OFFICIAL REPORT
AITHISG OIFIGEIL

Economy, Energy and Fair Work Committee

Tuesday 11 September 2018

The Scottish Parliament
Pàrlamaid na h-Alba

Session 5

Tuesday 11 September 2018

CONTENTS

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ECONOMY, ENERGY AND FAIR WORK COMMITTEE
24th Meeting 2018, Session 5

CONVENER

*Gordon Lindhurst (Lothian) (Con)

DEPUTY CONVENER

*John Mason (Glasgow Shettleston) (SNP)

COMMITTEE MEMBERS

*Jackie Baillie (Dumbarton) (Lab)
*Colin Beattie (Midlothian North and Musselburgh) (SNP)
*Angela Constance (Almond Valley) (SNP)
*Jamie Halcro Johnston (Highlands and Islands) (Con)
*Dean Lockhart (Mid Scotland and Fife) (Con)
*Gordon MacDonald (Edinburgh Pentlands) (SNP)
*Andy Wightman (Lothian) (Green)

*attended

THE FOLLOWING ALSO PARTICIPATED:

David Anderson (Scottish Government)
Ivan McKee (Minister for Trade, Investment and Innovation)

CLERK TO THE COMMITTEE

Alison Walker

LOCATION

The David Livingstone Room (CR6)

Scottish Parliament

Economy, Energy and Fair Work Committee

Tuesday 11 September 2018

[The Convener opened the meeting at 10:00]

Interests

The Convener (Gordon Lindhurst): Good morning and welcome to the 24th meeting in 2018 of what is now the Economy, Energy and Fair Work Committee. I remind everyone to turn electrical devices off or to silent, please.

I welcome our new committee member, Angela Constance, and ask her to declare any relevant interests.

Angela Constance (Almond Valley) (SNP): Thank you, convener. I have no relevant interests to declare. My entry in the register of interests is there for everybody to see.

Decision on Taking Business in Private

10:00

The Convener: Under agenda item 2, do members agree to take agenda items 4, 5 and 6 in private?

Members *indicated agreement.*

European Structural and Investment Funds Inquiry

10:00

The Convener: Agenda item 3 is our European structural and investment funds inquiry. I welcome Ivan McKee, the new Minister for Trade, Investment and Innovation, and David Anderson, head of the Scottish Government's European structural funds and state aid division. I ask Ivan McKee to make an opening statement before we move to questions.

The Minister for Trade, Investment and Innovation (Ivan McKee): Thank you, convener, and good morning, committee. This is my first appearance in front of the committee in my new role, and I hope that it will be the first of many. Thank you very much for the invitation to contribute to the European structural and investment funds inquiry and for the provisional findings that your work has already produced.

The European social fund and European regional development fund programmes have provided significant funding to Scotland for more than 40 years to promote economic development and cohesion. Going back to the 1970s, Scotland received funding for a wide range of activity, including, for example, road improvements in Ayrshire and new water supplies on the Scottish islands. Now, the European Union's aims of smart, sustainable and inclusive growth towards the Europe 2020 targets, and the Scottish Government's sustainable, inclusive growth ambitions, as set out in the national performance framework, neatly align. The programmes support a number of the Scottish Government's priorities.

Skills Development Scotland and the Scottish Further and Higher Education Funding Council use funds from the ESF towards meeting the aim of a well-equipped workforce, with some 17,000 individuals receiving skills training. That is in addition to other programmes that are working to contribute to alleviating poverty and increasing social inclusion by providing support to 15,000 individuals, including those in low-income households, lone parents and those not in work.

The ERDF programme supports investment in 16,000 small and medium-sized enterprises to grow and create jobs and opportunities, and it aims to support 500 organisations to develop low-carbon processes and technologies to facilitate Scotland's transition towards a low-carbon economy.

In May, when the committee took expert advice from a number of organisations, it was stated that the programmes support between 10 and 25 per cent of local authority economic development and employability spend. I am sure that members will agree that the programmes' significant contribution to economic development in Scotland cannot be overestimated.

However, the process is not without its challenges. The programmes come with significant audit and compliance requirements. The European Commission has issued around 6,000 pages of rules via three regulations, eight implementing acts, nine delegating acts and more than 100 pieces of guidance. The Commission requires that all expenditure that is claimed complies with those rules. Failure to do so can result in serious penalties. We have experienced problems in the past where non-compliance has been identified, resulting in funding being reduced.

The Scottish Government, as a responsible managing authority, works hard to support those who apply for and receive those funds by distilling the complexity of and clarifying understanding of the compliance and audit process to avoid risk and maximise the positive outcomes that are provided for Scotland. That is achieved by carrying out thorough checks and regular reviews of guidance and processes, and always seeking opportunities to simplify the process where possible.

In the committee's provisional findings, it identified value in programmes that are based on needs-driven funding and good practice from current and previous programmes and which are directed at people and places. The United Kingdom Government has also recognised the value of those programmes and the contribution that they have made. That is demonstrated in its commitment to replace them with a shared prosperity fund. It has acknowledged that it will engage with us and counterparts in Wales and Northern Ireland and respect the devolution settlements, but, to date, there has been no detail from it on how it intends to take that proposal forward.

The EU exit was not Scotland's choice, but we will work with the UK Government to avoid and mitigate the worst effects for Scotland. That includes ensuring that repatriated powers are transferred to the Scottish Parliament along with a sustainable funding package and any proposed replacements for the ESF and ERDF programmes.

The aims of the programmes add distinctive characteristics such as a longer timescale beyond a single year or even a parliamentary session; the recognition of regional development, particularly in the Highlands and Islands; and partnerships, including those between Government, public bodies and the third sector. Those characteristics remain a good starting point for future programmes.

