



OFFICIAL REPORT
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Finance and Constitution Committee

Wednesday 15 March 2017

Session 5



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FINANCE AND CONSTITUTION COMMITTEE
9th Meeting 2017, Session 5

CONVENER

*Bruce Crawford (Stirling) (SNP)

DEPUTY CONVENER

*Adam Tomkins (Glasgow) (Con)

COMMITTEE MEMBERS

Neil Bibby (West Scotland) (Lab)
*Willie Coffey (Kilmarnock and Irvine Valley) (SNP)
*Ash Denham (Edinburgh Eastern) (SNP)
*Murdo Fraser (Mid Scotland and Fife) (Con)
*Patrick Harvie (Glasgow) (Green)
*James Kelly (Glasgow) (Lab)
*Liam Kerr (North East Scotland) (Con)
*Ivan McKee (Glasgow Provan) (SNP)
*Maree Todd (Highlands and Islands) (SNP)

*attended

THE FOLLOWING ALSO PARTICIPATED:

Scott Mackay (Scottish Government)
Derek Mackay (Cabinet Secretary for Finance and the Constitution)
Kerry Twyman (Scottish Government)

CLERK TO THE COMMITTEE

James Johnston

LOCATION

The David Livingstone Room (CR6)

Scottish Parliament

Finance and Constitution Committee

Wednesday 15 March 2017

[The Convener opened the meeting at 10:00]

Decision on Taking Business in Private

The Convener (Bruce Crawford): Good morning and welcome to the ninth meeting in 2017 of the Finance and Constitution Committee. Neil Bibby has provided his apologies.

Under agenda item 1, do members agree to take item 4 in private?

Members *indicated agreement.*

The Convener: Thank you.

Subordinate Legislation

Budget (Scotland) Act 2016 Amendment Regulations 2017 [Draft]

10:00

The Convener: Agenda item 2 is consideration of the Scottish statutory instrument that seeks to amend the Budget (Scotland) Act 2016. We will consider the motion seeking approval under item 3, but first we have an evidence session on the draft regulations.

I welcome Derek Mackay, Cabinet Secretary for Finance and the Constitution. Mr Mackay is joined by a couple of his colleagues from the Scottish Government. Scott Mackay is the head of finance co-ordination and Kerry Twyman is the deputy director of finance programme management. I welcome all the witnesses to the meeting.

Cabinet secretary, do you wish to make a short opening statement?

The Cabinet Secretary for Finance and the Constitution (Derek Mackay): Yes please, convener.

The spring budget revision provides the final opportunity to formally amend the Scottish budget for 2016-17. This year's spring budget revision deals with four different types of amendment to the budget—first, a few funding changes; secondly, a number of technical adjustments that have no impact on spending power; thirdly, some Whitehall transfers; and finally, some budget-neutral transfers of resources between portfolio budgets, including a modest budget redirection to ensure that we maximise our available budget. The net impact of all those changes is an increase of £372.1 million in the approved budget.

Table 1.1 on page 5 of the supporting document shows the approved budgets following the autumn budget revision and the changes that are sought in the spring budget revision. The supporting document to the spring budget revision and the brief guide that my officials have prepared provide background information on those net changes.

The first set of changes comprises mainly the £100 million capital stimulus allocations that the First Minister announced in September 2016 along with the £23.8 million that has been allocated over a number of lines as detailed in the brief guide. In total, those changes increase the budget by £123.8 million.

The second set of changes comprises a number of technical adjustments to the budget. They are mainly non-cash and therefore budget neutral as they cannot be redeployed to support discretionary spend elsewhere, and they have a net positive

impact of £221.5 million on the overall aggregate position. It is necessary to reflect those adjustments to ensure that the budget is consistent with the accounting requirements and the final outturn that will be reported in our annual accounts.

The largest of those changes relates to an increase of £50 million that is required for the non-cash student loans resource accounting and budgeting charge to better align the budget with the actual requirement. Again, that is a technical adjustment to the budget and the increase in funding cannot be used to support discretionary spending elsewhere.

The Scottish budget aligns with the accounting requirements under the Government financial reporting manual. Accordingly, budget provision is included in the Scottish budget for the financial year to reflect the recognition of relevant health and prison assets within revenue finance infrastructure schemes, in accordance with the accounting requirements. The adjustment to the budget at the spring budget revision is £20.6 million. Other technical adjustments include increased annually managed expenditure budget cover for provisions around impairments and fair-value adjustments and other non-cash adjustments to portfolio budgets.

