Finance and Public Administration Committee

Fiscal Framework Outturn Report

Briefing from the Scottish Parliament Information Centre's Financial Scrutiny Unit

What is the Fiscal Framework Outturn Report?

The Fiscal Framework Outturn Report (FFOR) was published on 30 September 2021. Publication of this report follows a recommendation of the Budget Process Review Group (BPRG) and is designed to support the Budget process by setting out the implications of outturn data for the upcoming Budget.

In essence, the purpose of the FFOR is to show how actual receipts collected for devolved/shared taxes compare with the forecasts made when the Budget was set. For Social Security powers, it shows how actual spend compares with forecasts made at the time the Budget was set.

Across the range of these devolved powers, the document sets out the level of either positive or negative reconciliation to be applied to the upcoming Budget.

The document also sets out the latest Scotland Reserve position (the Scotland Reserve is essentially the account into which underspends or surplus tax receipts can be placed), planned borrowing and overall borrowing levels relative to borrowing limits.

The thinking behind the BPRG recommending production of this document was that it would allow the Finance Committee to question the Cabinet Secretary around how the Government plans to handle any shortfall or surplus in the coming Budget.

Summary of key points

The BPRG final report recommended that the FFOR is published annually in September and is based on audited information as far as possible.

Due to a number of changes to previous publication schedules (outlined in the introduction to the FFOR) the majority of the outturn data used in this year's FFOR is provisional. As such the overall reconciliations applying to the 2022-23 Scottish

Budget are not final, and will only be confirmed when the 2022-23 Scottish Budget is published on 9 December.

Based on these provisional figures, the key points applying to the upcoming budget are as follows:

- A **total provisional negative reconciliation of £14.8 million**. This is the net figure across all the areas covered by the document – Income tax, Land and Buildings Transaction Tax (LBTT), Scottish Landfill Tax (SLfT), Social Security expenditure and the final BGA reconciliation for 2020- 21 Fines, Forfeitures and Fixed Penalties. This reconciliation figure will be taken from the 2022-23 Budget.

- In the context of the overall Scottish Budget, this is a relatively small sum and is significantly less than the -£319 million reconciliation which applied to the 2021-22 Budget, and the -£207 million which applied to the 2020-21 Budget.

- The document reports an expected balance in the Scotland Reserve at the end of this financial year of +£32 million. This is based on current plans and is subject to change as we move through 2021-22.

- Under current plans, the Scottish Government will have accumulated Capital borrowing of just under £2.5 billion by the end of 2022-23, 82% of its overall £3 billion limit. This is a sizeable share of the total capital borrowing available and may have implications for the Government's room for manoeuvre on Capital in the medium term.

- The Scottish Government plans to borrow £319 million in resource borrowing in the current financial year, which fully covers the negative reconciliation applied to the 2021-22 Budget.

Tax revenues, BGA and net Budget position

A key purpose of the FFOR is to report on outturn data for Scottish tax revenues, along with the outturn and final block grant adjustments (BGAs). This comparison of outturn revenue and BGAs with the forecasts made at the time of the budget allows the FFOR to identify the degree of 'reconciliation' that will be required in the subsequent budget.

For tax powers, Scottish budgets are now underpinned by two sets of forecasts.

- Forecasts for a block grant adjustment (BGA), which is an estimate of the revenue foregone by the UK in devolving tax powers to Scotland - these forecasts are undertaken by the Office for Budget Responsibility (OBR)
- Forecasts for the revenues to be raised by Scottish taxpayers based on Scottish Government policy decisions - these forecasts are undertaken by the Scottish Fiscal Commission (SFC).

The forecasts are reconciled with outturn data when that becomes available, so that the funding available to the Scottish Government ultimately corresponds to the actual revenues and BGAs.

As outturn data is available on different timescales for each of the taxes, there are different processes in place for how income tax is reconciled compared with the fully devolved taxes. For the fully devolved taxes, outturn data is usually available approximately 6 months after the end of the Financial year. For income tax, outturn data is available around 16 months after the end of the financial year. This longer lag time for income tax relates to the self-assessment income taxpayers having around 10 months after the end of the financial year to pay income tax dues.

