach in their recent report published on 22 January 2021[13].

38. In 2019-20, HMRC undertook an exercise to match their Scottish taxpayer records to a third party data source (known as a 'data clash'). The aim of this was to test whether HMRC's identification of Scottish taxpayers was corroborated by other sources. Evidence from this exercise aligns with HMRC's analysis that they are correctly identifying 98-99 per cent of Scottish taxpayers.

Costs

Table 3

£m	2018-2019	2019-2020	2020-2021 forecast
Implementation	2.0	0.6	0
Administration/Operation	0.8	0.9	0.8

[10] Fiscal framework: agreement between the Scottish and UK Governments - gov.scot (www.gov.scot)
[11] https://www.gov.uk/government/statistics/scottish-income-tax-outturn-statistics-2018-to-2019
[12] https://www.nao.org.uk/report/administration-of-scottish-income-tax-2019-20/
[13] https://www.audit-scotland.gov.uk/uploads/docs/um/nao_srit_2020.pdf

Move to normal running costs

39. HMRC completed the implementation work to deliver Scottish Income Tax during 2020-21, and the costs for this year reflect the move to business as usual of Scottish Income Tax.

40. HMRC estimates that the overall cost of implementing Scottish Income Tax powers, from the Scotland Act 2012 and Scotland Act 2016, to be £24.3 million. This excludes any extra costs that may arise, and will be recharged to the Scottish Government, from work required to accommodate any future changes to rates and thresholds.

41. Final figures for 2020-21 are not available. For the financial year 2020-21 to quarter three, Scottish Government has been invoiced running costs of £500,000 for Scottish Income Tax. HMRC has forecast a total cost for 2020-2021 of £0.8 million.

Assurance from NAO

42. The NAO published its fifth report into the administration of Scottish Income Tax on 22 January 2021. The NAO reported that "HMRC has adequate rules and procedures in place to ensure the proper assessment and collection of Scottish income tax and that those rules are being complied with". Audit Scotland reviewed this approach taken by the NAO, and endorsed its findings in their own report published January 2021.

Scottish taxpayer identification

43. HMRC estimate that there are around 2.5 million Scottish taxpayers. Scottish Government and HMRC agree on the importance of the correct identification of Scottish taxpayers to enable successful implementation of the Scottish Income Tax powers. HMRC undertake regular assurance activity on its live customer data to ensure that its identification of the Scottish taxpayer population is as accurate as possible.

Outturn

44. HMRC published the 'Scottish Income Tax Outturn Statistics: 2018 to 2019'[14] in September 2020, showing that receipts from Scottish Income Tax were £11.6 billion in 2018-19.

[14] https://www.gov.uk/government/statistics/scottish-income-tax-outturn-statistics-2018-to-2019

Rates

45. Scottish Income Tax rates and bands for 2020-21 are as follows[15]:

Table 4 Scottish Income Tax rates and bands for 2020-21

Income in Range	Name	Rate
Over £12,500* – £14,585	Starter Rate	19%
Over £14,585 - £25,158	Scottish Basic Rate	20%
Over £25,158 - £43,430	Intermediate Rate	21%
Over £43,430 - £150,000**	Higher Rate	41%
Above £150,000**	Top rate	46%

*Assumes individuals are in receipt of the Standard UK Personal Allowance.

**Those earning more than £100,000 will see their Personal Allowance reduced by £1 for every £2 earned over £100,000.

46. The Scottish Government's proposed Income Tax rates and bands for 2021-22 are summarised below. They were approved through the Scottish Government's Scottish Rate Resolution for 2021-2022 on 25 February 2021.

Table 5 Scottish Income Tax rates and bands for 2021-2022

Income in Range	Name	Rate
Over £12,570* – £14,667	Starter Rate	19%
Over £14,667 - £25,296	Scottish Basic Rate	20%
Over £25,296 - £43,662	Intermediate Rate	21%
Over £43,662 - £150,000**	Higher Rate	41%
Above £150,000**	Top rate	46%

*Assumes individuals are in receipt of the Standard UK Personal Allowance.

**Those earning more than £100,000 will see their Personal Allowance reduced by £1 for every £2 earned over £100,000.

[15] Information on the rates and bands that apply in Scotland is available on gov.scot

VAT assignment

Plans for Value Added Tax (VAT) assignment were enacted in section 16 of the Scotland Act 2016, which allows for receipts from the first 10 percentage points of the revenue attributable to Scotland from the standard rate of VAT and the first 2.5 percentage points of the reduced rate of VAT to be assigned to the Scottish Government, with a corresponding adjustment made to the Block Grant received from the UK Government. VAT rates will continue to be set at a UK-wide level.

Key developments

47. Due to the current economic climate, the Scottish Government and HMT have agreed to delay the implementation of VAT assignment and review it as part of the Fiscal Framework Review, due to take place in 2022.

48. Work continued throughout 2020 on finalising the model and implementation process

49. Data on Scottish VAT assignment, up to 2018, was published by HMRC on 26 November 2020[16].

Costs

50. As part of the Fiscal Framework agreement, the Scottish and UK Governments agreed to share equally all costs incurred as a result of the implementation and administration of VAT assignment. In 2019-20 total costs incurred by HMRC and the Scottish Government were £0.5 million, and in 2020-21, up to quarter two (Q2) of the financial year, totalled £0.1 million. These costs were split equally between HMRC and the Scottish Government.

Table 6

£m	**2018-2019**	**2019-2020**	**2020-2021(up to Q2)**
Implementation	0.4	0.5	0.1

Implementation

51. VAT assignment had been expected to commence from April 2021, with full fiscal impact in the Scottish Budget 2021-22. Due to the uncertainty of the impact of COVID-19 and EU Exit on VAT receipts, however, the Scottish and UK Governments have agreed to delay implementation of VAT assignment and review as part of the Fiscal Framework Review.

