



OFFICIAL REPORT
AITHISG OIFIGEIL

Finance and Constitution Committee

Wednesday 4 November 2020

Session 5



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FINANCE AND CONSTITUTION COMMITTEE

27th Meeting 2020, Session 5

CONVENER

*Bruce Crawford (Stirling) (SNP)

DEPUTY CONVENER

*Murdo Fraser (Mid Scotland and Fife) (Con)

COMMITTEE MEMBERS

*Dr Alasdair Allan (Na h-Eileanan an Iar) (SNP)

*Tom Arthur (Renfrewshire South) (SNP)

*Jackie Baillie (Dumbarton) (Lab)

*Alexander Burnett (Aberdeenshire West) (Con)

*Angela Constance (Almond Valley) (SNP)

*Patrick Harvie (Glasgow) (Green)

*Dean Lockhart (Mid Scotland and Fife) (Con)

*John Mason (Glasgow Shettleston) (SNP)

*Alex Rowley (Mid Scotland and Fife) (Lab)

*attended

THE FOLLOWING ALSO PARTICIPATED:

Charlotte Barbour (Institute of Chartered Accountants of Scotland)

John Cullinane (Chartered Institute of Taxation)

Councillor Gail Macgregor (Convention of Scottish Local Authorities)

Eileen Rowand (Chartered Institute of Public Finance and Accountancy)

Mark Taylor (Audit Scotland)

CLERK TO THE COMMITTEE

James Johnston

LOCATION

Virtual Meeting

Scottish Parliament

Finance and Constitution Committee

Wednesday 4 November 2020

[The Convener opened the meeting at 09:00]

Pre-Budget Scrutiny 2021-22

The Convener (Bruce Crawford): Good morning and welcome to the 27th meeting in 2020 of the Finance and Constitution Committee. The first item on our agenda is evidence taking as part of our pre-budget scrutiny from respondents to our call for views. We will hear from two panels.

I welcome the first panel of witnesses and thank them for providing us with written submissions. Mark Taylor is audit director at Audit Scotland; Councillor Gail Macgregor is the resources spokesperson for the Convention of Scottish Local Authorities; and Eileen Rowand is the chair of the local government directors of finance section of the Chartered Institute of Public Finance and Accountancy.

If the witnesses do not mind, I will go straight to questions. My first question is for Mark Taylor from Audit Scotland. In your organisation's submission, you talk about

"the challenges facing Scotland and their possible impact on the 2021/22 Scottish budget".

On the implications for block grant funding, you highlight that

"the majority of UK spending on Covid-19 has been funded by additional borrowing, which generates Barnett consequentials",

and that

"If the UK government chooses to fund some of the continuing Covid-19 spending through reprioritising spending in other budgets in devolved areas, the Barnett consequentials are reduced. In such circumstances, the Scottish Government would also need to decide whether to reprioritise its own budgets accordingly."

To what extent is that likely to impact on the Scottish Government's budget for 2021-22? If it is likely that that happens, should we expect to see the details in the United Kingdom Government's one-year spending review at the end of November?

Mark Taylor (Audit Scotland): Good morning. The context for that question is the huge amount of uncertainty, volatility and complexity that is built into the budget as we work through this year and as we look towards the 2021-22 budget.

It is clear that the way in which the Barnett formula works means that consequentials can go up—which is generally our experience—and that they can go down. As the UK Government seeks to manage its own budget, it is of course trying to balance expenditure across a number of headings. As we have seen, as it finds savings from its own budgets elsewhere, the consequence of that sometimes plays through to the Barnett consequentials. As we look through this year, we will continue to see some of that; there is uncertainty around that and there has been a whole discussion around the implications of that. Our expectation is that such volatility will continue into next year as well.

Of course, there is a challenge for the Scottish Government and the Scottish Parliament in setting the budget when we are not clear at this stage when the UK budget might fall. When the UK budget comes, I think that it will provide details and information about the starting point for next year. However, as we have seen, a lot happened through the year this year, and we would expect that to continue. In relation to the way in which the budget is established and prepared, it is a case of making sure that the expectation of further change is recognised at the outset and that it is clear to the Government and the committee where the room for manoeuvre might be as things develop throughout the year.