As members know, we do not want a rigidly bureaucratic programme; we want to simplify the management of the programmes where possible, in line with public finance standards, to ensure that funding is spent appropriately and audited proportionately. By aligning the strengths of the programmes with Scottish policies and priorities, including the national performance framework, the economic strategy and the enterprise and skills review, we need to strike a balance between compliance and complexity that will maximise the impact of future programmes on Scotland.

I am happy to answer any questions from the committee.

The Convener: Thank you for that statement.

You commented that the promotion of economic and social cohesion through ESIFs has been on-going for 40 years. Can you point to specific examples in which those funds have helped to reduce economic and social disparity in deprived regions in Scotland, as opposed to the programmes simply being delivered? Some regions are not improving.

Ivan McKee: Some of the evidence that the committee has received from representatives from the Highlands and Islands is very clear. In future sessions, they will strongly point to the huge value that the funds have made to the Highlands and Islands. That area of Scotland has received a particular focus in the delivery of the programmes, to the extent that match-funding requirements have been reduced. The current programme has put £150 million into the Highlands and Islands, and hundreds of millions of pounds have been put in over previous programmes. It is difficult to say what difference there would have been without those programmes, but the best example that I can give is that people from the Highlands and Islands have said very clearly that the programmes have resulted in significant benefits to the region.

On reducing inequality, another example is the work on the youth employment initiative, and we might want to talk about the decommits later. Other programmes have been in place, but the work that has been delivered through that programme has led to Scotland's youth unemployment reducing significantly from 25 per cent to around 10 per cent, which is below the UK average. A significant focus of the programmes has been on reducing youth unemployment.

Those are a couple of examples in which regional and economic disparities have been reduced through the focus that the programmes have brought to Scotland.

The Convener: Are the programmes and the reduction in the disparities directly related in that way?

Ivan McKee: All that we can do is look at the structure of the programmes and the performance framework that is agreed with the European Union, and the deliverables that are part of that. I mentioned in my opening statement the 10s of thousands of individuals, as well as the businesses, that have been supported directly through the programmes. Those individuals and businesses have benefited from that support. It is difficult to say how that stacks up against the macro, because we are never sure of the counterfactual and what would have happened anyway—the impact of other interventions that the Scottish Government would have taken and other factors that might have pushed in the other direction. However, we can clearly point to the support and benefits that the programmes have given individuals and organisations, and to what the programmes have done at a macro level for the Highlands and Islands and youth unemployment.

I have a couple of other specific examples. The state-of-the-art videoconference suites at the University of the Highlands and Islands have made a huge difference to connectivity and the ability to work together. Scottish Enterprise ran the Scottish co-investment fund, and the data shows that the additional net gross value added through to 2025 is estimated at £290 million. There will be a significant impact on economic growth to the Scottish economy as a consequence of those programmes.

Jamie Halcro Johnston (Highlands and Islands) (Con): Good morning, minister. You rightly point out the importance of the Highlands and Islands area, which accounts for 20 per cent of the funding across both the funds. You mentioned some individual figures, but I have figures for committed funding that suggest that 51 per cent—it may be slightly higher now—of the European regional development fund money has been committed and that 33 per cent of the European social fund money has been committed. If those funds were fully committed, the sums would add up to around £180 million on previous exchange rates.

What can the Scottish Government do to ensure that that potential allocation is met, that the compliance requirements are met and that the money that is available is fully utilised for the Highlands and Islands?

Ivan McKee: Thanks for the question. Across the country, not just in the Highlands and Islands, we face the challenge of how to allocate and deploy the funds in a way that complies with the audit requirements that I have talked about.

In the earlier stages, we recognised that there was a slower take-up, particularly in the Highlands and Islands. I know that Keith Brown, who was the cabinet secretary at the time, wrote to organisations to encourage them to step up and become more engaged in the programme. In the Highlands and Islands, because of EU rules and the fact that the Highlands and Islands is a transition area that is distinct from the rest of Scotland, we were able to relax the match-funding requirements so that as much as 70 per cent or, in relation to specific programs or activities, 80 per cent of the funding can come from the funds. That is one specific step that we have taken to try to encourage organisations and programmes to use the funds as well as possible to support development in the Highlands and Islands.

Jamie Halcro Johnston: Are you confident that that total allocation will be met? Do you have a figure that you are working towards for a potential allocation?

Ivan McKee: It is difficult to say at this stage, because we are several years out. We can perhaps talk about that in more detail later. With the N+3 principle, we have three years after we have committed the funds to utilise them. However, given the complexity of the audit requirements, it is difficult to predict whether we are going to miss a target because someone does not comply with audit requirements at some point down the line or because we do not have enough proposals or programmes coming forward to utilise the funds. However, the officials on the team and the managing authority are certainly working hard to push that and, although it would be difficult to say that we are going to utilise all of the funds, the signs at the moment suggest that the vast majority will be deployed to support the development of the Highlands and Islands.

Jackie Baillie (Dumbarton) (Lab): I would like to pursue this issue a bit further and take it a bit wider.

It is always instructive to learn from the past in order to avoid making similar mistakes in the future. At the end of 2017, your expenditure targets were not met, and something like €22 million, which I am sure that you will agree is a substantial amount of money, was either lost or decommitted. What do you think caused those problems and what have you learned since then that will enable us to avoid them in future?

Ivan McKee: You are absolutely correct. That was funding for the 2014 period, which, with the N+3 arrangement, tripped out at the end of 2017. Of that €22 million, around €16 million was associated with south-west of Scotland youth employment initiative programmes. As I said earlier, in some ways you can see the significant reduction in youth unemployment that we have seen in the post-economic crash period as a success of the programmes and other initiatives. However, what that has meant is that there are fewer places to spend that money. When the programmes were designed and the funds allocated, youth unemployment was around 25 per cent. We have now reached a point where youth unemployment is around 10 percent, which is one of the lowest rates in the EU and is the lowest rate in the UK. Because of that, obviously, it becomes harder to find places to allocate the money. That is the significant driver—

Jackie Baillie: I understand exactly what you are saying, but you will appreciate that the Scottish local authorities economic development group pointed to seven criticisms, not all of which related to the improvement in youth unemployment. For example, it noted that there were delays of up to a year for the Scottish Government to issue guidance and that there was a wasted exercise around consideration of the cost models to be used, which, inevitably, led nowhere. Do you intend to sharpen up on those issues, rather than just point to one thing when clearly there are more problems than that?