[16] Scottish VAT Assignment 2018 Estimate (publishing.service.gov.uk)

52. In 2020-21, the Scottish and UK Governments worked together to progress the draft VAT assignment methodology with the aim of delivering the best model and implementation process.

53. Work carried out throughout 2020 was reviewed and noted in December 2020 by senior officials in the Scottish and UK Governments. This will be included as part of the review of the Fiscal Framework.

Scottish VAT assignment forecasts

54. The Scottish Fiscal Commission (SFC) has responsibility for producing forecasts of the VAT that will be assigned to Scotland. Their latest forecast of VAT revenue assigned to Scotland was published in January 2021[17]. This forecast has no impact on the Scottish Government's budget as this is a transitional period, where VAT assignment will be forecast and calculated, but not applied to the budget.

[17] https://www.fiscalcommission.scot/wp-content/uploads/2021/01/Scotlands-Economic-and-Fiscal-Forecasts-January-2021.pdf

Block Grant Adjustments, Reconciliation and Indexation

The Fiscal Framework agreed that the Scottish Government's Block Grant would be adjusted to reflect the impact of the transfer of greater fiscal powers to the Scottish Government. Deductions are made to reflect the retention of devolved tax revenues and additions are made to provide funding for devolved social security benefits.

Key developments

55. As a UK Budget had not been published at the time of the Scottish Budget in February 2020, provisional Block Grant Adjustments (BGAs) were used to inform the Scottish Budget 2020-21 as directed under the Fiscal Framework.

56. Updated BGAs were produced at the UK Budget in March 2020. The Cabinet Secretary for Finance decided to use the provisional BGAs to inform the Scottish Budget 2020-21.

57. Executive competence for five of the Social Security powers was transferred to the Scottish Government at the 2020-21 Scottish Budget and the Block Grant Adjustments for these benefits were calculated for the first time and are now in operation.

58. The third Fiscal Framework Outturn Report[18] (FFOR) was published on 1 October 2020 to report, amongst other things, on the operation of the Block Grant Adjustments. However, the latest published Fiscal Framework data update, which supersedes data set out in the FFOR, is included in Annex C of the Scottish Government's Medium Term Financial Strategy (MTFS) 2021[19].

59. Outturn data for 2018-19 Income Tax was published on 23 September 2020, determining the income tax reconciliation, which in turn impacted the 2021-2022 Scottish Budget.

60. Scottish and UK Government Ministers have agreed that the issue of the BGAs for the Proceeds of Crime (POC) should be considered as part of the Fiscal Framework Review.

Provisional BGAs

61. The Fiscal Framework sets out that, where the Scottish Budget takes place before the UK Budget, the Scottish Budget will be based on provisional BGAs. Since the UK Budget 2020 took place after the Scottish Budget, provisional BGAs were used to inform the 2020-21 Scottish Budget.

[18] https://www.gov.scot/publications/fiscal-framework-outturn-report-2020/pages/6/
[19] https://www.gov.scot/publications/scotlands-fiscal-outlook-scottish-governments-medium-term-financial-strategy/pages/14/

62. For taxes, the provisional BGAs were based on forecasts published by the Office for Budget Responsibility (OBR) at the UK Spring Statement 2019, which were then restated on 16 December 2019, alongside the Welsh Budget. The restated forecasts took account of the 2017-18 outturn data as well as in-year information from the Pay as You Earn (PAYE) system, but did not take into account any changes in the underlying economic outlook.

63. For Social Security, as the UK Spring Statement 2019 did not include Scottish forecasts for all of the benefits being transferred in 2020-21, the Scottish and UK Governments agreed a bespoke methodology for calculating these provisional BGAs and their corresponding baseline year figures[20].

64. The Framework also sets out that, where the UK Budget takes place less than three months before the start of the financial year, provisional BGAs will be applied to the Scottish Block Grant for that year. However, the UK and Scottish Governments agreed that the Scottish Government could choose to use the BGAs provided alongside the later UK Budget if it preferred to do so. The Cabinet Secretary for Finance decided to use the provisional BGAs to inform the Scottish Budget.

65. A similar order of events has occurred this year, with provisional BGAs underpinning the Scottish Budget 2021-22, announced in January 2021, as the UK Budget was not published until 3 March 2021. While an updated set of BGA figures for 2021-22 is now available, the Scottish Government has confirmed that it will also continue to use the provisional BGAs to inform the Scottish Budget 2021-22.

66. In-year reconciliations to the 2020-21 Scottish Budget have been made in the normal way, on the basis of the comparison between the provisional BGAs which underpinned the 2020-21 Scottish Budget and the provisional BGAs which underpinned the Scottish Budget 2021-22.

Data update: Fiscal Framework Outturn Report 2020 and Scottish Government's Medium Term Financial Strategy

67. As set out in the Written Agreement between the Scottish Government and the Finance and Constitution Committee[21], the Scottish Government published a Fiscal Framework Outturn Report on 1 October 2020 to report on the operation of the Fiscal Framework.

68. Due to COVID-19, the Scottish Government's MTFS was not published in May 2020 as per the normal timings, but was instead published alongside the Scottish Budget in January 2021. That meant that the Scottish Fiscal Commission did not publish forecasts of tax revenues and social security

[20] https://www.gov.scot/publications/scottish-budget-2020-21/pages/24/

[21] https://www.parliament.scot/S5_Finance/General%20Documents/20180517WA_with_SG.pdf

expenditure in May 2020, and the forecasts contained in FFOR 2020 were from the Scottish Budget in February 2020.

69. Similarly, the forecasts of the Block Grant Adjustments were based on the OBR's forecasts of UK tax revenues and social security expenditure at the UK Budget in March 2020. Therefore, the forecasts included in the FFOR 2020 did not account for the impact of COVID-19. Given delays to the publication of outturn data as a result of COVID-19, the report also largely draws on provisional 2019-20 outturn revenue and expenditure and BGA data.

70. The Scottish Government's MTFS, published in January 2021 alongside the 2021-22 Scottish Budget, sets out updated forecasts that accounted for the impact of COVID-19 and final outturn data for tax revenue and social security expenditure.