We have seen this year that a significant amount of funding has come from the UK Government, which has supported most of the Covid spend. Nonetheless, there is also an opportunity for the Scottish Government to make adjustments to its own spending plans in expenditure areas in which it is perhaps not possible to spend at the same level because demand has fallen off, and in areas in which there is a necessity to move money around. The Scottish Government has done that, and I would expect that pattern to continue.

The Convener: Thank you—that was helpful. You paint a picture of a fairly turbulent situation that will probably continue to be subject to significant on-going change, so who knows what additional Barnett consequentials might become available or vice versa?

I know that Murdo Fraser wants to explore this area, but I want to begin to tease out the timings. If you were in the Government's shoes—I know that you are not—given the level of turbulence and the potential for change as we go along, what would that lead you to think about the timing for publishing your budget?

Mark Taylor: I absolutely recognise the challenge that the Government and its officials have at this time. I will resist the temptation to suggest directly a budget day; when best that

might be is a judgment for the Government and the Finance and Constitution Committee.

Historically, the Scottish Government requires to set its budget before the UK Government sets its budget; that provides a starting point for the year and, through the summer, autumn and spring budget revisions, there is the possibility of updating that. I expect that pattern to be followed next year.

One of the key considerations is what can and cannot be changed down the line. For example, there is only one opportunity to set Scottish income tax rates and bands for the year; they cannot be changed down the line. In other aspects of the budget, there is perhaps an opportunity to rebase things and tweak policies and spending priorities as we go and, this year, we have seen the Government's ability to do that. However, I recognise that it is very difficult to do that once a budget and momentum are established. It is also challenging for the public bodies and councils that are in receipt of funding, because they need a degree of certainty and expectation. Therefore, I appreciate that room for manoeuvre is limited, but we have seen this year that there is an opportunity to develop the budget position through the year.

The Convener: For my final question in this section, I will move on to a slightly different area. In your submission, you also cover the implications of tax revenues, which will depend on the performance of the Scottish economy relative to that of the rest of the UK. The committee is now well versed on that, because it is an area that we have covered in our previous budget reports. If Audit Scotland has determined a view on the matter, it would be useful if you could outline what the current Covid situation might mean and how it might affect tax revenues and the Scottish budget. Others will want to ask similar questions, but I want to set the scene.

Mark Taylor: Of course, as the committee knows, forecasting and looking ahead to the impact of that is very much the Scottish Fiscal Commission's business. From an Audit Scotland perspective, we recognise the range of things that might happen and the factors that are at play. As the committee understands, because we have talked about it before, we would expect a hit on tax take and an increase on spending pressures across the piece, but particularly in social security.

As you said, convener, what matters to the overall budget is the relativity—the difference between what happens in the Scottish context and the UK context. Ultimately, that affects the amount that is available in the budget. To further complicate the picture, there are timing differences on different aspects of that. It is very difficult to speculate on that. I think that spending pressures will go up and that tax take is likely to drop down; I

think that that will happen across Scottish Government taxes and a range of taxes.

Another key ingredient is how the UK Government responds to the situation now and in the next budget year. Its overall fiscal policy sets the overall spending envelope and the appetite that it has for different levels of borrowing, as well as how that plays through to the underlying block grant. The tax and social security effects are about the relativity on a per-head basis; in addition to that, there is the relativity of the performances of the different jurisdictions over the year and in the period leading up to it.

Although the Scottish income tax impact will come down the line and that amount is locked in, the budget for next year will be driven by what the forecasters—the Office for Budget Responsibility and the Scottish Fiscal Commission—make of the relative position as the budget is set, as well as their take on the prospects for the economy and, importantly, how that flows through to tax take and social security spending.

The Convener: I do not envy the Cabinet Secretary for Finance having a fixed budget in such turbulent times. Others will undoubtedly want to touch on flexibilities that might be available.

Murdo Fraser (Mid Scotland and Fife) (Con): I will direct my question on local government funding at Councillor Macgregor and then Eileen Rowand.

