INTRODUCTION

1. CBI Scotland is an independent organisation funded by its members and representing firms from across the country of all sizes and from all industrial, commercial and business sectors.

2. The Scottish Government has a substantial remit and budget, and the freedom they have over how that expenditure is deployed means they can play a valuable and pro-active role in stimulating economic activity, particularly during the early part of the Spending Review period. Businesses contribute to the funding of the devolved government and public authorities through a range of taxes and charges, and their success or otherwise can be affected by the spending and taxation decisions taken. Businesses are also suppliers to the public sector, and the Spending Review will provide greater clarity on the intended plans and projects for the next three financial years which will allow firms to plan ahead accordingly.

3. Our members’ over-riding priority for the Budget and Spending Review - as set out in our Budget submission to the Finance Secretary in advance of his 21 September 2011 statement to Parliament - was that it helped galvanise future growth. Our members recommended that the way to do this was by: putting the devolved finances on a sustainable footing; reforming public services; keeping a firm lid on costs applying to businesses; investing in the economy; and promoting competition.

4. Longer term, CBI Scotland believes that a re-balancing of devolved spending is required with a greater proportion spent on investments that support wealth creation such as skills, innovation, and transport and communications infrastructure, as advocated by the Scottish Parliament’s Enterprise & Culture Committee in its 2006 report on business growth. We would encourage the Committee to question the Scottish Government over whether it shares this view and if so set out a timetable for achieving it.

5. We welcome this opportunity to contribute to the Committee’s scrutiny of the Scottish Government’s spending and taxation plans for the coming three years.

KEY MESSAGES

6. CBI Scotland fully endorses the Scottish Government's stated purpose of improving sustainable economic growth. Given the economic backdrop and state of the UK’s public finances, this Budget and Spending Review was always going to be challenging. There were a number of very welcome announcements in the Budget and Spending Review, but unfortunately also a ‘sting in the tail’ in the form of two unwelcome tax rises on business which should be reconsidered.

7. In line with our submission to the Scottish Government in advance of the unveiling of its spending plans, CBI Scotland believes Ministers should have taken a bolder approach to making savings in order to invest further in GDP-enhancing measures and also avoid the two new taxes on business.

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1 CBI Scotland’s 11-page submission to the Finance Secretary in advance of his 2011 Budget & Spending Review was published on 29 August 2011.
2 'The Scottish Economy: the priority of priorities: Agenda for a growing economy in Scotland’, CBI Scotland’s 2006 manifesto
COMMENTARY ON ASPECTS OF THE SPENDING REVIEW AND BUDGET

Capital expenditure
8. CBI Scotland is greatly encouraged that the Scottish Government has sought to switch money from revenue spending in order to enhance capital spending on important infrastructure projects such as renewables, affordable housing and transport. The announcements on transport projects such as the Forth Crossing, M8 Ballieston to Newhouse, Aberdeen Western Peripheral Route, and Edinburgh/Glasgow rail link, are all welcome and are projects that CBI Scotland has consistently supported. The capital projects identified in the Budget will provide much-needed employment in the short term and help to build Scotland’s economic capacity in the longer term, as well as minimising future maintenance bills and congestion. As highlighted previously by CBI Scotland, we would like the Scottish Government to make further progress on other key long term projects (e.g. dualling of the A9 to help unlock the potential of the North) and look forward to the next iteration of the Infrastructure Investment Plan providing clarity on the project pipeline for the decade ahead. The Scottish Government’s decision to supplement its traditional capital expenditure by leveraging in additional privately funded sources of capital through its NPD programme, and to fund this using revenue expenditure, is the right course to pursue. This represents investment that would otherwise not happen or not happen for a considerable period. We welcome the continued role envisaged for the Scottish Futures Trust, the proposed extension of the use of Tax Increment Financing, and the National Housing Trust (NHT) model for affordable housing.

Costs of government
9. The decision to reduce significantly some of the costs of government such as administration and through greater streamlining of back-office functions3 is necessary and welcome, and together with the potential asset sales identified recently by the Scottish Futures Trust, will help to minimise reductions in economically important areas of spending. The proposals to freeze the pay bill for a further year for core civil service4 and make public sector pensions more affordable - just as the private sector has had to do over recent years – are sensible given the proportion of overall spend that relates to the wage bill.