10:15

Ivan McKee: If, as you said, we are going to learn from the past and the problem of the €22 million, it is important to point out that the lion's share of that—€16 million—related to the youth employment initiative. If we want to fix the problem, we have to look at what was by far the biggest cause of it, which is why it is important that we talk about that.

On the delay, the programme is a 2014 to 2020 programme, so it was approved at the end of December 2013 by the European Commission. The Scottish Government then worked with the rest of the UK, which is the member state, to put together a partnership agreement, which was agreed towards the end of 2014. Then, at the start of 2015, the Scottish Government called for programmes to take up the funds. As I said, the take-up was initially slow, and we had to go back out and in some cases review the match-funding requirements to encourage more people to come forward. The initial delay was to do with getting in place that partnership agreement with the rest of the UK, which happened in the latter part of 2014.

The point about the unit costs feeds into the simplification agenda, which the committee might also want to talk about later. To go into that in a bit more detail, it is about moving away from a situation in which individual receipts and timesheets have to be approved to a situation where we can say what the cost of an individual is, allocate their time, understand the cost per hour for that individual and allocate funds on that basis. That clearly makes the whole process and audit requirement much simpler. Work was done at the start of the 2014 to 2020 programme to deliver that, and unit costs have been put in place for parts of the programme spend, although not for all of it. In other areas, the flat cost system, whereby the individuals' costs are taken and a percentage uplift is added for administration and travel costs, has been put in place.

The programme has been simplified using those two approaches, so it is not fair to say that that work was wasted. I think that I am going to be asked about simplification and reducing bureaucracy, and that work was done at the start of the programme to ensure that that happened to an extent.

Jackie Baillie: I was trying to reflect the view of the Scottish local authorities economic development group, rather than my view, but I take what the minister says.

What is the current allocation in the programme?

Ivan McKee: There is £420 million committed as of today.

Jackie Baillie: What is your expectation of spend? I appreciate that it is difficult to predict, but you will have internal processes through which you know how much it is intended to spend. I am interested in how those internal processes work and what the figures are.

Ivan McKee: I have spoken about the €22 million decommit that we are already aware of. There is also an issue with exchange rates, which I will ask David Anderson to talk about in a minute. It is important to recognise that, when the programmes were put in place, the exchange rate was €1.25 and today we are at about €1.11 or €1.12. Because all the programmes from the EU side are funded in euros, that makes a difference to the number of pounds that we have to spend.

I ask David Anderson to talk through the details of the numbers as of today.

David Anderson (Scottish Government): As the minister said, it is still our intention to get all of the funds allocated as far as we can throughout the life of the programme, and we are planning for that. We are still working on getting all the money committed. As the minister says, quite what that number is depends on the exchange rates and any further decommitments that might become necessary. However, there are some things working in our favour. One is that we have been working with the Scottish local authorities economic development group and other stakeholders to be absolutely clear with them how much money is still there and how much money they want, going through round 2. We are asking them to bring forward their ideas and we are having that good dialogue.

Another thing is that, where we identify that we might have shortfalls in take-up, we are talking with partners to see where else we might spend the money. We have discussions on-going with health colleagues, universities and one or two others to try to ensure that we use the money, although obviously that will be within the rules.

The final point is that the UK HM Treasury guarantee changed in July. Prior to that point, funds that were committed by the date of Brexit were guaranteed. That date has now shifted out to the end of 2020. Clearly, we would not want to wait that long to commit the funds, if we were to crash out of Europe, but it does give a little more elbow room to commit final funding.

Jackie Baillie: A Scottish Government response to the Scottish Council for Voluntary Organisation's criticism would be welcome. Let me quote from SCVO directly. It states that

> "many aspects of Scottish Government work very well. But management of the European Structural and Investment Funds is not part of this."

Do you agree with that view, and what action will you take, as the new minister, to improve things?

Ivan McKee: I do not agree with everything that SCVO has said. There are one or two things that we will take on board and look at, but SCVO made a number of comments, a lot of which were about the bureaucracy around the process and the need for simplification. I point to the statements that I made in my opening remarks, when I said that we are existing under an onerous audit requirement, with 6,000 pages of EU requirements, which officials have reduced to two handy, simple documents for organisations to work with. However, because things change from one programme to the next, the EU requirements under the 2014 to 2020 programme are different from those under the 2007 to 2013 programme.

Perhaps there was some misunderstanding about the new rules, and some people have still been working under the old rules. There have been some issues around that and I have examples of all manner of things that have led to audit problems. Some of them seem simple and straightforward, such as people not keeping records or timesheets, or not recording building costs or staff costs correctly. A number of detailed issues have led to issues with funding being called down from the European Union as a consequence. You will be aware that, in the previous 2007 to 2013 programme, three of the four programmes were under suspension at one point because of audit non-compliances.

It is a serious issue that needs to be dealt with properly, so I understand SCVO's comments, but the processes that are in place need to be regulated, robust and, I am afraid, quite bureaucratic, to ensure that we are compliant with the European Commission requirements.

There are some comments about match funding that we need to take on board. Very often, the Scottish Government provides match funding for third-sector organisations, so it effectively becomes a 100 per cent grant to third-sector organisations, but that is not always the case, and I take on board the point about lead partners not always stepping in to put match funding in place in the way that had been expected. It is important to recognise that the SCVO chief executive was also a member of the joint programme monitoring committee, so SCVO has had an opportunity to make comments as part of the on-going process, which have been listened to.