71. Annex C of the MTFS sets out the final reconciliation to the 2021-22 Budget as follows:

> A reconciliation of -£319 million would be made to the 2021-22 Budget which is the net impact of the reconciliations for Income Tax from 2018-19, and for the fully devolved taxes, Fines, Forfeitures and Fixed Penalties, Proceeds of Crime Act revenues, and Carer's Allowance for 2019-20.

Income Tax reconciliation

72. Outturn data for Income Tax for 2018-19 was published by HMRC on 23 September 2020 and a reconciliation of -£309 million was applied to the 2021-22 Budget. This was the second income tax reconciliation since the implementation of the Fiscal Framework. Further information on the reconciliation can be found in the Fiscal Framework Outturn Report.

Proceeds of Crime

73. The Scottish Government believes that the application of a BGA for POC Act revenues of £4 million per annum breaches the Smith Commission's "no detriment" principle . This is because the Scottish Government previously retained these proceeds (subject to a cap of £30 million, which was never breached). Further to discussion through the official-level Joint Exchequer Committee (JEC(O)), in January 2021 the Cabinet Secretary for Finance and the Chief Secretary to the Treasury agreed that the issue should be considered as part of the Fiscal Framework Review. The BGA remains at £4 million pending the outcome of the review.

Borrowing and Scotland Reserve

Key Developments

74. The Scottish Government's MTFS 2021 set out the principles and policies that guide the use of the Scottish Government's borrowing and reserve powers.

75. The SFC's January 2021 forecasts indicate that the criteria for a Scotland-specific economic shock occurring in 2021-22 have been met. This has resulted from the fact that the respective SFC and OBR forecasts have been produced at different points in time. The OBR forecasts produced alongside the UK Budget in March 2021 indicate that the criteria for a shock continue to be met, however, this continues to result from timing differences in the forecasts.

76. There is no evidence that Scotland's economic or tax performance has been materially different from that of the rest of the UK. The triggering of the shock provides the Scottish Government with some limited additional flexibilities in relation to the use of borrowing for forecast error, and the Scotland Reserve.

77. In an attempt to manage volatility risk, in 2021-22 Scottish Ministers plan to borrow £319 million to smooth the negative budget impact of forecast errors arising from tax and social security reconciliations. A decision has been taken to borrow £450 million to support infrastructure investment. Final borrowing drawdown will be confirmed over the course of the year.

Scotland-specific economic shock

78. The Fiscal Framework has provisions for a 'Scotland-specific economic shock' to be triggered. When this happens, the Scottish Government has access to increased borrowing and reserve flexibility. This provision is triggered when onshore Scottish GDP growth is below one per cent in absolute terms on a rolling four-quarter basis, and one percentage point or more below UK GDP growth over the same period. This can be either on the basis of outturn data, or on the basis of forecasts.

79. The SFC's forecasts, published on 28 January 2021, show that the technical requirements for this provision are triggered in 2021-22. The OBR's March 2021 forecasts also show that these criteria continue to be met. However both forecasters have been clear that rapid developments in relation to the pandemic can result in material differences between their respective forecasts, even if only a couple of months apart. It is as a result of these differences that the Scotland-specific economic shock provisions are met.

80. The SFC has made clear that the outlooks for Scottish and UK GDP are broadly similar. There is also no evidence to date that Scotland's economic or

tax performance has been materially different from that of the rest of the UK. Further information is set out in the SFC's Economic and Fiscal Forecasts[22], the Scottish Government's MTFS, and the SFC's March 2021 Fiscal Update.[23]

81. The triggering of this provision of the Fiscal Framework allows the Scottish Government to borrow £600 million rather than £300 million per year for forecast error on tax receipts and social security expenditure, and removes the limits on drawdown from the Scotland Reserve. This applies in the financial years 2021-22 until 2023-24.

82. These flexibilities will not be withdrawn retrospectively should revised forecasts or outturn data indicate that the criteria for a Scotland-specific economic shock are no longer met.

Capital Borrowing

Since 1 April 2017, the Scottish Government has had the power to borrow up to £450 million each year, up to a maximum total of £3 billion, to support investment in capital infrastructure.

2020-21 draw down

83. The 2020-21 Scottish Budget outlined plans to borrow £450 million, noting that final borrowing decisions are subject to the in-year budget management position.

84. At the time of publication of the 2021 MTFS and 2021-22 Scottish Budget no funds had yet been drawn down but for the purposes of budgeting and forecasting plans were revised downward to £300 million for 2020-21.

85. £150 million of Capital Borrowing was drawn down from the National Loans Fund in February. This borrowing has a term of twenty five years and interest rate (on an annuity basis) of 1.14 per cent.

86. Final decisions on additional borrowing drawdowns have not yet been confirmed with funds expected to be received on 30 March, with the amount and interest rate subject to change until this date.

2021-22 borrowing plans

87. As part of the Scottish Budget 2021-22, a decision has been taken to borrow £450 million to support infrastructure investment.

[22] https://www.fiscalcommission.scot/forecast/scotlands-economic-and-fiscal-forecasts-january-2021/
[23] https://www.fiscalcommission.scot/forecast/fiscal-update-march-2021/

88. As is the case with 2020-21, final decisions on the specific borrowing arrangements for 2021-22 are taken over the course of the year, reflecting an on-going assessment of programme requirements and value for money assessment of the options available. Final borrowing levels may therefore be below initial estimates.

Capital debt stock

89. On the basis of existing and planned borrowing, the Scottish Government will have accumulated £2.2 billion in capital debt by the end of 2021-22, 74 per cent of its overall limit. Details of the capital borrowing and repayment schedule can be found in the Scottish Government's MTFS, published January 2021.

Resource Borrowing

Since 1 April 2017, the Scottish Government has had the power to borrow up to £600 million each year within a statutory overall limit for resource borrowing of £1.75 billion.