Public services reform
10. We endorse the themes underpinning the Scottish Government’s public service reform agenda – namely integration of services, investment in workforces, service standards and outcomes improvements, and preventative spending. However, Ministers have missed out an important ingredient for achieving improvements in service quality, innovation and cost reduction, namely greater competition5 in the delivery of public services. Once a decision is taken on whether a particular service is needed then government should be open minded about who would be best placed to deliver it. This was something the Scottish Government’s own Independent Budget Review was clear about when it advocated “a mainstream role” for the private sector in service delivery and specifically urged government and public authorities to regularly review this. We await clarity on whether or how the devolved administration will take this forward, along with the Christie Commission’s recommendation6 that there should be “competitive neutrality” between all potential

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3 The enterprise bodies are to be tasked with helping public bodies reduce overheads, letter from the Cabinet Secretary for Finance to CBI Scotland’s chairman, 21 September 2011
4 P17, SPICe briefing on 2011 Spending Review and Draft Budget
5 CBI Scotland outlined its recommendations for reforming the delivery of public services in its evidence to the Christie Commission.
6 Christie Commission report 2011, recommendation 7.26
suppliers of public services so that in-house bidders are not favoured over for-profit or not-for-profit suppliers.

Skills, education and innovation
11. Investment in learning and skills is vital if Scotland is to prosper and take advantage of the commercial opportunities our open access to global markets provides. The protection of the funding for higher education, at a time when the devolved administration’s own research\(^7\) shows Scotland is already behind its competitors in terms of university funding as a percentage of GDP, is welcome as is the case for Skills Development Scotland which provides welcome support for firms not least in helping to recruit apprentices and other talent. The success of Scottish business is greatly dependent on the research, innovation and graduate talent that is produced by our universities, and we welcome plans to expand the Interface service and innovation voucher scheme. We continue to believe however that a mixture of funding from the public sector and individual graduates should be forthcoming for our universities. The ‘Opportunities for All’ initiative appears valuable, and will ensure all 16-19 year olds are offered training if they are not in work or education, though we still await the detail on this.

Air Route Development Fund
12. The lack of any re-introduction in the Budget of an Air Route Development Fund (ARDF), as advocated in our August 2011 Budget submission to the Cabinet Secretary for Finance, is disappointing. An EU-compliant ARDF would help establish new international flight connections from Scotland to overseas business destinations and hubs, make it easier for firms to access markets and customers abroad, and help deliver the step change in Scotland’s export performance that will aid the rebalancing of our economy. This is all the more so given the UK Government’s short-sighted decision to restrict the ability of London’s key interlining airports to expand.

Ferries
13. The financial support on offer to fund ferry services to Scotland’s island communities is significant, however the Budget was a missed opportunity to extend consumer choice and encourage better value for money by encouraging a plurality of service providers.

Freight Facilities Grant
14. Support for the freight industry is set to reduce from £2.9m to £1.1m according to the budget document. We understand that this reflects a decision to end the Freight Facilities Grant which is disappointing and could undermine the effort to encourage firms to undertake a modal shift in freight transport from road to rail or water. The Mode shift Review Support Grant funding remains the same in cash terms we understand, however with inflation this represents a real terms decline in support year on year.

Broadband
15. We are pleased to see a continuing government policy and financial commitment to stimulating demand for competitively-priced broadband infrastructure and services. The establishment of the Next Generation Digital Fund for broadband infrastructure, and the aim to use it to leverage private sector investment in superfast broadband, is most welcome.

\(^7\) ‘Building a smarter future: towards a sustainable Scottish solution for the future of HE’, Dec 2010, p34
Scottish Water
16. Scottish Water has done well to improve its performance over recent years. However, CBI Scotland has advocated in the past – along with the Independent Budget Review and the Scottish Futures Trust - that Scottish Water’s investment intentions should be made less reliant on the public purse for two reasons - to minimise or avoid any collateral damage resulting from cuts and pressures in public spending, and to free up public money for spending on other GDP-enhancing capital investment. The Scottish Government’s decision to reduce its support for Scottish Water’s capital programme by £120m over the next three years is therefore concerning, as is its admission that as a result there are “risks … to the pace of delivery of the capital programme”. We must continue to have a modern and effective water and sewerage service for commerce and industry, particularly to the development industry given past fears over development constraints and which in time will impact on the initiatives pursued under the SFT and NHT, and every effort should be made to minimise the risk of any slippage in the pace of investment.

Business support, tourism & grants
17. CBI Scotland continues to support the Scottish Government’s focus on priority sectors deemed crucial to long-term economic performance, firms with high-growth potential, and on exports assistance. It is encouraging that the budgeted monies available for business support, tourism and grants to industry appear to have risen, and that the “operational spend” for the enterprise networks and VisitScotland has at least been maintained. That said, it is unclear from the data in the budget document whether funding for export assistance through SDI has been protected or enhanced, something CBI Scotland advocated in our evidence to the Economy Committee during its recent internationalisation inquiry, and which will be important to realising the target for 50% export growth by 2017. A question remains over how the boards of the various enterprise agencies will allocate and prioritise their spending and what this means for individual programmes. Given that the separate budget heading for Industry & Technology Grants is set to disappear, it is difficult to be clear exactly what will happen to this important funding stream, which declined last year by 10%. Grant schemes like RSA and SMART, and newer ones like WATERS and POWERS, are viewed positively by our members as a valuable means of encouraging industry to invest, expand and locate in Scotland, particularly in the low carbon economy, and even more so at a time of rising external finance premiums and tight credit markets. It is therefore encouraging to note the proposed doubling of support to the food & drink sector and the new £60m capital fund for offshore wind and marine technology.

