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The Scottish Parliament
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Dear Convener,

Thank you for providing your Pre-Budget 2025-26 report, and for the opportunity to respond. I have attached a detailed annex to this letter, which responds directly to each of the points within your report. I would also draw to your attention the following overarching points.

The Committee focussed on the challenges facing the Third Sector in Scotland, in particular third sector funding. It stressed the need to deliver stability and certainty for the sector and reflected the breadth of evidence received by third sector organisation and representatives working in Scotland. I recognise many of the challenges and opportunities reflected in the Committee's report and continue to work with my officials to champion the voice of the sector across Government and ensure that the vital work of third sector organisations is well understood and valued as part of a thriving Scottish society.

The Scottish Government set out its commitment to Fairer Funding in 2022 and remains committed to improving grant making and funding relationship for the sector by the end of this parliament. The Scottish Government recognises the financial pressures on the Third Sector at this time and is concerned about the additional pressure that the UK Government's decision to make changes to employer national insurance contributions places on many organisations within the sector.

I hope that this information is useful, and I look forward to discussing these issues further when I appear before the Committee next month as part of your Budget scrutiny process.

Yours sincerely,

SHIRLEY-ANNE SOMERVILLE

SCOTTISH GOVERNMENT RESPONSE TO SOCIAL JUSTICE AND SOCIAL SECURITY COMMITTEE PRE-BUDGET REPORT 2025/26 – THIRD SECTOR FUNDING PRINCIPLES

Question	Draft response
<p>32. The Committee asks the Scottish Government what progress has been made in increasing the number of multi-year grants since December 2023 and how multi-year funding will be included in its Funding Principles. For example, will the Scottish Government stipulate funding should be for a minimum of three years.</p>	<p>The Scottish Government recognises that the third sector needs clarity and stability to secure its resilience and to grow its capacity. That is the basis for our commitment to progress a Fairer Funding approach for the sector, including exploring options for multi-year funding. We understand that there are operational and economic benefits from sustainable funding and the opportunities that this can create for organisations to better plan and expand core services needed by communities across Scotland. The constrained fiscal position means that multi-year funding is very challenging to deliver as such commitments inevitably reduce the Scottish Government's flexibility in future years. However, we remain committed to increasing the number of multi-year agreements for third sector organisations where possible.</p>
<p>37. The Committee acknowledges the risks to the third sector if multi-year funding is not well-managed and resourced properly. The Committee recommends that as part of the Scottish Government's consideration of its Funding Principles, it takes into account the increased costs for organisations that comes from multi-year funding rolling-on. Also, the Committee urges that the Principles, or any guidance that underpins them, to acknowledge the power imbalance of those discussions which could make organisations reticent to ask for additional funds.</p>	<p>The Scottish Government recognises the cost pressures facing third sector organisations and the balance of risk posed by multi-year funding arrangements. We are committed to the principles of positive partnership which support effective relationships between grant managers and grant holders and provides practical guidance to help achieve positive funding relationships and tackle any problems that may arise in a productive way.</p>

<p>38. In relation to the issue of multi-year funding creating a barrier to new entrants, the Committee is persuaded by the evidence it heard that statutory funders should be able to minimise this risk if they approach their funding in a staggered way. Nevertheless, the Committee still has concerns that rolling-forward of funding every year after an initial multi-year award could have the unintended consequence of blocking other organisations from applying for that funding. As such the Committee, asks the Scottish Government to explore options to address this aspect in its Funding Principles or in any supporting guidance.</p>	<p>The Scottish Government recognises the challenges in relation to rolling funding, and notes the Committee's reference to the Children, Young People, Families and Adult Learning fund. If not managed correctly, multi-year funding could create cliff-edges or increasing cost pressures for organisations and we will consider this as we continue to develop our approach to multi-year funding. We are committed to learning lessons from existing funding arrangements and embedding these and good practice into all our grant making.</p>
<p>43. The Committee draws the Scottish Government's attention to the extensive evidence it has received concerning the negative impact the ongoing lack of funding certainty is causing in the sector, in particular as voiced at the Committee's workshops. The Committee believes the Scottish Government, should be looking at options to prioritise multi-year funding in advance of the UK Government's Spending Review. An option would be to commit to multi-year baseline funding, for example at 80%. Therefore the Committee asks what actions the Scottish Government has taken to deliver on multi-year funding since April 2023 and whether it has explored the option to provide baseline funding that can be reviewed once budgets are known.</p>	<p>The Scottish Government recognises the financial challenges faced by the third sector and the impact that this can have on organisational resilience. The sector faces many of the same cost pressures associated with annual budgets as the public sector, however we recognise that there are particular challenges given fixed funding and falling donations. The Scottish Government is committed to increasing the number of multi-year funding arrangements but is constrained by the annual budget process, as any commitments to multi-year funding inevitably reduce the flexibility in budgets in future years.</p> <p>The UK Government has committed to a spending review in the spring of 2025. However, grant recipients need clarity and stability regarding funding in advance of this. We are committed to increasing the number of multi-year funding agreements by 2026 and are focused on deliverability and scalability given that the Scottish Government continues to face the most challenging financial situation since devolution.</p>