The Fiscal Framework sets out the conditions and limits for elements of resource borrowing:

- for in-year cash management, an annual limit of £500 million;
- for forecast errors and annual limit of £300 million; and
- for any observed or forecast shortfall where there is or is forecast to be a Scotland-specific economic shock, an annual limit of £600 million.

2020-21 draw down

90. The 2020-21 Scottish Budget set out plans to borrow £207 million, noting that final borrowing decisions are subject to the in-year budget management position

91. At the time of publication of the 2021 MTFS and 2021-22 Scottish Budget no funds had yet been drawn down but plans remained unchanged.

92. Final decisions on resource borrowing drawdowns have yet to be taken and funds are expected to be received on 30 March with the amount and interest rate subject to change until this date.

2021-22 borrowing plans

93. In an attempt to manage volatility risk, in 2021-22 Scottish Ministers plan to borrow £319 million to smooth the negative budget impact of forecast errors arising from tax and social security reconciliations.
94. As the MTFS states, the Scottish Government will assess all planned resource borrowing decisions to smooth the funding trajectory over five years.

95. In order to promote budget stability and maintain flexibility in the Reserve, Scottish Government budgets will assume full borrowing against known and/or forecast Income Tax reconciliations. Any in-year volatility will be managed within the resulting overall budget envelope.

Scotland Reserve

The Scotland Reserve has applied since 1 April 2017. It replaces the Budget Exchange mechanism and enables the Scottish Government to manage volatility associated with its fiscal powers. The Scotland Reserve is capped in aggregate at £700 million, with annual drawdown limited to £250 million for resource and £100 million for capital. There are no annual limits for payments into the Scotland Reserve.

96. The triggering of a Scotland-specific economic shock has removed the annual drawdown limits on the Reserve. This applies in in the financial years 2021-22 until 2023-24. However the annual cap of £700 million remains.

2019-2020 Reserve position

97. The 2020-21 Reserve position, as reported to Parliament as part of the Spring Budget Revision process, is reproduced below. The Cabinet Secretary will provide an updated report on the Reserve position to the Scottish Parliament as part of the provisional outturn statement in June 2021.

Table 7: 2020-21 Reserve position

	Resource	**Capital**	**FT**	**Fiscal**
	£million	**£million**	**£million**	**£million**
2019-20 opening balance	381	65	159	605
2019-20 withdrawals	-249	-60	-120	-429
2019-20 Additions	85	74	97	256
2020-21 opening balance	**217**	**80**	**136**	**433**
2020-21 Scottish Budget commitments	-131	-5	-32	-168
2020-21 Summer Budget Revision	-18	-7		-25
2020-21 Autumn Budget Revision		-58	28	-30
2020-21 Spring Budget Revision	-22	5	22	5
Estimated 2020-21 Drawdown	-171	-65	18	-218
Provisional Reserve balance at Spring Budget Revision	**47**	**15**	**153**	**214**
Budget Monitoring forecast	164	18	99	281
Forecast Reserve Position	**211**	**33**	**252**	**495**

98. Table 7 sets out analysis of the forecast Reserve position at the time of this report being published. Final figures show current forecasts for the year-end Reserve balances for Resource, Capital and Financial Transactions

99. Notwithstanding the flexibilities provided through the triggering of a Scotland-specific economic shock, a reserve capped at £700 million with a maximum limit of £350 million for annual drawdowns severely limits the capacity for Scottish Ministers to plan for the impact of future fluctuations in tax receipts while also prudently managing any underspend across financial year.

Request for additional fiscal flexibilities in response to COVID-19

100. The Cabinet Secretary has repeatedly called on the UK Government to provide additional fiscal flexibilities to allow the Scottish Government to mobilise and deploy funding in the most effective way to support Scottish citizens in response to the COVID-19 pandemic, given the significant and ongoing economic and fiscal challenges that it has presented. The flexibilities requested include:
    - greater borrowing powers;
    - flexibility to utilise capital underspend for resource expenditure;
    - increased reserve limits; and
    - greater end-year flexibility.

101. The UK Government has confirmed that the further funding allocated as part of the UK Supplementary Estimates process in the 2020-21 financial year would be accompanied by additional flexibility to carry forward into 2021-22, without having to use the Scotland Reserve. However, this flexibility is limited and temporary. It does not change the fact that Scottish Government cannot borrow at its own hand to fund spending in response to COVID-19 or support the economy in the way that countries around the world have done.

102. The Scottish Parliament's Finance and Constitution Committee has also recommended that HM Treasury should give further consideration to providing the devolved governments with greater access to borrowing in emergency situations such as the current crisis, as set out in its Pre-budget Scrutiny 2021-22 report.[24] This position was endorsed by the Scottish Parliament in a motion on 9 December.

[24] https://sp-bpr-en-prod-cdnep.azureedge.net/published/FCC/2020/12/7/03127c26-3305-11eb-9ccf-000d3a23af40/FCC-S5-20-13.pdf

Social Security

The Social Security Directorate is responsible for ensuring the safe and secure transition of the benefits being devolved to Scotland, for the new benefits created, and the implementation of powers under the under the Scotland Act 2016. To achieve this, a Social Security Programme was established, and a new agency, Social Security Scotland created.

Social Security Scotland operates in accordance with the eight principles set out in the Social Security (Scotland) Act 2018 and Social Security Charter. This gives the Scottish Parliament greater powers to ensure that social security in Scotland is tailored to the needs of Scottish citizens.

Social Security Scotland is already successfully delivering ten benefits and once fully transferred, the Scottish Parliament and the Scottish Government will be responsible for delivery of social security benefits ultimately worth over £4 billion of spending each year in Scotland.

Key developments

103. During 2020-21 the Social Security Directorate adapted to the challenges of COVID-19 through re-planning the safe and secure delivery of the remaining devolved benefits. Together with Social Security Scotland, three new benefits have been successfully launched in 2020-21, while the systems and capability continue to be developed to deliver the higher-volume and more complex disability benefits, starting with Child Disability Payment in 2021-22.