Scottish Investment Bank
18. CBI Scotland is supportive of the Scottish Investment Bank’s Scottish Loan Fund, first unveiled in April 2010 by the First Minister, which is designed to complement more traditional forms of lending to businesses. In particular, we support the focus on exporters and firms with real growth potential since it is these companies who will offer Scotland the best chance of a return to sustainable growth.

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8 P191 budget document
9 Letter from Scottish Government Business Directorate Director to CBI Scotland, 21 September 2011
10 ‘£50m loads package to support jobs and investment’, Scottish Government press release, 21 April 2010
Enterprise Zones
19. CBI Scotland is open-minded about the proposed introduction of four Enterprise Areas, as a means of stimulating new additional economic activity, and recognise that the mixture of devolved and reserved powers involved will require both the Scottish and UK administrations working together to deliver them. However, it is surprising that there is a lack of information in the budget document as to the financial support that will be ploughed in to Enterprise Areas, e.g. in the form of business rates relief.

Prompt payment
20. CBI Scotland supports the Scottish Government’s efforts to ensure it and its agencies settle supplier invoices within 10 days, aiding the cash flow of its suppliers. Significant progress has been made. We would ask that the Committee monitors this, as it builds on the principles which underpin the widely adopted ‘CBI prompt payment code’.

Planning
21. The total to be spent on planning is set to fall by a further 15% over the next three years, and comes after last year’s reduction by a fifth. While fully recognising that most of the delivery of planning is the responsibility of planning authorities, our concern is that these reductions in budget may be premature and counterproductive given that: (1) our members believe there has yet to be a significant and lasting improvement in the performance of the planning system, (2) the need to facilitate much needed private sector investment (e.g. in energy) let alone the Scottish Government’s own enhanced capital programme, and (3) the poor signal it sends to planning authorities who might decide to follow suit. For example, the latest official data shows only a modest improvement in the number of major commercial and industrial applications which are dealt with timeously, with fewer than half being dealt with within the four month target period. Ministers should give further consideration to introducing a Business Rates Incentivisation Scheme in order to incentivise local authorities to consent more commercial and industrial applications.

Scottish Variable Rate
22. We applaud the decision to rule out the use of the Scottish Variable Rate, which the Christie Commission said could generate £1.2bn in new tax revenues, as its implementation could place a costly additional administrative burden on employers in both the public and private sectors.

Council Tax freeze
23. CBI Scotland supports the Scottish Government's ambition to freeze Council Tax, which increased greatly during the decade before it was frozen. A continued freeze will see public anxiety over the level of the tax lessen, and subsequently diminish any demands for wholesale changes in the form of tax applied and which might place the administrative burden for calculating and collecting any replacement tax onto employers.

Poundage rate party
24. CBI Scotland welcomes the Scottish Government’s pledge to maintain poundage rate parity with England, and the continued relief on offer to small firms (which is part funded by a supplementary levy applying to all larger firms with a rateable value in excess of £35,000). Keeping taxes down helps firms’ fund their investment

\[11\text{p91 Budget document}\]
\[12\text{p17 Budget document}\]
plans, crucial in an era when retained profits have become ever more important in financing future investment intentions, and helps maintain cash flow.

**Increased business rates on firms with empty commercial premises**

25. The decision to increase the tax paid by firms with empty commercial premises (e.g. offices, retail units, or licensed premises) is very concerning, and we specifically asked Ministers not to introduce such a tax increase in our submission to them ahead of the Budget statement. It is disappointing too that there is the dearth of information in the budget document on the rationale, how it will work, and the amount to be raised by this additional tax, although we have subsequently learned\(^{13}\) that it is anticipated to generate a total of £36m over two years from its introduction in April 2013. Commercial buildings and premises are rarely left empty by design, particularly as they do not generate an income, and this new tax could see private sector investment in new developments or regeneration projects curtailed, particularly in more economically-deprived areas which can be harder to let. This would be at odds with the Scottish Government’s stated ambition to “encourage new private investment”\(^ {14}\) and could undermine its proposed Regeneration Strategy\(^ {15}\). We would urge the Committee to ensure a full Business & Regulatory Impact Assessment is forthcoming.