With regard to Whitehall transfers and allocations from Her Majesty's Treasury, there is a net positive impact on the budget of £26.9 million. That includes additional funding of £5 million for the HM Treasury contribution to the V&A museum in Dundee and the Burrell renaissance project.

The final part of the budget revision concerns transfers of funds within and between portfolios to better align the budgets with profiled spend. There are a number of transfers between portfolios as part of the revision process, and they have no overall impact on spending power. The main transfers between portfolios are noted in the SBR supporting document and the guide to the SBR. In line with past years, there are a number of internal portfolio transfers that have no effect on portfolio totals but ensure that internal budgets are monitored and managed effectively.

As previously mentioned, the committee will wish to note that, as part of a robust budget management process and in line with good practice, we have taken the opportunity at the spring budget revision to redeploy some budgets to meet emerging pressures. As always, we will proactively manage the flexibility that is provided under the budget exchange mechanism that was agreed between HM Treasury and the devolved Administrations.

I confirm that, as has been done in previous years, it is my intention to make a statement to

Parliament on provisional outturn in respect of both the Scottish Parliament budget and the HM Treasury budget. The brief guide to the spring budget revision that my officials have prepared sets out the background and the details of the main changes that are proposed, and I hope that colleagues have found that helpful.

The Convener: Thank you, cabinet secretary. You mentioned a couple of times the Whitehall transfers and the allocations from HM Treasury. What stipulations are attached to those transfers? Are they essentially ring fenced for the purpose that is outlined? Is there any flexibility at all?

Derek Mackay: No. They are specifically for particular functions, as detailed. It is as simple as that.

The Convener: That was a pretty straightforward answer.

Quite a number of the budget transfers are recurrent. Do you agree that, if they are recurring annually, it would help to mitigate some of the confusion around the actual position of certain budgets if they were included in the draft budget document?

Derek Mackay: There are two categories. One is recurring transfers, and trying to incorporate them at the earlier stage would make sense. That is a fair comment. Maybe the budget review group will consider that, and we can then reflect on it. We have tried to look at recurring budget lines and incorporate them, where that makes sense, rather than having the change process.

Keeping the existing approach might still make sense for the other category, which is where portfolio holders commission services. The best example that I can give is the training of nurses. It looks as if that goes across the health and education budgets. There is a clear education function, but it obviously supports health. There will be examples where it makes sense to keep the approach, but where the committee believes that we should try to incorporate more, we should do that.

As I said, there are two categories, but I am happy to reflect on the issue further if the budget review group thinks that that would help with transparency. There are examples where transfers have recurred every year and examples where one portfolio essentially procures a service from another.

The Convener: I understand that. Will you talk us through the decision-making process for allocating funding changes during the year? There are members here who have not always been on the committee and it would be helpful for them to understand the Government's process in allocating the transfers.

Derek Mackay: Maybe my officials can cover some of that. From a political point of view, there will be natural underspends in some places and overspends in other places. That can be across Government, within portfolios or even within projects. As we manage the overall multibillion-pound budget, there will be changes within it to reflect the actual spend requirement and deliver on the Government's policies at the most basic accountancy level.

Kerry, would you like to cover the detail?

Kerry Twyman (Scottish Government): Yes. That is absolutely right. We monitor everything closely across the Scottish Government on an ongoing basis, so we are very aware of where projects are slipping and where there are additional pressures elsewhere in demand-led budgets. We manage everything closely to keep within our overall allocations. Where we see some underspend emerging, we match that to where the need is to ensure that we end the year at a precise position and we do not lose any spending power over the year.

James Kelly (Glasgow) (Lab): Good morning, cabinet secretary. In looking at the figures, I was surprised to see an emerging underspend in the housing line, bearing in mind that housing is a major issue and that there is support across the Parliament for house building, not only to address the housing shortage but to support the construction industry. Will you explain the background to that?

Derek Mackay: That is a fair question. There are two elements. The smaller element is the higher-than-expected level of receipts from the sale of homes. The larger element is how we profile the spend on delivering the housing target. There is no question but that we are working towards meeting our housing target, but how that is profiled and how money is spent in the housing portfolio is being managed.

We have set a figure and people are working towards that ambitious target, which runs to 2021. It is simply a question of the way that people have profiled the spending of the money over that period. It does not all need to be spent in the first year. Obviously, spend will increase as we go into each year to deliver that target.

