

FINANCE COMMITTEE CALL FOR EVIDENCE

DRAFT BUDGET FOR 2013-14

SUBMISSION FROM ROYAL SOCIETY OF EDINBURGH

Summary

- The RSE urges the Scottish Government and Parliament to use this opportunity to reconsider the founding principles of the budget-setting process in Scotland, making it fit for purpose in a time of tightening public expenditure.
- It is essential that, when setting the Budget, the Scottish Government takes a strategic long-term view and links, in a transparent and consistent way, spending to outcomes within this strategic context. The RSE calls for the establishment of a Treasury function which would provide an objective and full cost-benefit analysis and opportunity cost analysis for each policy option in order that priorities can be set and choices made.
- The Scottish Government must also provide clear, transparent reporting on its spending and the impacts this has on the Scottish economy. This should include transparency and consistency on spending announcements and changes to proposed spending made throughout the year.
- With the information that would be made available through the above mechanisms, the Scottish Parliament, including the Finance Committee, would be able to take a significantly enhanced role in assessing and then approving the draft Budget and holding the Government to account for its spending.

Introduction

1. The RSE welcomes the opportunity to respond to the Finance Committee's call for evidence ahead of its scrutiny of the draft Budget 2013 – 14. This response has been produced by a Working Group of Fellows with appropriate expertise and experience in matters relating to the Scottish economy.

2. The RSE has previously provided comments to the Finance Committee on the Comprehensive Spending Review and draft budget 2012 – 13¹. Many of the key points made in that paper are still relevant. In particular, we stress the need for a strategic approach to be taken to ensure that spending decisions support the Scottish Government's key objective of achieving sustainable economic growth; the importance of priorities being set within that strategic context; and the necessity of a full cost-benefit analysis of policy options, supported by evidence. These matters are becoming increasingly urgent as constraints on public spending continue to tighten.

¹ "Scottish Budget Spending Review and Draft Budget 2012 – 13: a briefing for the Scottish Parliament's Finance Committee"; RSE, October 2011, http://www.royalsoced.org.uk/cms/files/advice-papers/2011/br11_05.pdf

The budget-setting process

3. As budget constraints tighten in the current and upcoming years, and the reality of cuts begins to take hold, the RSE strongly advises that the Scottish Parliament and Scottish Government take this opportunity to reconsider the founding principles of the budget-setting process in Scotland. A process which, since 1999, entailed agreeing the distribution of a Scottish Budget with year-on-year growth, is no longer fit for purpose in a time of decreasing public spending which requires difficult and far-reaching decisions to be taken.

The role of the Scottish Government

4. While the primary responsibility for the setting of the Budget must remain with the Scottish Government, this must be done in the context of a more strategic, long-term view than that which is encouraged by the current annual budget-setting timetable. Spending must be clearly and demonstrably linked to the Government's stated core objective of sustainable economic growth, with consideration given to the long-term implications of spending decisions. The current annual reports provided by the Scottish Government on its progress against indicators within the National Performance Framework do not link spending to outputs; nor does the Framework act as a mechanism through which choices between priority areas can readily and objectively be made.

5. Recognising that the prioritisation of some funding streams and projects over others is already both necessary and challenging, and will become increasingly so, the RSE calls for a Treasury function to be created within the Scottish Government, to be tasked with undertaking a full cost-benefit analysis and opportunity cost assessment of all policy options. Such analysis is the only means through which priorities can be rationally set and justified. If political sensitivities and potential ramifications restrict full public disclosure of difficult issues and choices by the Government, then an independent body, similar in status perhaps to the Office for Budget Responsibility at UK level, should be set up as a vehicle through which these discussions can take place. This function would greatly enhance public debate and understanding of the realities and implications of budget cuts and be able to answer the numerous questions put forward in the public arena, such as what the protection of funding for some flagship policies (connected to healthcare, universal benefits, higher education etc) means for the funding of other areas.

The role of the Scottish Parliament

6. With the detailed information made available through such full analysis as discussed above, preferably enhanced by analysis of the type and quality undertaken by the Institute for Fiscal Studies at the UK level, the Finance Committee would be in a much stronger position to fulfil its remit of examining the Scottish Government's spending plans. Both the Finance and subject committees would be better able to scrutinise the draft budget by portfolio and by line, with a full understanding of the options available, their costs, benefits and opportunity costs. This would facilitate more informed, higher quality debate on the draft budget by MSPs and allow parliamentarians to agree the budget on a portfolio/disaggregated basis, rather than merely approve the top line, which, fundamentally, is substantially set by the UK Government. This approach would also enable MSPs more effectively

to hold the Scottish Government to account on its performance against its spending decisions and to approve significant 'in-year' changes in resource allocation compared with the plans it has previously approved, in line with good parliamentary practice.