Income tax

As members know, provisional outturn data for Income Tax for 2019-20 was published by HMRC on 22 July 2021. These will not be fully audited until October 2021, so the FFOR figures are based on the provisional data.

Table 1 shows that at the time the Budget for 2019-20 was set, the net effect on the Budget from Scottish Government policy was forecast to be £182.5 million. However, the outturn net effect on the Budget was £148 million, meaning that the Scottish Budget was better off by £148 million as a result of income tax being devolved. Because the Budget was set with forecasts assuming the Budget would be £182.5 million better off (but was only £148 million better off), there is a requirement for a negative reconciliation of £34.5 million to be made in respect of Income Tax to the Scottish Budget next year based on these provisional outturn figures (£182.5m - £148m = £34.5m.)

Table 1: Provisional Income Tax Reconciliation to 2022-23 Budget, £ million

2019-20 Income tax	Revenues	BGA	Net effect on Budget
Forecasts – Budget Act 2019	**11,683.6**	**-11,501.1**	**+182.5**
Provisional Outturn	**11,832.6**	**-11,684.6**	**+148.0**
Provisional Outturn against forecast	**+149.0**	**-183.5**	**-34.5**

This is a significantly smaller reconciliation than has been applied for income tax forecast errors in the previous two years for which the Scottish Government has set income tax policy in Scotland, and for which we have outturn data (see Table 2). Over the three years for which we have Scottish NSND income tax outturn data, there have been negative reconciliations totalling £547.5 million.

Table 2: Forecast error reconciliations since NSND Income tax devolved

Year tax collected	Reconciliations between Outturn and forecast, £ million	Year reconciliation applied to
2017-18	-204	2020-21
2018-19	-309	2021-22
2019-20	-34.5	2022-23
Total 2017-2020	**-547.5**	

Source: HMRC outturn data

The SFC's latest forecasts estimate that the 2020-21 Scottish income tax outturn data will for the first time result in positive reconciliations of £130 million which will be applied to the 2023-24 Scottish Budget.

Their latest forecasts for the 2021-22 income tax reconciliation (to be applied to the 2024-25 Budget) is a positive reconciliation of £851 million. This, however, comes with a significant health warning attached due to the differing economic prospects at the time in which the SFC and OBR have produced their most recent forecasts.

> "Our estimate of the reconciliation for 2021-22 is significantly affected by the forecast timing comparability issue. Given this, we do not think it's likely that the reconciliation will be as large as £851 million, and this is likely to be revised significantly downwards once updated OBR forecasts are available that are more comparable to our own latest forecasts."

Fully devolved taxes

Revenue Scotland manages and collects the fully devolved taxes (LBTT and SLfT) and these revenue streams feed in to the Scottish Budget as they are collected. This means **reconciliations for revenue are not necessary for these taxes**. The Scottish Government manages any variance between forecast and actual revenues as part of its in-year budget management process.

The pandemic had an impact on the revenues collected by these taxes. For LBTT, revenues in 2020-21 were £124.1 million lower than forecast when the Budget was set. For Landfill Tax, £9.6 million less was collected in Revenues in 2020-21 compared with forecasts when the Budget Act was passed in February 2020.

However, **the BGAs for these taxes do undergo reconciliations and are reconciled in two stages**. The first stage is an in-year reconciliation, which normally takes place within the same financial year, on the basis of updated OBR forecasts produced for the UK autumn fiscal event. Outturn data becomes available in the autumn following the end of each financial year. Using these outturn figures, a final reconciliation is applied to the Block Grant in the financial year two years after the original BGA was applied.

However, for LBTT and Landfill Tax, most of the reconciliation for 2020-21 happened within the financial year and has already been absorbed into Budgets.