James Kelly: I am still somewhat surprised. Your target is to reach 35,000 houses by 2021, but recent figures show that, at this stage, you have only 6,000 forecast completions. I understand that there will be more spending to push that up, but that figure seems relatively low at this stage in the process. I am surprised that the underspend was not reallocated to other projects in the housing sector.

Derek Mackay: The programme will escalate as we make progress, do the necessary preparatory work, make the investment and build things up. I again reassure Mr Kelly that we will meet our target. This is just about how housing has been delivering the spend to do that—there is no question of our renegeing on the target or moving back from it. This is about how the spending has been profiled. Kerry Twyman can give you more technical detail.

Kerry Twyman: On your point about reallocating funding to other housing projects, the vast majority of such projects require quite a long lead-in time for planning, procurement and so on. The cabinet secretary is absolutely right: we will ensure that the targets are met and the funds made available in the following year, but we will reallocate the money to an area that can use it in year. The worst-case scenario would be that we reallocate the money to another large capital or housing project that then slips, that we find ourselves at year end with a double slippage and that the funding is lost. We are careful to ensure that, when underspends emerge, we reallocate the money to where it can actually be used.

James Kelly: Just to be clear, can you tell me where the £21.5 million has been reallocated to?

Scott Mackay (Scottish Government): It is part of the full reallocation that is set out in the brief guide. There is a whole list—

James Kelly: I have seen the list. So the money has gone against one of the projects, such as the farmers payments or something like that.

Kerry Twyman: It would not be farmers payments, because they come under financial transactions. It would have been one of the other capital reallocations that are shown in the list.

James Kelly: We have a table that sets out a list. I highlighted one example from it, and you said that the money has not gone there. Where might it have gone?

Derek Mackay: We should make it clear that it is not the case that a specific line goes from one project to another; it will contribute to the overall capital. It is not possible to say that it has gone specifically from project A to project B. It just goes towards the overall funding underspend.

James Kelly: I understand that. I see from the table that there are credits and debits and that moneys coming out of underspends have gone into other projects. One of the main beneficiaries in that respect has been farmers loans. Kerry Twyman said that this underspend has not gone there, so am I right in saying that it has gone across to another line in the table, such as police and fire pensions or Angus Growers? Is that a fair comment?

Kerry Twyman: Again, it is probably not as simple as that. As we have said, the money may have gone to other capital projects that have then released financial transactions to be put against farmers loans. We may have re-evaluated how we are scoring things and exactly how projects are being funded. There is no direct read-across in the list with regard to where the money has gone.

James Kelly: I understand that there is no direct read-across in the sense that you are not transferring £21.5 million to a discrete project. The point is that there are not that many projects in the table. I highlighted one example and you said that the money has not gone there. Is it fair to say, then, that it has been reallocated across the other lines?

Derek Mackay: I think that it is fair to say that it will have gone towards funding the rest of the capital programme. We are talking about the global figure.

James Kelly: Okay. I will leave that question there, convener, but the point remains that, as a committee member and a regional MSP for Glasgow, I am concerned that the housing budget this year has not been fully spent.

The Convener: Forgive me—I do not have the information in front of me—but what is the housing spend in the draft budget? If I remember rightly, it was close to 700 million quid. I just want to understand the scale of the £21.5 million against the overall housing spend.

Kerry Twyman: The overall budget was £703.3 million, so the £21.5 million is a very small percentage of it. I add that, with large capital projects, we always expect some shift in timing.

The Convener: Okay. That has helped me to understand the perspective. James Kelly, do you have a second question?

James Kelly: Sorry—does the cabinet secretary have something else to say?

10:15

Derek Mackay: I just want to give the reassurance again. We have housing targets and we will meet them, but we will meet them with profiled spend that reflects what my housing colleagues believe is the right thing to do. We will not just spend the money because that is the figure that we have set. That is the requirement or the money that they believe they have to spend in the year to deliver on the overall commitment. Obviously, that means escalation going forward. We are not talking about future years' budgets today, but that will be reflected in them.

James Kelly: I will move on to another issue. In the justice portfolio, there has been a transfer of

£52.6 million from the police change fund to the Scottish Police Authority. Can you give us more detail on that?

Derek Mackay: Yes. It is a continuation of the funding for police transition, reform and VAT. It is a continuation of that approach.

James Kelly: What has been sacrificed to take £52.6 million out of the police change fund and move it to the SPA? What was planned as expenditure in that line that is now not needed or cannot take place?