<p>56. It is clear from the evidence to the Committee that a shift towards more flexible, unrestricted core funding would be a positive step, as this would enable organisations to cover their core costs, adapt to changing circumstances, and engage in long-term planning. However, the Committee is also aware that because this is public money, there needs to be some surety that funding is being spent appropriately and the risks are minimised. The Committee asks the Scottish Government for its views on what it can do to support this objective. In addition, the Committee asks the Scottish Government how many of its funding arrangements currently include core costs and how many grants are permitted to be used flexibly to cover core costs.</p>	<p>The Programme for Government 2024 commits the Scottish Government to making improvements to grant making, including greater clarity and consistency of existing arrangements. Officials within the Scottish Government have been instructed to review the current grant making processes and make improvements to practice whilst ensuring value for money in grant making.</p> <p>The new Commercial Value for Money team is working with teams across the Scottish Government to review grant spending and identify opportunities to meet priority outcomes while achieving better value for money. This includes developing effective reporting mechanisms to monitor the effectiveness of spend, identifying the wider social benefits and providing commercial scrutiny of costs to ensure clarity on where we are spending money.</p> <p>The Scottish Government currently provides third sector infrastructure bodies, such as SCVO and the TSI network, with core funding in recognition of the vital role they play in supporting the wider sector to contribute to improved outcomes.</p>
<p>57. Evidence also emphasised the importance of a collaborative approach to funding design, which would ensure that funding mechanisms are appropriately tailored to the needs of communities and support the long-term sustainability of the third sector. The Committee calls on the Scottish Government to further support intermediary bodies to play a greater role in working with statutory funders, and other public bodies, such as Integrated Joint Boards, and third sector organisations to ensure funding design meets everyone's needs.</p>	<p>The Scottish Government both funds and works closely with third sector infrastructure bodies, such as SCVO and the TSI network, to support the wider third sector to contribute to improved outcomes.</p>

<p>66. Given current financial challenges, the Committee is aware that funding cuts can be part of the tools available to statutory funders to address budget concerns. Nevertheless, the Committee asks the Scottish Government to be more strategic with its decision-making, for example around the actual financial return of cuts and the timing of its spending decisions to minimise the impact of mid-year cuts. In instances where that is not possible, the Committee asks the Scottish Government to consider what other actions it could take to mitigate the impact of such funding cuts.</p>	<p>Determination of where grant funding is allocated is dictated by the design of a grant which, in turn, is driven by delivery of policy aligned to National Outcomes, Programme for Government and other such policy-related objectives. Every business area will have their own criteria and local arrangements.</p>
<p>75. The Real Living Wage agenda is an important Government policy, but the Committee heard that there were difficulties in implementing it fairly as part of statutory funders' funding conditions. The Committee asks the Scottish Government what actions it is taking to support the implementation of the Real Living Wage through its grant funding, including full cost recovery.</p>	<p>Fair Work First conditionality, introduced in July 2023, requires recipients of public sector grants to pay their workers at least the real Living Wage (rLW) - putting more money into the pockets of low pay workers – and provide appropriate channels for effective workers' voice, such as trade union recognition.</p> <p>Updated Fair Work First guidance, clarifying the administrative requirements was published on 18 November 2024.</p> <p>The Scottish Government will be undertaking an evaluation of our Fair Work First policy, working with stakeholders, including trade union partners, to understand how effectively it is being delivered and what more can be done to strengthen our approach.</p> <p>Funders may approve a limited exception to meeting the rLW condition where a potential grant recipient genuinely cannot afford to pay the real Living Wage to part(s) or all of its workforce.</p> <p>The application of rLW in grants is monitored through the relevant funder's standard grant management processes and the recovery of any costs should be in line with the terms of their grant award.</p>