In your joint submission, I was interested to read the comments about fiscal flexibilities and the need for a fiscal framework between the Scottish Government and local government. We regularly hear from the Scottish Government about its complaints and concerns about the fiscal framework and the relationship that it has with the UK Government. We also hear about the fact that it feels that its hands are tied in certain areas and that there is a lack of information.

From reading your submission, it seems that similar complaints are being made by local government regarding its relationship with the Scottish Government. I am interested to hear your thoughts on that. What do you think needs to improve as regards the relationship between the Scottish Government and local authorities, both in general terms and more specifically in the context of the budget that is coming up shortly?

Councillor Gail Macgregor (Convention of Scottish Local Authorities): Good morning. The sun has just come beaming in my window, so I hope that you can still see me.

In respect of the fiscal flexibilities, over the past few months, local government has been very good at working collaboratively with the Scottish Government, and the fiscal flexibilities have arisen

from an acknowledgment—as Mark Taylor has touched on—of the volatility and uncertainty that exist. Local government has been proactive in trying to find solutions to get us through the short to medium-term difficulties that we are facing as a result of Covid.

The fiscal flexibilities were instigated by local government, and by working collaboratively with the Scottish Government, we have reached a point at which three of those flexibilities will be capable of being utilised by local councils, should that be required. I stress strongly that directors of finance are not looking at those as palatable options; they are for a worst-case scenario. However, they will certainly help some—although not all—councils to plug a gap, if required. I stress that none of the options is a replacement for cash. If additional consequentials come through, we will keep an eye on those and ensure that local government's share is given to local government. The fiscal flexibilities have been a positive piece of work with the Scottish Government, but they are by no means the solution.

Because of Covid, much of the work on our fiscal framework was halted temporarily, and we need to get back to the stage of having proactive discussions about what the relationship between local government and the Scottish Government will look like.

Fairly recently, we launched our blueprint, which encapsulates local government's vision for the short, medium and long term. That is an important piece of work that we need to do with the Scottish Government. It is certainly signed up to doing it, but it is a question of finding the space in the current landscape to make that work meaningful. That would also involve all Opposition parties across Parliament.

We are currently looking for a substantial shift in the balance of funding, more sustainability of budgets, longer-term budgeting and more flexibility around the funding that we receive to ensure that it is utilised in the best possible way at local level.

That was a quick canter through the fiscal flexibilities and the framework, but I can pick up on any specific points.

Eileen Rowand (Chartered Institute of Public Finance and Accountancy): I will start with the fiscal flexibilities. As Councillor Macgregor has outlined, those are one-off measures that we can take—they do not provide recurring funding. A number of directors of finance are considering how they can use those flexibilities to meet Covid pressures.

It is worth while highlighting the fact that the flexibility that is available to councils varies. A lot of it depends on councils' loan structures and when they took out public-private partnership and

private finance initiative contracts, for example. The impact of Covid also varies. The flexibilities will provide solutions, but they will not be a panacea. A great deal of funding has been provided, but we are still wrestling with a significant funding gap. We are all trying to develop financial strategies that will ensure the sustainability of councils' funding in-year.

09:15

That is where we are this year. We are obviously starting to look at next year. The fiscal flexibilities apply next year, so we will still be able to use them. In looking at our budget for next year, we are looking at what the impact of Covid will be and whether the flexibilities will help us with that. It might well be the case that there will not be full coverage through that means and that there will still be a requirement for funding.

On the fiscal framework, commitments were made to look at replacing council tax and devolving non-domestic rates, as well as the fiscal framework for funding local government. What is important to me as the director of finance for a council is reaching a point where there is stability of funding for local government. If we look at the funding for local government in recent years and the funding in the Scottish block, it is clear that there has been a significant difference. We are keen to develop a fiscal framework that gives us more certainty on how the Scottish block moves and how that impacts on councils' funding.

The issue of relativity—how local government funding compares with funding for other public bodies in Scotland—is extremely important. Local government plays an important role in a number of services, such as health and social care and wellbeing. Our response to the pandemic has shown the value of local government. If we are to continue to provide services, we need funding. I recognise the challenge that the Scottish Government faces in choosing how to use its money. We are trying to make the case for more stability for local government funding.