Kerry Twyman: That line is specifically for the police change programme. Every year that line is set up specifically for that function. It is reform money that sits in the Scottish Government in that line and then is transferred in year. The reason why the money was not initially put into the SPA line is that every year the required amount is determined and then passed across to the SPA. That money was never intended for any purpose other than police reform.

James Kelly: So it sits in the police change budget and is transferred over.

Kerry Twyman: Yes, based on the requirement that has been assessed.

Scott Mackay: It was always intended for that purpose.

James Kelly: Why was it split? Some £34.8 million was revenue and £17.8 million was capital, but it appears that, in the transfer across, it has all been allocated to revenue. What is the thinking there?

Scott Mackay: That is a technical adjustment that has to do with the way in which arm's-length bodies' budgets are presented in the Scottish budget documents. For the purposes of the budget document, all of SPA's budget is recorded as revenue, because it is not reflected in Scottish Government accounts as a direct capital expenditure. It is still in effect a capital grant, but it is an indirect capital grant as far as the core Scottish Government is concerned. It is not a change against our Treasury budgets, but it is presented as such in the Scottish budget documents. It does not mean that that money will not be spent on capital, but it is presented slightly differently in the document.

James Kelly: Are you saying that there is not a capital line and that it is all revenue?

Scott Mackay: That is how it is shown in the Scottish budget documents. The budget document has to align to the presentation that we show in our accounts. In our accounts, we record only capital expenditure that is directly undertaken by the core Scottish Government. That does not include capital expenditure that is undertaken by

arm's-length bodies, so it shows as revenue in the Scottish budget documents, but against our Treasury control aggregates it is still recorded as capital. It is a technical presentational difference rather than a substantive move between capital and revenue.

James Kelly: Are you saying that, although it is presented as revenue, that £17.8 million will in the end be spent against capital, albeit by an arm's-length body?

Scott Mackay: Yes.

Murdo Fraser (Mid Scotland and Fife) (Con): Good morning. I have a couple of questions in two distinct areas. The first relates to the £100 million capital stimulus funding that was brought forward in the current financial year, based on an underspend in the previous year. Can you give us an update on how much of that £100 million has been spent?

Derek Mackay: My understanding is that it either has been spent or is on track to be spent. It is as clear as that.

Murdo Fraser: So you expect it all to be spent by the end of the financial year.

Derek Mackay: Yes. There are some elements for which there might not be total payment.

Kerry Twyman: Yes. We expect it all to have been passed across to the relevant bodies by the end of the year and we expect the projects to be virtually completed by then. We will assess that when we come to do the final accounts and the provisional outturn.

Murdo Fraser: Given that this is capital stimulus funding that is intended to stimulate the economy, do you do any assessment of its impact on the wider economy?

Derek Mackay: That is a good question. We have not done an assessment of the impact since the decision, but to arrive at that £100 million, we went through an assessment of how the resource could best be used. There was a range of factors, such as how quickly the money could be spent, geographic interests and return on investment. We went through an approach to make sure that the money would be well spent and I am happy to share that with the committee, but we have not done a post-spend analysis.

There are interesting lessons in it for us all about determining spend and what gives greatest value, but we used a particular approach using our economists as well as a range of other factors.

The Convener: It would be helpful if you could show the committee that.

Derek Mackay: Yes.

Murdo Fraser: If the Government has the capacity to do some work after the event, convener, it would be interesting to see whether the spending has had the desired outcome in line with expectations.

Derek Mackay: Sure. Again, that is a fair point. We are talking about £100 million that lies within a much more substantial spend, but I will take the point forward about assessing Government expenditure and looking at the impacts to see what gives us the greatest return.

Murdo Fraser: Thank you. I want to move on to a different issue, which is loans to farmers. In the funding adjustments, a financial transaction of £48.5 million is shown, if I read that right. Is that to do with the failures in the common agricultural policy information technology system?

Derek Mackay: Yes, this is about the CAP payments that have not been delivered in the fashion that the Government would have liked. The issue is not new; Mr Ewing has reported on it to Parliament. The money was for the financial transactions that allowed us to make loans in advance of farmers getting their payment. Farmers warmly welcomed having that certainty and getting those payments from us in advance.

Murdo Fraser: Looking at the transfers, I see that there has been a transfer of £7.5 million from the economy, jobs and fair work portfolio to the rural economy and connectivity portfolio for loans to farmers. If I read it correctly, part of that £48.5 million is £7.5 million that is being taken out of the economy department funding. That means that, because of failures in the IT system, the economy portfolio is down £7.5 million that could have been spent on other things. Is that right?