<p>85. The Committee recommends that the Scottish Government and statutory funders ensure that funding arrangements include provisions for inflation-based adjustments, particularly multi-year grants and those that roll on year-to-year. This would help to ensure that organisations can maintain their service levels and meet wage commitments without having to cut back on essential services and so organisations do not deplete their reserves.</p>	<p>The Scottish Government recognises the impact that the recent period of high inflation and the cost of living crisis has had on the operational costs of delivering services for the third sector. However given the significant financial constraints we continue to face we won't be able to respond as fully as we would like. Nevertheless all grants are assessed carefully and the needs of individual organisations considered in the progress.</p>
<p>93. Unless the challenges set out in this report are addressed it is difficult to see how parity can be achieved. The Committee believes the first step is to ensure three-year funding is provided as the default (noting the need for flexibility around certain projects) and that funding arrangements take account of inflation. The Committee therefore calls on the Scottish Government to set out its plan on how it will address these priorities.</p>	<p>The third sector is hugely diverse and works alongside the public and private sectors across all services and industries, often providing lifeline services in our most vulnerable communities. The Scottish Government is committed to increasing the number of multi-year funding arrangements for third sector organisations to promote stability and certainty and enable organisations to plan service delivery over a longer time horizon. The Scottish Government is exploring options to deliver progress against its fairer funding objectives by 2026, recognising the financial constraints that the government is operating under.</p>
<p>105. The Committee considers the solution to address application and reporting issues is to streamline the process and introduce a level of standardisation. This would reduce duplication and ensure that all organisations, regardless of size or capacity, have an equal opportunity to access funding. The Committee recommends that a streamlined and standardised application and reporting process should be implemented by all Scottish Government departments by the end of this Parliamentary session in 2026. Also, that the Scottish Government shares its knowledge from this process with other statutory funders to assist them to make similar improvements.</p>	<p>The Scottish Government (Core) grant management process, in line with the principles set out in the Scottish Public Finance Manual (SPFM), offers standard templates and checklists, covering application and reporting, which grant-making teams can use and tailor for their own requirements. Scottish Government grants are wide-ranging, depending on policy aims and objectives. For this reason, standard best practice resources have been designed to be flexible for teams to adapt to fit their need and local requirements.</p> <p>We do recognise the benefits of a straightforward application process, which must be balanced with the safeguarding the use of public funds. To promote grant management best practice, the Scottish Government expanded its corporate offer last year by creating a dedicated support function. The Grants Capability and Assurance Team are technical specialists responsible for delivering an improvement plan to strengthen capability across SG (Core). The Team is initially focusing on developing directive supplementary guidance and a maturity exercise to identify areas of poor practice that will</p>