In my new role as minister, I will undertake to meet SCVO as part of our efforts to design what the future might look like, notwithstanding where we are with Brexit and the uncertainty around the shared prosperity fund. I may say more about that later, but I will certainly undertake to meet with SCVO and other stakeholders as we attempt to design the future.

The Convener: Is that not just basic stuff? Keeping records of staff costs and things like that is not really that complicated, is it? If that is what is causing audit trail problems, surely those issues should not be arising.

Ivan McKee: When you are working on something as broad and involving as many organisations, as much money and as many instances of claims as we are talking about here, there will always be a percentage that is problematic. As I said, the requirements that we are working under are pretty onerous and the EC will bring in auditors to work through and double-check what the officials in the Scottish Government are doing, so it is important that we are on top of that.

You would need to ask the organisations themselves why those issues arise, but in any situation where you have many transactions going on a percentage of them will be non-compliant. That is why it is important that we are rigorous about the audit requirements and that we produce the guidance so that organisations understand them. We produce monthly e-bulletins to keep organisations up to date, and we work directly with organisations as best we can to make sure that they are all aware of what the requirements are and feed back any audit non-compliances in time so that they have the opportunity to fix those.

Angela Constance: I want to pick up some of the concerns that have been raised by SLAED. I note that, in his opening remarks, the minister pointed to the 6,000 pages of rules and the 100 pages of guidance, and that you reiterated the Scottish Government's role in distilling the complexity of those rules and that guidance, with a view to reducing risk. However, as you have heard from other members—and as you will have seen in evidence that the committee has received—there is criticism from stakeholders about the level of inflexibility and bureaucracy.

Specifically, SLAED gave a long list of reasons why it can be difficult to translate commitments into expenditure. One of them was

"Elongated Scottish Government appraisal and assessment procedures."

Minister, can you say more about how you will ensure that Scottish Government practice does not add to an already complicated process?

Ivan McKee: Without going into a huge amount of detail on specifics, it is fair to say that we understand the simplification agenda very well. It is at the forefront of our minds. Earlier, I gave examples of where we had looked for areas in which we could reduce complexity in the claims process by looking at unit costs and flat costs and so on. The finest example is that we took the 6,000 pages of rules and reduced them to about 100 pages, then we worked closely with organisations to make sure that they understand the requirements. We work through the process with them as best we can.

The managing authority and the Scottish Government did not put in place the bureaucracy and audit requirement. That is the reality of the EC rules that we are working under. Those rules are robustly interpreted and implemented, and the consequences of not complying with them are pretty significant. I can understand that organisations that are outside looking in would see what they see, but I have demonstrated that, in its intent and what it has done with the design of the claims process, its cost management and the way that it is working hard to simplify and make accessible the complex rules around the process, the Scottish Government is very much committed to understanding the issues and making the process as simple as possible for organisations to participate in. At the end of the day, we want to move the funds into these organisations and get the benefit for Scotland from them. It is in nobody's interests to make the system more complicated and cumbersome than it needs to be, or the funds more difficult to access.

Angela Constance: Are you confident that current processes and procedures do not add complexity, or are you saying that, where it exists, you will endeavour to reduce complexity, particularly looking to the future?

Ivan McKee: Absolutely. That is exactly what I am saying. David Anderson can give a bit more detail on the specifics.

David Anderson: When we get an application for funding, we have to make sure that it fits the programme. We then have to submit it to a managing authority approval panel. That has a certain number of checks and there is a standard template form that allows people to fill in the data of who wants the money. We then check that that complies.

We do that as quickly as we can. We often have a dialogue with the stakeholder to make sure that the numbers that are set out are correct, that what it is delivering fits, and that it is clear. On that basis, we make a formal commitment of grant funding between Scottish ministers and the actual person who is being funded. We have to be sure about what we are buying, so we make that point as quickly as possible.

In previous programmes, we had to submit the application to a panel that met infrequently, but that panel now meets on a six-weekly cycle, so there should be little delay—if any—between getting an application and submitting it. When it is ready to put to approval we can do that as quickly as possible. We take some out of sync to make sure that we do not hold people up. Recently, we had one in which Highlands and Islands Enterprise was interested.

In all of that, we talk with SLAED. On Friday, one of my team leaders will give a presentation to SLAED to set out and share information about amounts of money and what needs to be done.

One of the ways of breaking down delays is to have an open dialogue. We have a good and positive dialogue with SLAED. We help where we can to make the process as slick as possible.

10:30

Angela Constance: The minister’s commitment to meet SCVO is welcome, as is his commitment today to take on board any concerns.

One of the things that SCVO raised that works well was how the third sector division in the Scottish Government met 100 per cent of eligibility costs and provided match funding. Does the minister have any initial thoughts on how he will pursue that approach, given that it would not be just for his department but for departments across the Scottish Government?

Ivan McKee: In terms of match funding?

Angela Constance: In terms of increasing the Scottish Government’s ability to match fund.

Ivan McKee: I will make a general point about match funding and David Anderson will talk about specific details.

Clearly, a range of organisations apply for funding. They are able to match fund in some cases, which is to be encouraged, because it brings more money into play and significantly increases the total that can be spent through those programmes. As a consequence of match funding, the total is significantly more than the money that comes from the EC. Match funding also demonstrates commitment from organisations. It makes them more committed to deliver and ensures that they have thought it through, because they are putting their own money on the table to support the programme.

There is a place for match funding but we recognise that, in some cases, it is not possible for the types of organisations—typically in the third sector—that we are working with. The mix is important.

David Anderson: On the point that SCVO made about the third sector fund, it was the choice of the third sector division to use Scottish Government money to match the European money and make it effectively a grant situation. That is the exception rather than the norm. The total value of the programmes is about €900 million. By having match funding, the overall investment in Scotland in these programmes is about €1.9 billion.

If we were to match fund everything at source, we would not lever in as much opportunity as if we were to seek match funding from those applying for the money.