Derek Mackay: Scott Mackay can cover the detail of the budget line transfer, but the £7.5 million has been deployed from FT underspend and targeted for this purpose. When the CAP loans are repaid, the money for financial transactions is recovered. There is a timing issue around whether it is in this financial year or the next but, because of our budget exchange mechanism and the rules around FTs—the limit that we were allowed to carry forward was increased by the UK Government at our request—there is essentially no loss, because the money is paid back and we can redeploy it to financial transactions.

Murdo Fraser: I understand that. I am looking at the internal transfer from economy, jobs and fair work to rural economy and connectivity, which is £7.5 million.

Derek Mackay: Are you referring to the main document, Mr Fraser?

Murdo Fraser: I am looking at the Scottish Parliament information centre briefing. I will see whether I can find it in your document.

The Convener: It is mentioned on page 2 of the supporting document.

Derek Mackay: To be clear, there is no loss of money; it is simply a policy reallocation.

The Convener: The money goes out from the economy side to the rural payments side and will come back in once the loan is repaid. Is that effectively the situation that you are describing?

Derek Mackay: Yes.

Scott Mackay: The funding will be recycled as the loans are repaid. As the cabinet secretary and my colleague have said, it is about maximising the effective use of the budget over the piece and drawing funding from emerging underspends across a range of areas and redeploying it to maximise its effectiveness in line with emerging pressures.

Murdo Fraser: My only observation is that, given the importance of the economy portfolio to the Government's objectives and to Scotland's wider economic interests, £7.5 million is a fairly chunky sum of money to take from the economy portfolio. That money that is not available to spend by the department, because it is being transferred over to deal with the loans to farmers issue.

Derek Mackay: I will just check whether this is to do with the financial transactions element. The financial transactions for some schemes are demand led. It has been a Government priority to ensure that we assist farmers in relation to the CAP payments. That money has gone into the economy, albeit to the rural economy, because a policy decision was taken to respond to that issue. Because there was not demand for certain FT budget lines, funding became available for us to use them for this purpose, which is clearly a priority.

Murdo Fraser: Are you able to provide in writing to the committee more information about how the underspend arose in the economy department?

Derek Mackay: On the FTs, yes, I can do that.

Murdo Fraser: Thank you—that would be helpful.

Willie Coffey (Kilmarnock and Irvine Valley) (SNP): I note that any transfers into the rural economy were certainly welcome in my part of Scotland.

On page 9, the SPICe paper refers to a net increase of about £22.8 million in the allocation to local government, which is very welcome. Is that on top of the £160 million extra that you allocated

to local government? What is the nature of the £22.8 million adjustment?

Derek Mackay: The £22.8 million budget revision is for the current financial year. Additions are made to local government funding during the year. Some of that comes from portfolios, and some of it might be a consequence of spending decisions. However, as we have described in previous debates on local government finance, the additions relate to decisions that are taken subsequent to the draft budget or on the portfolios. That is not the case with the £160 million, because it is for the next financial year.

Willie Coffey: Do the adjustments include any stipulations or is local government free to choose how it deploys the funds that it receives?

Derek Mackay: A range of funds go to local government from the overall grants settlement; there are also ring-fenced funds. In the same way that I described earlier, a policy decision might be taken that a specific portfolio funds local government. That could be on a range of actions covering a number of local government functions.

Kerry Twyman: The two key transfers—and the bulk of the transfers—were the £10 million for maintaining teacher numbers and the £5 million towards support for the one-plus-two language policy. You will be aware of the discussions on those two areas.

Derek Mackay: The detail is in the communities section in the supporting document.

Scott Mackay: There is a list of the individual transfers that make up the funds on page 48 of the SBR document.

The Convener: As there are no further questions, we move to item 3, which is consideration of motion S5M-04150.

Motion moved,

That the Finance and Constitution Committee recommends that the Budget (Scotland) Act 2016 Amendment Regulations 2017 [draft] be approved.—[*Derek Mackay*]

Motion agreed to.

The Convener: I thank the cabinet secretary and his officials. In the coming days, we will prepare a short report for the Parliament setting out our decision on the order.

10:29

Meeting continued in private until 10:41.

This is the final edition of the *Official Report* of this meeting. It is part of the Scottish Parliament *Official Report* archive and has been sent for legal deposit.

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