Murdo Fraser: I would like to pick up on a couple of points that you have made. Local authorities hold reserves. Where are we with those? Are councils having to dip into those? What will be the impact on next year's budget? Will reserves have to be utilised to help balance the books? We know that councils have had to do that in the past, but we may now be in an even more serious situation.

My second question is about the timing of the budget, which the convener mentioned earlier. When do you want to see the Scottish Government budget?

Eileen Rowand: Councils will be looking at their reserves as a way of dealing with the pandemic. The position on that varies from council to council. Some councils do not have the scope in their reserves to provide the cushion that reserves are intended to give.

In Fife, we have been trying to estimate the impact on the current year and to look at the funding that is coming from the Scottish Government. We are also looking at the measures that we can take to reduce in-year costs and to incur only essential spending, as well as whether we can use flexibilities and our reserves.

Reserves are similar to fiscal flexibilities: they are a one-off. They are there for councils to use in dealing with short-term shocks. Covid is not the only thing that we have to deal with. My council has a risk register of the items that we expect will impact on our budget: there are 15 to 20 items on that list. Our policy is to hold 2 per cent of our funding in reserve for dealing with those shocks. That includes Covid. However, I certainly would not want to clear out my reserves in full, because it is my responsibility as a section 95 officer to ensure that the council is sustainable, and that means that we will have to hold a level of reserves. I anticipate having to use reserves. It is not the case that I do not want to, but I am looking at the other risks that we face.

With regard to the timing of the budget, my answer is “as soon as possible”. As for what we are doing as a council, I will take a budget report to our committee in November, and then, as we do every year, we will try to anticipate different factors, including the size of grant that we receive from the Government and what flexibility we have.

We will also model a number of scenarios of what the budget cap could be. Then, in the background, we will be planning in order to look at how we can address them. However, until we actually get the Scottish Government budget, there are issues with that. I know that there have been discussions about that not being until early February. We have to get our council tax bills out at the start of March at the very latest, so the timing of the Scottish budget has a real impact. We can do a lot of planning in the background, but we will not have those figures. Once we get them, we will have a very short period between knowing what the Scottish Government budget is, determining how it impacts local authority spending and setting the local authority budget and council tax.

Councillor Macgregor: I would like to cover the technical aspects of a number of the areas that you want answers about. On balancing our budget, having been in my job for 13 years, I have to say that, when people ask what reserves are for and when we are going to use them, the rainy-day

scenario has always been brought out. My feeling at the moment is that we are in a rainy day.

There is acknowledgment from councils that reserves must be used, but that is why we have put together this basket of options alongside the fiscal flexibility, the additional cash funding that has come through to councils and the other mechanisms that we have put in place, which we hope can ensure that every council has a mechanism to get it through a very difficult period. The basket of options is very important.

In respect of the budget timing, obviously this is the second year that we will have a delay to the budget, although it is for very different reasons. That delay causes complications, which Eileen Rowand has covered. Ensuring early engagement and as much certainty about figures as possible is key. We are already engaged in proactive discussions with the Scottish Government on an early budget and the implications of it running on late. As Eileen touched on, one big implication of a delay is councils not being able to set council tax early enough to enable them to get the bills out to households in time.

Mirroring last year, we might need to look at decoupling council tax from the main budget. That would have risks, but at least it would give a level of certainty around that element of the budget. In respect of the rest of the budget, if we can look for at least estimates of projections to come as early as possible—I think that Mark Taylor touched on this earlier—with some form of reconciliation occurring slightly later, that would be a better scenario that it dragging on into March and councils not having that certainty.

My answer is: the earlier the better. We are in constructive discussions to that effect already.

The Deputy Convener (Murdo Fraser): Thank you both. I think that we have lost connection with the convener, so I will take over as convener for the time being and try not to let that go to my head. I will bring in Patrick Harvie, and then Angela Constance.

Patrick Harvie (Glasgow) (Green): I will pick up on one or two of Murdo Fraser’s questions before turning to a different issue.

First, on the timing issue, how much actual harm resulted from the fact that some councils had to make decisions on budgets and council tax before the Scottish budget had been passed? That was obviously deeply uncomfortable for many people making local decisions, but was actual harm caused, in the sense of services being cut or jobs being lost, as a result of that cart-before-the-horse approach to budget setting?