	<p>inform further capability improvements. The Team is also looking at technology developments to both improve the transparency of Scottish Government grant giving and to standardise the application process for recipients. 'Find and Apply for a Grant' are tools developed by the Cabinet Office, and discussions are underway to understand the path to adopt at the Scottish Government. This would allow for greater standardisation, with scope for teams to add their grant-specific eligibility requirements. To support streamlining, the use of this tool could be broadened out to statutory funders such as local authorities and public bodies.</p>
<p>112. Based on the evidence the Committee has received, it appears that the issue of delayed notification of funding has not been resolved. Guaranteeing funding decisions are issued and funds are paid as soon as possible would have a hugely positive impact on the third sector. The Committee calls on the Scottish Government to explain why it has not been able to resolve this issue and what steps it is taking to ensure this is addressed for the forthcoming financial year.</p>	<p>The Cabinet Secretary for Social Justice wrote to the Committee in May 2024 setting out the progress and outstanding notifications for 2024-25. As a result of budget challenges, we were unable to provide notification to all third sector organisations before the end of March 2024. The data demonstrated that over half (58%) of third sector grants were notified by that date, including 87% of funding from the social justice portfolio, with many more grant offers being notified in the first two weeks of the new financial year. This provides us with a baseline on grants performance for the first time and, given the circumstances, presents a positive starting point from which to progress. Confirmation of funding to all our key partners and stakeholders for 2025-26 will be made as soon as possible after the Budget statement.</p>
<p>119. The Committee recommends the Scottish Government and its partner awarding-bodies take action to improve the transparency of their grant funding decision-making processes, to ensure greater accountability, improve consistency across Government departments and to help third sector organisations identify funding gaps.</p>	<p>Transparency of grants can be understood two ways: the advertisement of grant opportunities and the review of proposed grant applications received. Local grant giving teams are responsible for assessment and award of a grant in line with best practice. As mentioned in the response to paragraph 105, the Grants Capability Team are looking to standardise the existing approach to advertising grants through 'Find and Apply'. Adoption of these tools will also provide a view of both live and proposed grants, with the ability to store successful/unsuccessful applications. Together, there is a potential for this information to be used by grant making teams to inform their decision making process. The specifics of what is available is included in the investigatory work currently underway.</p>

	<p>Another opportunity to strengthen best practice of the Scottish Government's application process, is the use of data from Oracle Cloud (the financial management system used for grant disbursement) to support with understanding the landscape of grant giving and decision-making processes in achieving value for money. However, for effective analysis, a data set of an entire financial year would be required to produce meaningful insight(s).</p>
<p>127. The third sector is critical to ensuring that those in need are supported. Indeed, the Committee heard at its workshops that the sector should be called the 'essential sector'. How funders support the third sector's work can have a markedly positive impact on addressing equality issues, or as some of the evidence suggests, further entrench inequalities. The Committee recommends that the Scottish Government reinforce in its Funding Principles that statutory funding processes should contribute to the reduction of inequalities and asks the Government to undertake data collection on what groups of people and geographic areas benefit from its funding.</p>	<p>All Government grant funding of third sector organisations is subject to the Public Sector Equality Duty, as well as due diligence, before grant awards are made. We are driving an ambitious and progressive agenda to ensure that equality and human rights are embedded in all we do. This includes ensuring our spend advances equality and human rights for Scotland's people.</p> <p>Grants are carefully monitored to ensure that intended outcomes are achieved, together with value for money and aim to fulfill specific policy objectives including tackling inequalities. For example, the Government's Volunteering Support Fund is specifically targeted at reducing barriers to volunteering in Scotland. All third sector organisations are reliant on volunteer trustees or board members for their governance, and many rely on volunteers for operational leadership and the delivery of services. The Fund helps local community grassroots organisations to support and promote volunteering among a variety of groups who experience disadvantage or barriers to volunteering. This includes supporting more volunteers who are Black and Minority Ethnic, disabled or with a long term health condition. There is excellent evidence of positive impact from the Fund, particularly in relation to equality and diversity. Organisations have increased the diversity of the third sector's volunteer pool, in particular to include people who experience disadvantage or would traditionally experience barriers to volunteering. Benefits include reduced loneliness and social isolation, improved health and wellbeing as well as provision of support and care for others.</p>

134. The Committee draws the Scottish Government's attention to the oral evidence the Committee has gathered in relation to the Scottish Government's recent consultation on Disclosure Scotland fees.

The Scottish Government followed the evidence provided to the Committee on the Protection of Vulnerable Groups (PVG) Scheme fee waiver for volunteers. The themes present in the oral evidence reflects many of the responses given to the Scottish Government through the consultation and engagement process earlier this year. The Minister for Children, Young People and the Promise has also met directly with volunteer involved organisations, through the Cross Party Group on Volunteering, to listen to their experiences and concerns in relation to the future of the PVG fee waiver for volunteers. Scottish Ministers are considering all evidence gathered carefully in making a decision. An update will be provided as soon as possible to provide more certainty for organisations.