Dean Lockhart (Mid Scotland and Fife) (Con): I want to follow up on the point about match-funding requirements, and to get a wider view of the benefits and challenges that are experienced. Are there occasions when the match-funding requirements have been too rigid and investments have been prevented, or is there sufficient flexibility in the system to allow the requirements to be tweaked, if necessary?

Ivan McKee: I will make a couple of points. First, we must adhere to EU requirements on the level of match funding. The percentages have been relaxed for the Highlands and Islands because it is a transition area, so we can go as high as 70 per cent and even, in some circumstances, 80 per cent. In general, the figure in the requirements is 50 per cent. We are working in that context.

We relaxed the percentage requirement for the Highlands and Islands, as we were able to do within the rules, because we saw early on that there was a shortage of programmes coming forward. That relaxation stimulated more programmes and was thus demonstrated to be successful. Where we understand that match funding is a challenge for third sector organisations, we have worked hard to provide more.

Has there never been a case in which someone has been prevented from participating because of match funding? I am sure that there will be examples of that. In general, however, we work hard to mitigate the issue within the rules, as best we can.

David Anderson: I point to the example of Transport Scotland, which called for proposals in the Highlands and Islands with an intervention rate of 70 per cent, but there were no takers. We were able to up the percentage intervention rate, so we now have some takers on those programmes.

We have flexibility, so we change intervention rates in the programmes in order to respond to such demands. We responded in the mid-term review, when we looked at demand overall and made the case to the EU. As the minister said, we have to agree the total match-funding percentages with the EU. We cannot just do what we like—we have to meet an average. The EU was persuaded to allow us the flexibility to go higher so that we could ensure that the funds were taken up, which is what Ms Baillie's point was about.

Colin Beattie (Midlothian North and Musselburgh) (SNP): The minister referred to the UK's shared prosperity fund. How much do we know about how that fund will operate? Are there guidelines already in place?

Ivan McKee: There is very little in place, and only in the past two or three weeks has there been an official meeting on the fund. In its manifesto, the Tory party committed to putting in place a fund to replace the lost EU funds. In a statement in July this year, a UK Government minister said that the fund would be put in place, that it would be aligned with the objective and the four challenges of the UK Government's industrial strategy, and that the UK Government would respect the devolution settlement and engage with the devolved Administrations on the fund's design. That is as far as we have got, although David Anderson might be able to say a bit more about the latest discussions involving officials.

At the moment, it is very unclear what the shared prosperity fund will look like, how it will be deployed, how much funding will come to Scotland as a consequence, whether the decisions will be made at UK level or devolved to Scottish level, and to what extent the EU requirements will be mirrored. There are many unknowns, and we are running out of time.

The UK Government is moving forward to consultation to seek views on the fund. We had thought that that would have taken place by now, but we now believe that it is to take place later this year. Our hope and expectation is that we will have the opportunity to have discussions with the UK Government about how the requirements of the devolved Administrations will fit into the programme, and that we will not be treated as just another consultee filling in an online form. I met Lord Henley, the UK Government minister who is responsible for these matters, last month and raised those points with him. The picture is very unclear, and time is running on.

David Anderson: I am afraid that there is not a great deal more to say. Officials have met Westminster colleagues. Ever since the May 2017 manifesto commitment was made, we have been pressing on the issue. We have a group that includes the managing authorities across the UK. When the announcement was first made, we asked what the fund would look like, but we have had no detail on that, and have been pressing to get that detail. When I say "we", I mean the Welsh Government, the Northern Ireland Executive and the Scottish Government—as well, it must be said, as a number of parts of England, because the UK Government has made it clear that the fund will be allocated at region level.

That process is beginning. I have met officials from the UK Government, and I know that those officials have met Welsh and Northern Irish officials in the past week. The detail is still to come. The UK Government is looking to the consultation to establish what people need. One of the pieces of work that we have in train internally is considering the results of the committee's investigation and examining what stakeholders have said in order that we can work out what Scotland's ask is, so that we can put the case for what we want to the UK Government.

Colin Beattie: Has the UK Government made a commitment to maintaining the present level of funding for a specific period beyond Brexit, or do we not know?

Ivan McKee: There are two scenarios. There is the no-deal scenario, in which case there is, we understand, a guarantee in place whereby the funding gap would be filled until the end of the 2020 programme, which with the N+3 process runs through to 2023. In the eventuality that a deal is reached, the existing programme of EU funding will run through as planned to the programme from 2021 onwards.

My understanding is that no specific commitments have been made on the level of funding, so that is one of the unknowns. We have a strong requirement that Scotland will receive at least the level of funding that it would have expected from the equivalent EU programme.

Colin Beattie: I am trying to look at the matter positively. The creation of new funding mechanisms perhaps gives us an opportunity to improve on what exists. What should be the new fund's guiding principles?

Ivan McKee: That is a great question. I will take a step back from that. In my new role, I am keen to engage with stakeholders. The work that the committee has done so far and the eight points that it has raised about how it sees the fund working are helpful, as is the evidence that it has taken from stakeholders. I want to continue engagement with stakeholders in order to understand their requirements on some of the points that have come up in the meeting.

The UK Government has indicated that the fund will be built on its industrial strategy, so we are constrained by that. However, the principles of cohesion and social inclusion that underpin the EU funds are hugely important. The four Is of the Scottish Government's economic policy—innovation, internationalisation, investment and inclusive growth—are critical. They will underpin the programme, which will be lined up with the measures in the national performance framework so that a coherent approach is taken across all Government in Scotland.

That will involve a series of balances. We must consider how much flexibility we want versus how much stability we want. People like stability, but they also want flexibility so that they can make changes when circumstances change. We also have to decide on the extent to which the fund needs to be coherent strategically at all-Scotland level and how much we want to devolve responsibility to the regions to allow different choices to be made at region level. We have already talked about the audit requirements: we have to decide how strict we need to be on those to ensure that public funds are used well without the process becoming too bureaucratic.