104. Social Security Scotland is now well established and directly employs just over 1,000 people across its various sites. It is forecast to deliver £3.3 billion of payments by the end of 2020-21, £3 billion through Agency Agreements and around £300 million directly

105. Executive Competence for Attendance Allowance, Disability Living Allowance, Personal Independent Payment, Industrial Injuries Disablement Benefit, and Severe Disablement Allowance transferred to the Scottish Government on 1 April 2020. The Department for Work and Pensions (DWP) continues to administer these benefits through six Agency Agreements on behalf of Scottish Ministers. For 2021-21 the Programme Business Case (PBC) includes a forecast of £82 million will be spent on Agency Agreements. Covering the lifecycle of the agreements could require investment up to an additional £300 million. The actual agency agreement costs that the Scottish Government accepts from DWP are subject to negotiation, and these are scrutinised in detail. These costs will reduce over time as Social Security Scotland begins to fully administer more benefits and reaches steady state.

106. In response to the COVID-19 pandemic, Scottish Government increased investment in the Scottish Welfare Fund, distributing £57.5 million to ensure support is available for those in need. A one-off Coronavirus Carer's Allowance Supplement payment of £230.10 was made, doubling the payment which eligible carers received in June 2020.

107. The first payments of Child Winter Heating Assistance were made in December 2020, helping an estimated 14,000 children and young people in 2020-21. Job Start Payment was also introduced, supporting around 5,000 young people a year starting a new job after a period of unemployment.

108. The Scottish Child payment has been introduced with the first of these payments being made on 23 February 2021. Families will be paid £10 per week for every eligible child, with no limit on the number of children that can be claimed for.

109. The Scottish Government's immediate priority is ensuring that people in Scotland in receipt of disability benefits experience a safe and secure transition to devolved disability assistance. Households must continue to receive their benefits on time and in the right amount. The Scottish Government hold ambitions to create a system of disability assistance that works for people; and improvements are being made upon the current UK Government system in a number of important areas, including doing away with DWP-style assessments to access disability assistance.

Costs

Table 8

£m	**2018-19**	**2019-20**	**2020-21**
Implementation	55	82	125
Administration/Operation	46	67	225

110. The costs above, which have been updated following last year's report, are based on the Programme Business Case which was published in February 2020[25] and will be revised in due course. These do not include the impacts of COVID-19 which have had a significant impact on costs within this financial year whilst the timeline for the safe and secure delivery of the remaining benefits is planned.

111. The PBC provides a view on the whole life costs and benefits of the Scottish Government's Social Security Programme, over a 30-year timeframe to 2050. It shows the Scottish Government's investment in creating a new public service for Scotland, built from scratch with dignity, respect and fairness at the heart and will deliver for the people of Scotland for years to come. The system is being co-designed with clients on the basis of evidence. It is the

[25] Social Security Programme Business Case: Executive Summary (www.gov.scot)

largest and most complex exercise in devolution undertaken since the Scottish Parliament was reconvened twenty years ago.

112. The Scottish Government funds implementation costs incurred by the UK Government as a result of the devolution of welfare powers. For 2020-21 the Programme Business Case includes a forecast of £13 million for implementation recharges. If the current arrangement continues across the remainder of the life of the Programme, implementation charges could reach £70 million.

Social Security (Scotland) Act

113. In 2020-21, the Scottish Government passed legislation to underpin the delivery of the Social Security (Scotland) Act 2018[26], which sets out the over-arching legislative framework for the Scottish Government's Social Security powers. The Scotland Administration and Tribunal Membership (Scotland) Act 2020 contains specific provisions in a number of areas in relation to social security.

114. The Act contains provisions in relation to Appointees, non-disclosure of information in determination of assistance, offences, investigations, overpayment of recovery, and uprating in relation to 'top-up' assistance provided under Section 79 of the 2018 Act. It also contains provisions in relation to: the duty to inform clients of possible eligibility; to support persons who can give diagnosis in relation to terminal illness; suspension of assistance; and the ability to set the value of assistance to nil in certain circumstances. Finally, the Bill allows for the recruitment of members from the Reserved Tribunal to sit on the Scottish Tribunal.

Social Security Scotland

115. Social Security Scotland delivers its services in accordance with the eight principles set out in the Social Security (Scotland) Act 2018 and the Social Security Charter[27]. Foremost amongst these principles is the requirement that people be treated with dignity, fairness and respect. In February 2021 the results of the first client survey[28] were published. It showed that 90 per cent of clients said their experience was "good" or "very good" and feedback has also been provided that can be used to improve Social Security Scotland's services.

116. In the 2019-20 financial year, Social Security Scotland provided £346.7 million in payments to people across Scotland, making a total of around £540 million in payments since launch in September 2018 up to 31 March 2020. In

[26] Social Security Administration and Tribunal Membership (Scotland) Act 2020 (legislation.gov.uk)
[27] Our Charter: What you can expect from the Scottish Government and Social Security Scotland. (www.gov.scot)
[28] Social Security Scotland - Social Security Scotland Client Survey 2018-2020

the financial year 2020-21, Social Security Scotland expects to administer payments worth around £3.3 billion, £3 billion through Agency Agreements and around £300 million directly. Further details of this spending will be provided in Social Security Scotland's Annual Report and Accounts for the period, which will be published in winter 2021, in accordance with Statutory timescales.

117. With the launch of the Scottish Child Payment in February 2021, Social Security Scotland's service has now expanded to include ten separate benefit payments. It will continue to build capacity in 2021-22 in preparation for the launch of a range of disability benefits, which will become the major part of future operations.

COVID-19

118. Throughout the pandemic, the Scottish Government and Social Security Scotland have continued to ensure people are paid the money they rely on, while responding to the challenges of COVID-19 through re-planning the safe and secure delivery of the remaining devolved benefits. Scottish Government and Social Security Scotland continue to work jointly with the DWP and wider UK Government to ensure citizens receive the full range of support available.