Taking LBTT first, £166 million was added as an in-year BGA reconciliation in 2020-21, and thus has already been absorbed (offsetting the £124.1 million lower revenues mentioned above). The latest outturn numbers presented in the FFOR show that a very small final negative reconciliation of £6.1 million will now apply to the 2022-23 budget.

Total adjustments for LBTT are presented in table 3 below. It shows that LBTT revenues were £120.7 million higher than the BGA meaning that the Scottish Budget was better off from having this tax devolved. Table 3 also shows that a total BGA reconciliation of +£159.9 million has been added to the Scottish budget, which offsets a -£124.1 million shortfall in LBTT revenues against forecast. Although LBTT revenue fell in 2020-21, the Budget was protected by a more than offsetting BGA addition due to equivalent falls in the rUK equivalent Stamp Duty tax. Combined, this means that the reconciliation against forecast overall net effect on the Scottish Budget in 2020-21 from LBTT is +£35.8 million (see table 3 below).

Table 3: 2020-21 Provisional LBTT Outturn compared with Forecasts, £ million

	Revenues	BGA	Net effect on Budget
Forecasts – Budget Act 2020	**641.5**	**556.5**	**+84.9**
Provisional Outturn	**517.4**	**396.6**	**+120.7**
Provisional Outturn against forecast	**-124.1**	**+159.9**	**+35.8**

With SLfT, as with income tax and LBTT, the outturn data presented in the FFOR show that the Scottish Budget was better off from having SLfT devolved, with £19.4 million more being raised in this tax than being removed from the block grant. Table 9 of the FFOR shows that £0.4 million was added as an in-year BGA reconciliation in 2020-21, slightly offsetting the £9.6 million shortfall in revenues collected compared to forecasts. A further provisional final reconciliation of +£0.1 million is now required for 2022-23. This means that the reconciliation against forecast overall net effect on the Budget from SLfT is -£9.1 million (see table 4).

Table 4: 2020-21 Provisional SLfT Outturn compared with Forecasts, £ million

	Revenues	BGA	Net effect on Budget
Forecasts – Budget Act 2020	**115.9**	**-87.3**	**+28.5**
Provisional Outturn	**106.2**	**-86.9**	**+19.4**
Provisional Outturn against forecast	**-9.6**	**+0.5**	**-9.1**

Fines, Forfeitures and Fixed Penalties

Table 5 sets out the net effect on the Budget from Fines, Forfeitures and Fixed Penalties.

As can be seen, revenues came in £10.7 million lower than forecast, but that was partially offset by £4.1 reduction to the size of the BGA. The net effect on the Budget was a reduction of £6.6 million.

Table 5: 2020-21 FFFP Outturn compared with Forecasts, £ million

	Revenues	BGA	Net effect on Budget
Forecasts – Budget Act 2020	**25.0**	**-23.7**	**+1.3**
Provisional Outturn	**14.3**	**-19.6**	**-5.3**
Provisional Outturn against forecast	**-10.7**	**+4.1**	**-6.6**

Proceeds of Crime

The FFOR notes that

> "Revenue seized under the Proceeds of Crime Act 2002 is subject to a BGA. The basis on which this is carried out is the subject of dispute between the Scottish and UK Governments and the BGA remains at negative £4 million while the dispute remains unresolved. The Scottish and UK Governments agreed to consider this issue as part of the review of the Fiscal Framework."

And that:

> "No reconciliation takes place while the BGA remains the subject of dispute between the Scottish and UK Governments."

The Scottish and UK governments have been in dispute over this issue for some time now. It centres on how sums recovered under 'proceeds of crime' legislation (confiscation of money and assets that have been gained through criminal conduct) are budgeted for post-devolution.

Before sums raised from proceeds of crime legislation were officially devolved through Scotland Act 2016, the two governments had an agreement that the Scottish Government could retain sums raised through proceeds of crime in Scotland if these raised less than £30m in any year – which they always did. So HM Treasury never actually received any sums from proceeds of crime legislation in Scotland prior to their devolution.