Reporting and monitoring of Scottish Government spending

The role of the Scottish Government

7. The onus for providing clear, transparent information on how the budget is spent, and what is being delivered by public spending, clearly sits with the Scottish Government. A key concern is the current lack of transparency and clarity around spending that hampers any external, objective analysis of performance. It should be possible to track the impact of spending announcements throughout the year, showing the source of funds and clearly identifying cross-overs and transfers between portfolios, and avoiding double counting of resources under more than one heading.

8. As previously stated, while the Scottish Government does provide an annual report on its progress against indicators in the National Performance Framework, this does not make any clear link between spending and outputs. Such linkages are crucial for both the Government itself and for the bodies which hold it to account to be able to evaluate the impact of spending decisions. The RSE suggests that the Scottish Government undertake to provide clearer reporting on its spending at all levels (from portfolio budgets to spending programmes to individual activities), including changes that occur throughout the year, and on the direct impact such spending is likely to have on Scotland's economic growth.

9. The Auditor General for Scotland's report on the Scottish Government's consolidated accounts 2009/10² analysed spending against the original budget. One key conclusion was that most changes are made through the Autumn and Spring Budget revisions, but it was not always clear from the documents which Level 3 budgets - i.e. the budget level which typically reflects individual activities - were affected. Most changes were transfers within portfolios but there was little explanation of why the changes were necessary, making it difficult for informed scrutiny to take place. The report highlighted the need for improved clarity of reporting to Parliament of the reasons for proposed budget changes and the provision of more detailed financial information to Parliament on outturn against budget. While progress may have been made along these lines since 2010, there remains scope to do more.

The role of the Scottish Parliament

10. With mechanisms in the budget process to ensure that the Government provides the information called for above, the Finance and subject committees of the Scottish Parliament would be able more effectively to scrutinise draft budgets and monitor progress against current budgets. As discussed in paragraph 6, MSPs would be in a substantially stronger position to compare the Government's spending and 'in-year' changes to the budget that Parliament had approved. This would

² "The 2009/2010 Audit of the Scottish Government Consolidated Accounts"; Auditor General for Scotland; September 2010.

considerably strengthen the Scottish Parliament's role in holding the Scottish Government to account for its actions, spending and performance.

The Finance Committee's call for evidence

11. The questions set out in the Finance Committee's call for evidence ahead of its scrutiny of the Draft Budget 2013 – 14 are exactly those sorts of questions that could be more fully and properly answered if the mechanisms and processes suggested above were in place. These would ensure that information on the analysis of policy options and reporting are provided by the Scottish Government or appropriate independent bodies. With the current lack of transparency surrounding progress made in the first year of this Spending Review period, and ahead of the publication of the Draft Budget 2013 – 14, it is difficult to provide detailed responses to the issues raised in the questions. However, a number of comments relevant to the questions are set out below.

Question 1: the alignment of spending decisions with the goal of increasing sustainable economic growth

12. It would be useful to see a cost-benefit analysis of the Scottish Government's spending decisions against its stated core objective of sustainable economic growth. The general areas which would be expected to support long-term economic growth include training and skills development, capital spend on infrastructure, and a supportive business environment. However, in the current economic climate, even within these areas, priorities must be set. For example, the RSE is supportive of the Scottish Government's announcement at the time of last year's budget that it planned to transfer revenue funds to capital investment in infrastructure. However, whether and to what extent this has been realised, and the impact it has had, are not clear. Furthermore, not all infrastructure projects will stimulate equal long-term economic activity and therefore clear and transparent priorities must be established. We note that the Infrastructure Investment Board has been set up to monitor spend in existing projects and this seems to be working well. There may be a case to be made for the remit of the Board to be expanded to consider strategic infrastructure investment for Scotland, though its membership might have to be reviewed if it were; and consideration should also be given to its relationship with the Scottish Futures Trust.

Question 2: harnessing the public sector to support sustainable economic growth

13. As detailed above there is a need for proper financial reporting on the impact of the public sector in driving sustainable economic growth before its performance can be properly assessed. Therefore, we limit our response to this question to highlighting two key issues. First, we are concerned by the findings of an Audit Scotland report into the transfer of economic planning powers from Scottish Enterprise to Community Planning Partnerships (CPPs)³ which indicates that the quality of economic planning across CPPs is variable and often poor. This cannot be of benefit to Scotland. Second, we note that the Sustainable Procurement Bill will be coming before the Scottish Parliament next year and could be a powerful tool in

³ "The role of Community Planning Partnerships in economic development", Audit Scotland, November 2011, http://www.audit-scotland.gov.uk/docs/central/2011/nr_111103_community_planning.pdf

harnessing the potential of the public sector to drive sustainable economic growth. We look forward to seeing the details of the Bill.