119. The COVID-19 pandemic has had a major impact on the Scottish Government, on Social Security Scotland, and on DWP, whose support is needed to transfer social security powers. A timeline is being agreed between the Scottish and UK Governments to agree a revised timetable to deliver the remaining devolved benefits, and a process to complete case transfer, as soon as it is safely possible to do so.

<u>Self-Isolation Support Grant</u>

120. The Self-Isolation Support Grant (SISG) is a new grant of £500, offered through the Scottish Welfare fund, to ensure that people who are isolating don't have to choose between this and supporting themselves and their families financially, while helping to break the chains of transmission of COVID-19, and protect public health. Applications for the SISG opened on 12 October 2020 providing £500 grant to people required to self-isolate as a result of being contact traced and who:

- are in receipt of Universal Credit or other low-income benefits;
- are in employment; and
- will have reduced employment income as a result of having to self-isolate.

121. Since it was launched, the Scottish Government has extended the SISG to better support those it is intended to support. This includes parents of children who are required to self-isolate, and people who are not in receipt of

Universal Credit but whose usual income is at a level where they would qualify for this benefit if they applied for it.

122. From February 2021, the Scottish Government extended the eligibility criteria to those earning below the Real Living Wage, including those who receive council tax reduction. Also eligible are people with caring responsibilities for someone over 16, where the carer themselves meet the other eligibility criteria, and workers who earn less than £120 per week, meaning their level of income does not entitle them to statutory sick pay. In addition, the period during which people can apply for the grant has been lengthened to within 28 days of being told to self-isolate. This will significantly increase the number of people eligible for the grant and help remove financial barriers to isolating.

Scottish Welfare Fund

123. The Scottish Government increased investment in the Scottish Welfare Fund, distributing £57.5 million to ensure support is available for those in need. This included £22 million being distributed to local authorities in response to the COVID-19 outbreak which is in addition to the £35.5 million already committed to the Fund for 2020-21. To enable local authorities to meet the need in their areas and tackle financial insecurity, an additional £20 million of flexible funding was provided across the winter period. This funding has been utilised by councils in a number of different ways, including making cash grants for food and fuel to individuals and topping up Scottish Welfare Fund allocations to ensure demand is met in full.

Discretionary Housing Payments

124. In response to COVID-19 the Discretionary Housing Payment (DHP) budget was increased to more than £80 million in 2020-21 for councils to safeguard tenancies and prevent homelessness. Almost £60 million of the DHP budget was provided to ensure no one had to pay the bedroom tax; helping over 70,000 households in Scotland to sustain their tenancies. The cost of mitigation will increase as the numbers in receipt of Universal Credit increase since the Scottish Government remains committed to mitigating the impact in full. An additional £18.9 million was used to mitigate against the damaging impact of other UK Government welfare cuts, including the Benefit Cap and changes to the Local Housing Allowance rates, with a further £2 million budgeted to support care experienced young people through DHPs.

Coronavirus Carer's Allowance Supplement

125. A one-off Coronavirus Carer's Allowance Supplement payment of £230.10 was made this year, doubling the Carer's Allowance Supplement eligible carers received in June 2020. Along with December's 2020 Carer's Allowance Supplement, this means around 83,000 of Scotland's unpaid carers with some of the most intense roles and on some of the lowest incomes, received up to £690.30 more than carers south of the border. This extra investment of £19.2 million, brings our total investment through Carer's

Allowance, the Supplement and this payment to around £350 million in 2020-21.

Carer's Allowance

126. Changes were introduced to Carer's Allowance to ease the burden on carers during the COVID-19 outbreak. These included temporarily relaxing the rules regarding how long a carer can take a break from care and whether care needs to take place in the physical presence of the cared for person.

Young Carer Grant

127. Rules about the timing of applications for Young Carer Grants were relaxed so, for example, if someone applies after their nineteenth birthday, their application will be treated as though it was made on time if the delay was caused by COVID-19.

Benefits launched

Job Start Payment

128. Job Start Payment was introduced in August 2020, providing £250, or £400 for people with children, supporting around 5,000 young people a year starting a new job after a period of unemployment. In the current crisis, getting a job will represent a massive turning point for many young people – this payment will help ensure it does not also bring financial pressures.

Child Winter Heating Assistance

129. Social Security Scotland paid Child Winter Heating Assistance in December 2020 and Scotland is the only part of the UK to do this. This annual payment of £200 to each child who is receiving the highest rate of the care component of Disability Living Allowance will help up to 14,000 children and young people in 2020-21. This payment represents a £2.9 million investment in the well-being of the most severely disabled children and young people, helping to ease household financial pressures as a result of needing to heat the home throughout the day and night. Payments are made automatically each winter to eligible children and young people by Social Security Scotland.

Scottish Child Payment

130. The Scottish Child Payment (SCP) started being made on 23 February. Families will receive £10 per week for every eligible child, with no limit on the number of children that can be claimed for. It is the highest-volume benefit introduced to date by the Scottish Government, and could support up to 194,000 children this financial year – an increase of around 34,000 children since the pandemic began (Scottish Fiscal Commission forecasts of February

and September 2020[29]). The Scottish Child Payment together with the Best Start Grant and Best Start Foods will provide over £5,200 of financial support for families by the time their first child turns six. For second and subsequent children, this will provide over £4,900.

Disability assistance

131. In 2021 Child Disability Payment (CDP), the first of new Disability Assistance benefits[30], will be introduced. This replaces the UK Government's Disability Living Assistance for Children in Scotland. Adult Disability Payment will follow in 2022, replacing Personal Independence Payment.

132. A main priority is the safe and secure transfer of Disability Assistance, including existing Scottish clients, from the UK Government to Social Security Scotland, which means that in the immediate future fundamental changes will not be made to the existing benefit structure or rules. However a number of ways have already been identified to provide disabled people with a different experience when accessing the support they are entitled to.