But the devolution of proceeds of crime resulted in a formalised process by which the Scottish budget can be adjusted downwards to reflect the funding that the UK Government has ostensibly foregone as a result of devolving these funds.

Since 2018-19, rather than being able to retain revenue from proceeds of crime in Scotland – as would have happened pre-devolution – the Scottish Budget is having most of proceeds clawed back in the form of a reduced block grant.

The Scottish Government claims this breaches 'no detriment' principles. HM Treasury's view is that this is what the two governments have signed up to.

Social Security

For social security payments, forecasts are of spending rather than revenues and Block Grant Adjustments are therefore additions rather than deductions. Otherwise, the process of reconciling forecasts to outturn data functions in the same way as for the fully devolved taxes.

This paper does not go into the detail of these. The FFOR report (tables 13 and 14) sets out the position for each of the benefits. Some of these reconciliations are absorbed in-year (as with the devolved taxes), but there is a +£21.6 million reconciliation to be applied to the 2022-23 Block grant based on the latest provisional outturn information.

Net reconciliation requirement

Combining all of these reconciliations takes us to a net reconciliation figure to be applied to the 2022-23 Scottish Budget of £14.8 million.

Table 6: Total Provisional Reconciliation requirement for 2022-23 Budget

Power and year	Data	£ million
Income tax 2019-20	Provisional Outturn	-34.5
LBTT 2020-21 BGA	Provisional Outturn	-6.1
SLfT 2020-21 BGA	Provisional Outturn	+0.1
FFFP 2020-21 BGA	Outturn	+4.1
Social Security BGA	Provisional Outturn	+21.5
Total		**-14.8**

Borrowing

Capital Borrowing

Table 18 of the FFOR shows the Scottish Government's Capital borrowing plans. Key points are as follows:

- Under current plans, the Scottish Government will have accumulated Capital borrowing of just under £2.5 billion by the end of 2022-23, 82% of its overall £3 billion limit
- According to the table, in 2022-23 repayments for Capital borrowing will total just under £115 million
- No borrowing is assumed for 2023-24 onwards, although the policy set out in the MTFS was for annual borrowing of between £250m and £450m annually.
- Repayment periods for borrowing vary from 10 to 25 years.
- Interest rates for each year's borrowing are fixed and range from 0.6% to 1.9%

It is possible, perhaps likely based on previous years, that capital borrowing will tend to work out lower than plans, due to general slippage that can occur with capital budgets. The borrowing powers are useful as they allow the Scottish Government to plan to spend approximately 110% of their total capital budget, and then if slippage is 10% they end up back at their limit without needing to actually borrow.

Resource Borrowing

Limited information is provided on Resource borrowing (which can only be used for cash management and forecast errors). The document states that £207 million was borrowed to cover the negative reconciliations applied to 2020-21, and that the Scottish Government 'plans' to borrow £319 million to offset the negative reconciliation applied to the 2021-22 Budget, but notes that:

> "This borrowing has not yet been drawn down as borrowing drawdowns are subject to the in-year financial position."

Resource borrowing is repaid over five years, no information is provided as to the interest rate being paid on Resource borrowing already undertaken (ie the £207 million confirmed as being borrowed thus far) and how much is to be repaid in 2021-22, 2022-23 and beyond.

The document notes the following:

> "For future years, the Scottish Government will make a decision on whether and how to use resource borrowing based on the overall Budget situation."

Scotland Reserve

The Scotland Reserve position presented in the FFOR is the one reported to Parliament at the time of the Provisional Outturn in June 2021. The expected drawdown from the Scotland Reserve in 2021-22 is £599 million, which will take the balance at the end of this financial year to £32.1 million.

It does not set out any of the COVID consequentials that were carried into 2021-22 and have been allocated in the Autumn Budget Revision, published on 27 September. However, it does state that the final in-year update on the Scotland Reserve situation will come at the 2021-22 Spring Budget Revision (SBR) early next year.

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