There are a number of trade-offs, so it is important that we engage in that space so that we understand the best direction in which to move as we design a programme for Scotland—or, at least, as we advance our view of what it should look like.

Colin Beattie: Will you expand on some of the headline points that you just made and give an indication of the big societal challenges that a future fund should address?

Ivan McKee: As I said, we will be constrained by the UK Government's industrial strategy, which has identified themes: the ageing society, mobility and low-carbon growth. We do not disagree with those broad themes, because they make sense in the Scottish context. Therefore, we have to start from that basis and build on it, depending on the feedback that we get from stakeholders. However, the requirement for social inclusion, inclusive growth and cohesion runs across that, which is hugely important. Anything that we do must ensure that the least-developed regions in Scotland receive the investment that they need to bring them up to the standard that we want, and that people who are furthest from the labour market continue to be brought into it and upskilled. Those principles are central to what we want.

Colin Beattie: You said that your starting point for fund allocation is that Scotland should receive no less than it receives now. That said, is there a formula for allocation of funds throughout the UK that could be put in place and which should be adopted?

10:45

Ivan McKee: No. In terms of the rest of the UK, frankly, that is not a space on which we would want to comment. I heard the committee's earlier evidence about there being wide variations in the funding that English regions get. In terms of the split across the four nations, we obviously have a view on that. As I have said, we require not only to maintain at least the level of funding that we get at the moment, but to build on it, because we have specific requirements. The Highlands and Islands is only one of three transition areas across the UK. Historically, Scotland—the Highlands and Islands in particular—has enjoyed higher funding, and it is important that that is built in.

As I have said, we are very keen to push strongly the argument that funding for Scotland must be maintained at least at the level that it is at now, and that division of the funding among the four nations of the UK must take that into account. I do not want to comment on the specifics of how the rest of the UK would manage a lower level of funding.

Colin Beattie: Initially keeping the funding at the same level is fair because it is the situation that we are in now, but I presume that a formula would be put in place to replace the one that the EU uses. The UK Government should adopt a formula so that it can continue and build on that allocation. Over the past few years, we have been allocated, I think, about £871 million. Although we want to draw a line under that level of funding, we do not want it to stay there. It should move. How do we make that happen?

David Anderson: I will answer that question, if I may. No formula has been agreed in the discussions with the UK. When you look at the EU budget for the 2021 to 2027 period, it is interesting to see that the entire EU budget is under pressure. Therefore, if we were to stay in Europe, there would be a question mark over what our allocation would be.

As with all such funding discussions, we make pitches on what we want to do and the money that would be needed to do it. Colin Beattie's point is absolutely right: a discussion with colleagues will be needed about the overall shared prosperity fund—at the moment, no figure is attached to it—

and what the right level is and how it should be divided up. As the minister has mentioned, we benefit from EU funding disproportionately on a population basis among the four nations because of the needs of the Highlands and Islands.

It is also unclear what the shared prosperity fund will cover; we understand that it will cover the marine and fisheries fund. Scotland receives almost 50 per cent of that funding, because of how the fund is divided up. A bit of mixing needs to be done in order to work out what we want to do with the shared prosperity fund and how much money we would have to do that. After that, we will need to argue our case very strongly.

John Mason (Glasgow Shettleston) (SNP): I accept that there is a lot of uncertainty and I suppose that, at one extreme, the UK could put down a rigid system and we would have no flexibility at all. However, if we assume that there will be a fair bit of flexibility and that we will get about the same amount of money, how will that be allocated across Scotland? There has been criticism that we have only two sections in Scotland—the Highlands and Islands and the Scottish Enterprise areas, although they will become three with the new enterprise agency. Should we subdivide to council or regional level?

Ivan McKee: Two or three cycles ago, there were up to five different funding programmes in Scotland, but the number has gradually reduced over time—as you have heard in previous evidence, that has also happened in countries similar to Scotland, such as those in Scandinavia. The funds allocated to more developed countries have reduced, as has the number of programmes in order to reduce overall administration. In this cycle, in effect there is one Scotland-wide programme but with recognition and specific funding within that for the Highlands and Islands.

We come back to my earlier point about trade-offs and the need in all our decisions to think about what makes the most sense and where we want to be on the spectrum. The right balance will be between having something coherent strategically at an all-Scotland level, so that we can direct maximum resources to fix the problems that we have identified—youth unemployment is an area where there has been success; there are others, too—and which lines up with the national performance framework and the economic strategy, which is clearly important, and being able to make decisions at a local level.

The more the administration of that is devolved, the more complex the bureaucracy becomes and the greater the administrative burden and cost—that is part of the balance as well. However, we have to take on board the fact that there are different requirements in different parts of Scotland.

As I am new to this job, there is a good opportunity just at the right time to take views on the issue and reflect on it. I am keen to engage with stakeholders to take their views and to ensure that we get that balance right, within the constraints of the shared prosperity fund—as you rightly said, we might find that, in any event, our room for manoeuvre is severely limited.

John Mason: I accept that, but assuming that we have more room for manoeuvre, if, over time, the Highlands and Islands comes closer to the Scottish average—there is some evidence that it has done so, which in my opinion has been thanks to the extra funding, so it has been a success—I presume that we will have to consider where the other needs are. Mr Beattie and I are members of the cross-party group on industrial communities, which has a focus on ex-mining areas, particularly in Fife and Ayrshire, that still have particular challenges. The issues might be local—within a council area or a group of councils' area, as is the case in Ayrshire. Could we target relatively small areas of real need such as that?

Ivan McKee: We could do that. The other approach would be to have, for example, a fund for post-industrial communities—I am not saying that we will—that would allow us to focus much more specifically on programmes for communities. In any given council area, there will be a mixture of less well-off and more well-off areas. If we want to target a specific challenge, it might be better to do that through how we design the programme and interventions rather than regionally. Even in the Highlands and Islands, there are wide discrepancies between, for example, Inverness and some of the more outlying areas in the challenges that they face and the support that they need. That would be a way of becoming quite local, so we need to look at the issue in the round.