133. CDP will be introduced in summer 2021 as part of a pilot, with full rollout by autumn 2021, extending to the upper age limit of CDP from age 16 to 18 for clients entitled to CDP immediately before reaching age 16. Meanwhile, ADP will be piloted in spring 2022 and available across the country by summer 2022. Work is ongoing with stakeholders to make changes to ADP, including to better assess the impact of an individual's condition, particularly in relation to mental health, hidden or fluctuating conditions. DWP-style assessments will not be undertaken to allow people to access to Disability Assistance.

134. Pension Age Disability Payment is currently delivered by DWP in the form of Attendance Allowance, a benefit for people over 65. It is awarded to help with extra costs if a person has a disability severe enough that they need someone to help look after them. It is the Scottish Government's intention to provide this form of assistance for the same purpose, to provide mitigating costs for the additional costs incurred as a result of having a disability. The Scottish Government will work with delivery partners including the UK Government in coming months to re-plan delivery of Pension Age Disability Payment and agree when it will be possible to launch the new benefit in Scotland.

[29] https://www.fiscalcommission.scot/forecast/scotlands-economic-and-fiscal-forecasts-february-2020/ and https://www.fiscalcommission.scot/forecast/supplementary-publication-fiscal-update-september-2020/
[30] Disability benefits: overview - gov.scot (www.gov.scot)

Employability

The Scotland Act 2016 gave Scottish Ministers the powers to deliver employability support that helps disabled people or those at risk of long-term employment to seek, obtain, and retain employment.

Key developments

135. The Scottish Government continues to work closely with all parties to maintain the support required to help those who are further from the labour market in their journeys towards and into and work, with over 29,000 people joining Fair Start Scotland (FSS) in the first two and a three quarter years of service (as of December 2020).

136. The Scottish Government proactively publishes information on its employability services, with statistics published quarterly on performance to date.

137. The Scottish Government has also published annual reports and evaluation findings for 2019 and 2020, setting out Fair Start Scotland performance and outcomes for people and communities.

Costs

Table 9

£m	2018-2019	2019-2020	2020-2021 (forecast)
Implementation	0.6	0.0	0.0
Administration/Operation	14.8	18.7	23.0

Fair Start Scotland

138. Fair Start Scotland provides tailored, person-centred support to people who need help to find and stay in work, and achieve their full potential. Unlike previous UK Government initiatives, participation in FSS is voluntary.

139. The Scottish Government has contracted a mixed economy of public, private, and third sector service provided to deliver FSS across nine regional "Lots". The Scottish Government continues to work with service providers to continuously improve FSS support, ensuring it is tailored to participants' individual needs.

140. The most recent FSS performance (covering two years of delivery) has been outlined in both the annual and evaluation reports[31], which show that the

[31] https://www.gov.scot/binaries/content/documents/govscot/publications/research-and-analysis/2020/11/fair-start-scotland-evaluation-report-3-overview-year-two/documents/fair-

service has matured over the second year of delivery. Key local partnerships have been established and enhanced, participants value the support they receive, and continue to feel they are treated with dignity and respect.

141. The Scottish Government will continue to work with a range of partners to support the wider ambition of alignment and integration of employability services as set out in its No One Left Behind strategy. The Scottish Government also continues to work closely with DWP on delivering and improving FSS services, including increased joint partnership working to support under-represented groups.

142. Scottish Ministers are committed to supporting the continued development and delivery of devolved employability services. As part of the Scottish Government's economic response to the impacts of the COVID-19 pandemic, Scottish Ministers have extended the delivery of FSS services to end of March 2023 to allow for more people to benefit from support. In line with Scottish Fiscal Commission forecasts, a budget of £27 million has been allocated for FSS delivery in 2021-22, ensuring that support is available for those who face the greatest challenges to accessing the labour market.

start-scotland-evaluation-report-3-overview-year-2-november-2020/fair-start-scotland-evaluation-report-3-overview-year-2-november-2020/govscot:document/fair-start-scotland-evaluation-report-3-overview-year-2-november-2020.pdf

Fiscal Framework Implementation

The Fiscal Framework agreement between Scottish and UK Governments determines how the Scottish Government is funded, and underpins the powers set out in the Scotland Act 2016.

This chapter covers further areas of Fiscal Framework implementation relevant to this report: progress on policy spillovers; and the review of the Fiscal Framework.

Key developments

143. In August 2020, the Scottish Government agreed with the recommendation of the Advisory Group on Economic Recovery[32] to undertake the review of the Fiscal Framework as quickly as possible. The review should be robust and comprehensive, taking into account views from stakeholders. However, as the arrangements for the review depend on joint agreement with the UK Government, we rely on their commitment to achieve this ambition.

144. In October 2020, the Scottish Government and the Scottish Parliament's Finance and Constitution Committee and Social Security Committee published a joint report[33] to inform the review of the Fiscal Framework, and the independent report that precedes the review.

145. The Scottish Government continues to engage with HM Treasury to seek to progress the spillover claim in relation to UK Government increases to the income tax Personal Allowance. Further engagement will take place to resolve this issue as soon as possible.

Progress on policy spillovers

146. The Fiscal Framework makes provision for policy spillovers – instances when one government makes a policy decision that affects the tax receipts or expenditure of the other. In these circumstances the decision-making government should reimburse the other in cases of additional costs, or receive a transfer if there is a saving. Any decision or transfer relating to a spillover effect must be jointly agreed by both Governments.

Personal Allowance spillover

147. The Scottish Government continues to pursue a spillover claim in relation to UK Government increase to the income tax Personal Allowance.