Question 3: structural change in Scotland's sustainable growth rate

14. As mentioned in paragraph 12, the RSE considers spending priorities for long-term growth must include:

- spending on quality infrastructure that will stimulate long-term economic activity;
- training programmes and skills development at all levels; and
- a supportive environment for business and entrepreneurialism and creativity/innovation more generally.

15. Comments have already been made on the need to analyse and compare the costs, benefits and opportunity costs of infrastructure programmes in order to prioritise those that will have the greatest economic impact. In relation to training and skills, we note that while funding for the Higher Education sector has been protected to a certain extent (including with respect to tuition fees), the Further Education sector has been significantly impacted by spending cuts. The long-term implications of this on the delivery of skills required by particular industries must be considered.

16. In our paper to the Finance Committee last year, we also highlighted the inconsistency of policy decisions in relation to the business environment. In autumn 2011 the Scottish Government put forward a case for the devolution of corporation tax as part of the Scotland Bill, making clear its intention to reduce the tax rate if it were in the Government's power to do so⁴. However, the Scottish Government does have responsibility for non-domestic rates and is continuing to increase these each year. As non-domestic rates, unlike corporation tax, must be paid by all businesses, regardless of profitability, such increases act as a burden to those companies already struggling in the economic downturn.

Questions 4 and 6: equity and economic growth and the role of preventative spending

17. The RSE suggests that two key priorities for the promotion of equity in Scottish society and the Scottish economy are a focus on funding of early years development and skills development at all levels (see comments in paragraph 15). It has been widely recognised by all political parties in Scotland that preventative spending, including support for families and children from as early as pregnancy stage, is a vital, if challenging, shift in spending priorities that can deliver improved outcomes and equity in key areas such as health, social care and education.

18. However, while there has been a stated commitment to preventative and early years spending, it is difficult to identify the level of real funds dedicated to this purpose or to analyse progress over the relatively short time period that preventative spending has been on the agenda. Further comments on the role of preventative spending can be found in our response to the Finance Committee on the 2012 – 13

⁴ *Scottish Government Press Release 'Corporation Tax'*, 8 September 2011, <http://www.scotland.gov.uk/News/Releases/2011/09/08100944>

Budget and in our more recent response to the Finance Committee on fiscal sustainability in the face of demographic change and ageing population⁵.

Impact of budget cuts

19. Finally, the RSE would emphasise the need, both in the setting and scrutiny of the Draft Budget 2013 – 14, for informed discussion on the changing profile of budget cuts as we enter the second year of the Spending Review period, with spending constraints becoming more pronounced. The Scottish Government and the Scottish Parliament must consider the annual budget in relation to what has been happening and what is likely to happen in coming years, for example on-going flat revenues for local authorities and most public bodies, negative revenue for the Further Education sector and ‘flat real’ for the Health sector. It must be made clear to the public what this means on the ground, the difficult decisions that must continue to be made, and the impacts of the Government’s choices. While the Finance Committee’s questions focus on the spending that may be needed in the areas of promoting equity, preventative spending and providing opportunities for those with high levels of multiple deprivation, its scrutiny of the Draft Budget must carefully consider where cuts are to be made and what the impacts of these cuts will be.

Additional Information

Related RSE Advice Papers:

- Advice Paper 12-07; *Fiscal Sustainability – demographic change and ageing population: a response to the Scottish Parliament’s Finance Committee*; August 2012.
- Briefing Paper 11-05; *Scottish Budget Spending Review and Draft Budget 2012 – 13: a briefing for the Scottish Parliament’s Finance Committee*; October 2011.
- Advice Paper 11–12; *Preventative Spending in the 2012 – 13 Draft Budget and Spending Review: a response to the Scottish Parliament’s Finance Committee*; September 2011.

Advice Papers are produced on behalf of RSE Council by an appropriately diverse working group in whose expertise and judgement the Council has confidence. This Advice Paper has been signed off by the General Secretary.

Responses are published on the RSE website: www.royalsoced.org.uk.

⁵ “*Fiscal Sustainability – demographic change and aging population: a response to the Scottish Parliament Finance Committee*”, RSE, August 2012, http://www.royalsoced.org.uk/cms/files/advice-papers/2012/AP12_07.pdf