David Anderson can contribute on that.

David Anderson: On Mr Mason's point about whether we could target smaller areas, that is perhaps an opportunity going forward. At the moment, the only fund that is targeted at a specific area of Scotland is the youth employment initiative fund in the south-west; otherwise, all the funds span either the Highlands and Islands, the rest of Scotland or the whole of Scotland. We do not have flexibility to target specific areas, because of the EC rules. Therefore, if we want to target the Ayrshires—to use Mr Mason's example—perhaps we should be arguing for the flexibility to allow us to do so.

Angela Constance: To follow on from Mr Mason's point about economic development at a more local level, is the minister thinking about how any successor programme could meaningfully link with the local governance review, given that the Government's economic strategy is increasing its regional focus and given the importance of meaningful partnership work with stakeholders in the community sector, social enterprises, the third sector and local government?

Ivan McKee: That is a good point and something that I will certainly consider. I will have a look at the local governance review and see how the programme can align with it. Notwithstanding the fact that we do not know what we will be able to do in future, the changes perhaps give us scope to look more broadly at how we line up with that. The regional economic development agenda and the regional economic partnerships and what we are doing with city deals and city region deals also play into this. There are a number of moving parts, and it is important that we take time to consider how they can all be lined up to best deliver our overarching objectives.

Andy Wightman (Lothian) (Green): Welcome to the meeting, minister. As I understand it, the Government does not really have a regional economic development strategy as such, but it has a regional development agency—and is soon to have another one in the south—growth deals, which it is promoting, and a national planning framework. Aside from the resources that could potentially come from a shared prosperity fund, how do you see such a fund tying in with the existing economic policy levers that I have mentioned?

Ivan McKee: The fund gives the opportunity for that. At the end of the day, it all comes back to the overarching strategic objectives in respect of the four Is and what we measure in the national performance framework. On regional development, we have, as you have rightly said, Highlands and Islands Enterprise, which has a clear focus on economic development and community cohesion in the Highlands and Islands, and the new south of Scotland agency, which will take forward a similar programme. The city region deals have put a clear focus on local authorities and groups of local authorities bringing forward programmes that make sense for economic development in their specific areas.

As you have rightly said, a number of things are happening at different levels and, as I said to Angela Constance, there is now an opportunity for us to look at what we want the programmes to do and how the shared prosperity fund can best fit in with them. We are at the early stages of that. I have not come here with the answers on how we will do that, but I am conscious that the Government needs to take forward that work and that, in my new role, I need to engage with stakeholders to figure out how best to do that.

Andy Wightman: I will elaborate a little more. In the growth deals inquiry by another committee that I am a member of, there was a sense that, when pots of money became available, people just grabbed off the shelf projects that had been gathering dust or put together propositions quickly, and there was not a lot of strategic thinking underpinning some of the projects. Historically, there has been a pot of money that people have made bids for and I get the sense that some of the projects that have been funded had their genesis in similar initiatives—things have been taken off shelves and there has been a bit of ad hocery.

I come to my key question. You have a range of policies in place to try to take a more strategic approach. How much flexibility will you need to ensure that any new shared prosperity fund that comes to Scotland can properly fit in with existing plans and strategies and not just be a pot of money for which people make bids in a rather ad hoc fashion?

Ivan McKee: To some extent, that goes back to my earlier answer to John Mason. If we want a coherent strategic perspective at an all-Scotland level, we need a structure around which programmes will access the funds and a process that must be gone through to check that they are coherent and feed into the overarching strategy and objectives. I understand that, and that is the reason why there is a limit to how much can be devolved. There needs to be an overarching strategic perspective at the Scottish level.

The answer to your question is that we do not know where we are going with the shared prosperity fund. It is very difficult to answer the question before we see the details of the fund and how much scope we will be allowed in Scotland to decide how to design the programmes and allocate the funding. It is clear that we want to be able to do exactly what you said—to look at the landscape, our strategic objectives and what is happening locally, and design programmes that fit into that space—but it is very difficult to answer the question until we see what we will be allowed to do.

Andy Wightman: A specific point was made to us in a discussion with Robin Smail, who is an academic. He acknowledged that there may be a role for a sub-fund to deal with crisis situations or economic shock events. Notwithstanding Brexit, economic shocks routinely take place across the country. Would you consider or contemplate that, or would that be more appropriately dealt with in other parts of Government?

11:00

Ivan McKee: It depends on exactly what you mean by that. If you were to say, “Here’s a given pot of money and, by the way, we want to set up a sub-fund for crises,” the first thing that you would have to do, obviously, is to take some money out of the overall pot, which would make the overall pot smaller. You might decide that that is a priority or that you would rather have the money allocated now so that it could drive forward the strategic programmes that you want to drive forward at this stage. Money for such a sub-fund would not be free money; it has to come from somewhere.

Another factor is the type of crisis that you are talking about. If you are talking about something that is very local and affects a business or a group of businesses in a specific industry or part of an industry, it might be that there is a case for intervention, and the Scottish Government clearly has intervened in such cases in recent years in order to allow certain businesses and industries to go forward and develop. However, if you are talking about a larger shock, such as another financial crisis or Brexit, the impact of which no one can be sure about, whatever sub-fund we have could be dwarfed by the requirements of the crisis.

It is an interesting idea, but I am not sure that, once we start to pick away at some of the fundamental questions, there is much mileage in it. However, it is something that we will have on our agenda to consider.

Gordon MacDonald (Edinburgh Pentlands) (SNP): I want to continue this discussion about the UK's shared prosperity fund. If my understanding of what you said is correct, since the announcement of the shared fund in May 2017, there has been only one meeting between UK Government ministers and Scottish Government ministers. Is there a concern that the method of distribution, administration and evaluation of the fund might not be devolved to Scotland?