[32] https://www.gov.scot/publications/economic-recovery-implementation-plan-scottish-government-response-to-the-advisory-group-on-economic-recovery/
[33] https://www.parliament.scot/S5_Finance/General%20Documents/Report(2).pdf

148. UK and Scottish Government Ministers agree that the impact of Personal Allowance increases on the Scottish Budget should be accounted for. However, UK Ministers believe that only above inflation increases should be accounted for. The Scottish Government believes that all increases in the Personal Allowance should be accounted for because there are relatively more basic rate taxpayers in Scotland than in the rest of the UK. Therefore, any decision to increase the UK-wide Personal Allowance will reduce Scottish tax receipts. This means that the Scottish Budget is made worse off by increases in the Personal Allowance. The Welsh Fiscal Framework provides an example of a more equitable framework, which deals with this issue by using a BGA that automatically accounts for the differences in the composition of the tax base.

149. The Scottish Government continues to engage with HM Treasury to seek to progress the spillover claim.

150. If no resolution can be reached, the matter becomes a formal dispute and would be referred to Ministers to be raised and discussed at a meeting of the Joint Exchequer Committee (JEC) as per section 99 of the Fiscal Framework.

Fiscal Framework Review

151. The Fiscal Framework agreement states that a review of the Fiscal Framework should be undertaken by the Scottish and UK Governments after the Scottish Parliament elections in 2021, and that this will be informed by an independent report, which will be presented to both governments by the end of 2021.

152. In April 2020, the Advisory Group on Economic Recovery (AGER) was established to provide the Scottish Government with expert advice on Scotland's path to economic recovery after COVID-19. The Scottish Government welcomed the findings of the report[34] and its recommendations. In relation to the Fiscal Framework review, the Scottish Government agreed that the review, and independent report which informs it, should take place as quickly as possible and be robust and comprehensive, particularly given the significant political and constitutional changes since the agreement was made, and in light of the recent and ongoing experience of COVID-19.

153. However, the arrangements for the review depend on agreement with the UK Government, so progress on scope and timing for the review relies on their commitment to achieve this ambition. The Scottish Government will continue to engage with UK Government in good faith and set out a clear vision of what is wants the review to achieve.

[34] Advisory Group on Economic Recovery - gov.scot (www.gov.scot)

Scope of the Review

154. The MTFS sets out the Scottish Government position on the scope of the review. It should include both an assessment of how the framework has operated to date, as well as a wider consideration of the levers that the Scottish Government has to manage the risks to which the Scottish Budget is exposed, particularly in light of the COVID-19 pandemic.

155. Ultimately, it should ensure that funding arrangements are fair; that budget volatility is minimised; and that the Scottish Government has the powers and flexibility to manage risks and to support economic recovery in the years ahead.

156. The Scottish and UK Governments have begun engagement to progress the arrangements for the review, with a view to reaching agreement at a future meeting of the Joint Exchequer Committee.

157. Beyond the input of the two governments, the Scottish Government recommends that stakeholders' views should also be an integral part of the process.

Finance and Constitution Committee, and Social Security Committee Joint Working Group Report

158. In October 2020, the Scottish Government, and the Scottish Parliament's Finance and Constitution, and Social Security Committees published a joint working group report[35], which identifies a number of issues arising from the operation of the Fiscal Framework to date that should be considered by the body tasked with delivering the independent report, and that should ultimately inform the review itself. The report, which has been shared with the Chief Secretary to the Treasury, sets out a number of issues and recommendations for consideration including:

i. **Structural risks** - demographic risks and risks relating to the distribution of the tax base in Scotland relative to the rest of the UK

ii. **Forecast risks** - risks relating to forecast error, and the impact on the Scottish Budget, including the potential divergence in forecast performance of the SFC and OBR.

iii. **Budget management tools and capital borrowing powers** - whether the limits and caps on the borrowing and reserve powers are sufficient to manage the volatility created by the framework; how these limits should evolve over time; and the merits of a prudential capital borrowing regime.

[35] Report(2).pdf (parliament.scot)

iv. **The no-detriment principle** - the reasonableness of the arrangements in relation to administration and implementation costs and how the policy spillovers provisions in the framework are operating.

v. **Policy autonomy and policy risks** - how the devolved and reserved tax and social security regimes interact, and what changes might be considered to promote better policy co-ordination and to limit constraints on policy autonomy.

vi. **Intergovernmental relations and dispute resolution** – the effectiveness of the dispute resolution processes and governance arrangements.

vii. **Transparency and accountability** – scope to simplify the framework, and ensure the timely provision of information on the operation of the Fiscal Framework to support wider understanding and scrutiny.

viii. **COVID-19** – to consider whether any longer term changes are required as a result of the experience of COVID-19.

Analytical programme

159. The Scottish Government has committed to develop a programme of analysis to identify further options for reform of the Fiscal Framework. The MTFS 2021 contains new analysis relevant to the operation and review of the Fiscal Framework, including:

- An assessment of the forecast error risk to the Scottish Budget; and
- Evidence in relation to the risks to Scottish Income Tax receipts, including sectoral impacts and impacts in relation to income distribution.

160. The analysis illustrates the existing limitations and operational risks of the Fiscal Framework, and demonstrates the importance of consideration of these issues as part of the Fiscal Framework review.

Scottish Government Budget 2021/22: Supporting the COVID-19 Recovery Consultation

161. In September 2020 the Scottish Government launched "Budget 2021-22: Supporting the COVID-19 recovery – Scotland's taxes and Fiscal Framework consultation[36]" to seek stakeholder opinion on the role of its

[36] Budget 2021/22: Supporting the COVID-19 Recovery - Analysis of Consultation Responses - gov.scot (www.gov.scot)

devolved taxes and the operation of the Fiscal Framework during COVID-19 and to support economic recovery.

162. Stakeholder responses noted fiscal challenges faced as a result of COVID-19 and the existing fiscal arrangements, as well as providing recommendations to mitigate some of these challenges. There was strong support from respondents for increased borrowing limits to allow the Scottish Government to support the economy in response to the COVID-19 pandemic. Some respondents supported greater fiscal autonomy on a more permanent basis, and some suggested more permanent changes to the Fiscal Framework that should be considered, while others noted that the current arrangements were adequate.

163. Further detail can be found in the Scottish Government's published analysis of the consultation.

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