**Increase in business rates on larger retailers**

26. CBI Scotland is extremely alarmed at the decision to levy a new business rates tax from next April on larger retailers which sell alcohol and tobacco (the ‘Public Health Levy’), and the uncertainty this unexpected announcement has caused. The distinct lack of information in the budget document concerning this levy is concerning, e.g. how much will it generate in tax revenues, how it will work, how it will be calculated, how much it will cost firms, how long it will apply for, which types of firms will it apply to, whether tiered or banded levels of tax will apply as per last year’s larger retailer levy proposal, whether it will be in addition to the existing 0.7p supplement used to part-fund the Small Business Bonus.

27. We share the Scottish Government’s view that “the ability of our businesses to grow and be successful will depend upon a competitive tax regime”\(^ {16}\), but this proposed levy is inconsistent with that aim. We have yet to hear a convincing explanation as to how the levy fits with the Scottish Government’s stated ambition from its 2011 Economic Strategy of “making Scotland the most competitive place to do business in the UK” let alone the promise in the Budget document to “make Scotland an outstanding destination for investment”.

28. The Scottish Government should be promoting Scotland as an attractive destination for business investment and job creation, but unfortunately this levy sends out the opposite message to potential investors, risks Scotland’s reputation as a welcoming destination for business investment, and undermines the credibility of efforts to tempt large retail inward investments to our cities. The levy marks a decisive departure away from the Uniform Business Rate and poundage rate parity with the rest of the UK, which business fought long and hard for and which our members want to see the government honour. Indeed, the Cabinet Secretary for Finance has himself lately described as “damaging”\(^ {17}\) the previous policy which saw Scottish-based firms put at a “competitive disadvantage for 7 continuous years” by having to

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\(^ {14}\) ‘A Scottish Budget for Growth’, Scottish Government, September 2012

\(^ {15}\) Scottish Government’s Budget & SR document, p17

\(^ {16}\) Scottish Government economic strategy 2011, p37

\(^ {17}\) Spending Review 2011 – Open letter to Scottish business, Scottish Government website, 30 September 2011
pay 10% more in non-domestic rates than their counterparts in England until 2007 - yet he is now advocating large retailers pay over 20% more than English counterparts for at least the next 3 years. Unpicking poundage rate parity opens the door in subsequent devolved Budgets to the retail levy threshold being lowered or other sectors being targeted with similar levies, particularly if the Government’s programme of spending reductions and efficiency savings fail to generate the desired savings.

29. An early announcement on the detail to provide predictability for firms’ budgetary planning purposes ahead of the new financial year which starts in a few months’ time is important. We note the suggestion put forward recently by the First Minister\textsuperscript{19} (in the context of the UK Government’s recent oil & gas levy) that changes in business taxation should be subject to a year’s “statutory consultation” before their implementation, and wonder why this does not seem to apply in this instance.

30. We would urge the Committee to ensure a full Business & Regulatory Impact Assessment (BRIA) is forthcoming on this new regulatory proposal so that the best practice guidance issued by the Regulatory Review Group and thrust of the Scottish Government’s own better regulation agenda (i.e. to genuinely consult with business prior to the introduction of new regulations) is adhered to. The BRIA would assess the direct and wider implications of this new tax, e.g. its potential impact on the construction and store fit-out sectors, employment, the potential to cede jobs to online retailers based out-with Scotland resulting in lower tax revenues\textsuperscript{20}, the cost of the added complexity to the system on non-domestic rates, and the implications for other government policy objectives such as Business Improvement Districts.

31. As a result of this new tax larger retailers may find themselves subject to four bills for business rates, i.e. their normal business rate; the 0.7p supplement that all medium and larger sized firms pay to co-fund the Small Business Bonus; a BID levy should they fall within the auspices of a Business Improvement District; and this new larger retailers surcharge. This comes on top of the removal last year of Transitional Relief in Scotland, which still applies south of the border and which capped and phased in large rises in rates bills. We are deeply concerned that this new levy will make it more expensive to invest in Scotland and could put at risk much needed investment from the retail sector, as larger retailers often have a choice of locations elsewhere in the UK or indeed abroad for their investments and will rigorously evaluate post-tax returns on their investment options.

CBI Scotland
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\textsuperscript{18} Scotland on Sunday article says retailers will pay 22% more in rates under the retail levy, 2 October 2011
\textsuperscript{19} 6 Sep 2011, STV news website: ‘Alex Salmond has launched a fresh attack on the UK Government’s decision to levy a windfall tax on oil companies, claiming it has led to offshore projects being cancelled.’
\textsuperscript{20} Report to the Finance Committee on the Draft Scottish Budget 2011/12 by Prof David Bell, November 2010