Ivan McKee: At ministerial level, I had one meeting with Lord Henley, the responsible minister, but it was a broad, general introductory meeting and we did not go into a lot of specifics, other than to raise the concerns you have just mentioned.

There has been little engagement at the level of officials. I will let David Anderson talk about that in a minute, because I know that things have started to move recently. I mentioned the UK Government consultation, which we are expecting any time now, and we will see where that goes. However, on your general point, you are right to say that, other than some words stating that the Government will respect the devolution settlement, we have no specifics. We are concerned that there is no clarification about the issues around the control of what can be done with the fund, where the money goes, how the fund is managed, how it is audited, what the timescales are, what the methods for accessing it are, who can bid for it and what the match-funding requirements are, and about the possibility that all of that could be controlled at a UK level. We have seen nothing to suggest that that is not the case, as far as I am aware.

Gordon MacDonald: You also touched on the fact that this consultation is late. Given the delay in the system and the fact that Scotland currently has a pot of money available to it in the current EU structural fund round of about €944 million for the 2014 to 2020 period, what would the economic impact be in Scotland if there were to be a delay in the full implementation of the fund by the end of 2020?

Ivan McKee: The loss of those millions of euros would represent a significant impact—the impact would be more than just fiscal because, obviously, we get more benefit back for our investment. However, if we fall off a cliff and there is a no-deal scenario, the UK Government has indicated that there would be a Treasury guarantee, so it would fund the programmes to the end of the 2020 period. Beyond that, we do not know the scale of the numbers in the shared prosperity fund, so the issue is a big unknown. That is quite a concern.

David Anderson: The issue is not just about the cliff edge; it is about the fact that stakeholders are already planning now for what comes next. How we get some clarity is a live question in the minds of stakeholders, because they are wondering whether they can continue the programmes that they are running or whether they have to make some provision for them not being there. We have made that point to officials elsewhere, and they are aware of those concerns. Their view is that the shared prosperity fund will be ready to go on 1 January 2021.

Gordon MacDonald: Let us hope so. There has been a suggestion that any new UK shared prosperity fund will have the opportunity to look at different areas of the economy that it could not previously look at under EU rules. However, the committee heard evidence from Robin Smail of the European Institute of Public Administration and from Professor Bachtler that

"with aspects of state aid and public procurement, we will most likely have to continue to follow the EU regulatory framework."—[*Official Report, Economy, Jobs and Fair Work Committee*, 15 May 2018; c 32.]

Given that that is a possibility, how much scope is there for introducing programmes that are different from those that we currently have?

Ivan McKee: On the state aid point specifically, you—or the witnesses—are right, because the UK Government's expectation is that the state aid rules will continue pretty much as they are for the foreseeable future, not least because, if we are hoping to do a deal with the EU, it will want to know that we are not doing things with state aid that would disrupt normal trade. The expectation is that those rules will continue as they are, which means that the scope for doing something else is limited. There may be something in the margins, but at a significant level we do not anticipate that we will be able to tear up the state aid rules and operate as if they did not exist.

David Anderson may wish to add more on state aid.

David Anderson: The point about state aid that the minister has made is absolutely right. The question is about what flexibility there is going forward, and the EU rules and guidance are pretty detailed about what you can spend the money on and what the outcomes are targeted at.

We would all hope that there is the flexibility that the minister talked about in response to earlier questions. Flexibility to be able to write the programme that addresses the needs of Scotland's economy is the flexibility that would be sought, without prescribing to the nth degree what we actually mean by that in terms of funding outcomes. There is always a balance between prescribing to the nth degree and being very clear, and just leaving it very open, which makes people question how to define the value and how to define the audit trail to ensure that we have got the value out of the additional money.

Dean Lockhart: I have a supplementary question about Government support for the economy. Last week's programme for government announced a new national export plan with £20 million of support over the next three years. Could the minister clarify which agency will deliver the national export plan, and the form of financial support that will be available under the plan?

Ivan McKee: That is a bit off-topic, but I will answer. You are right to say that there is £20 million for peer-to-peer support for 100 businesses and support for 50 businesses to enhance and develop their export potential and encourage them to grow. That is part of a whole range of activities that are going on, and there will be more in the export plan, which I am working on at the moment with officials. I have a Board of Trade meeting next week to develop that further. Which agencies receive that money will depend on what businesses we are talking about and how that £20 million is going to be spent. The examples that I have given account for £2 million or £3 million of it, so exactly how the rest of it will be spent will be set out in detail in the export plan that will be unveiled in the spring of next year. We are working hard on that at the moment.

There is much more to it than those specific interventions. There is a lot of work going on around where trends in exports have been by sector and what kinds of companies offer the most potential to grow exports, and therefore what sectors and geographies we should focus resources on to maximise Scotland's export potential. That is quite a significant piece of work and it will see the light of day sometime in the early part of next year.

Dean Lockhart: Has it been decided which Government agency will deliver, oversee and implement the national export plan?

Ivan McKee: Clearly, all agencies are involved in it. Scottish Development International is at the forefront of that, because it is the agency that is working internationally, but other agencies have a role, for example in encouraging businesses to export, which Highlands and Islands Enterprise and Scottish Enterprise do at the moment through their account management processes as they engage with businesses and ask how they can help them to export more. Those businesses are then brought to the attention of SDI so they can be involved in trade missions and put in touch with GlobalScot, trade envoys or the investment and innovation hubs that operate internationally to provide a whole range of support to link businesses up with opportunities in their sectors globally.

To answer your question, it is SDI that is at the forefront of that work, but all the other agencies have a role to play in supporting and working with businesses to maximise their export potential.

The Convener: If there are no further questions from members, I would like to thank the minister and David Anderson for coming in today.

11:11

Meeting continued in private until 12:11.

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