On the matter of financial flexibilities, is the package of flexibilities that was agreed last month

between local government and the Scottish Government the end of the story, or are you still seeking additional flexibilities, which were not part of the package that has already been agreed, on capital receipts and debt repayments?

Councillor Macgregor: It depends on what we regard as “actual harm”. Obviously, all services can be impacted by delays. Any uncertainty within the system can cause a loss in morale, and it can create a culture of uncertainty within our staffing cohort. There can be a slight fear among the people we serve that their service will be cut. As you will be aware, councils go out to consultation on many of the measures that they believe they may have to cut. If we put that uncertainty out into the system, it is difficult to take it back. I will let Eileen Rowand, as a director of finance, give some local examples.

In respect of fiscal flexibilities and the package of measures that we considered, we have managed to come to some agreement on the ones that are within the gift of the Scottish Government, and we can now utilise them, although the detail of those measures is still being worked up to a certain extent.

There are two more asks that we had considered. One concerned what was effectively a Public Works Loan Board repayment holiday, which was in the gift of the UK Government. At this time, it was not willing to give us that flexibility on the basis that it would prefer to give us additional cash settlements. Cash has filtered through since that decision was made, but that will obviously not be enough to cover the deficit in local government.

The other ask was the ability to use capital for revenue purposes. Again, that was within the gift of the UK Treasury. I understand that Kate Forbes is continuing to pursue that, but I have not had a response or update on that particular issue.

Perhaps Eileen Rowand can talk about some actual harm within local communities in relation to the delay to the budget.

Eileen Rowand: We will be trying to do planning in the background before we potentially get to a Scottish budget position. The variables that could change may lead us to take some decisions that are perhaps premature, before knowing our funding position.

The first thing is council tax. You know that there is a 3 per cent cap. If we could get early indication of what flexibilities we have around council tax, that would be welcomed.

There are two other main areas. We will be making a lot of assumptions around planning for what the pay awards may be in comparison with the level of grant that we receive. If our core

funding reduces and there is a significant pay award, that will impact adversely on local government, and we will be considering the affordability of that.

Last year, we were not that far away in our planning assumptions from the initial budget that was agreed. More funding came in later in the process. That may have been down to a bit of luck last year. This year, there is greater uncertainty regarding the economy and what the UK Government’s response will be, but we should see more when the spending review is announced at the end of November.

On the question of what harm is done, if we have to set a budget in March and we do not get our information until February, if there is a significant movement, it can be a matter of coming up with alternative proposals. There could be a danger of agreeing to a reduction in service delivery that impacts on communities when that was not actually required. Those are the main areas, I suggest.

09:30

Patrick Harvie: I will move on to the context for the 2021-22 financial year. Coming through the pandemic and the Brexit uncertainty and the resulting harm are big features of the current year. We all hope that, by the time that we are into 2021-22, we will be looking to move beyond and recover from those crises. What are the key features of the recovery phase, particularly from Covid, that will impact on local government? We are all aware of the debate on the need to reset social care in many ways—I have no doubt that that will be a big election issue—but there will be immediate impacts on local government finances of trying to move beyond dealing with a pandemic and starting to recover from it. Can you paint a picture of the recovery phase?

Councillor Macgregor: Patrick, as I know you will appreciate, because I have been working with you for three years, local government budgets have been decreasing year on year anyway, so we went into Covid in a weaker position than we would have been in five years ago. The way that we have coped and dealt with it and worked collaboratively with Government has been a positive, in that having more discussion around how we deliver services and being more engaged from the start when Government is putting together policies and making announcements has a more positive impact in our communities.

One difficulty of reducing budgets year on year is that we are now moving out of a three-year pay deal. Pay claims will arrive on my desk within the next two or three weeks. We do not yet know what public sector pay policy in Scotland will be, and

that probably will not be announced until budget time. I will be beginning to engage in pay negotiations slightly blind on funding envelopes. We have on-going Scottish Government policy commitments on health and social care and the living wage, which are all very valuable things. However, putting those alongside the continuing Covid pressures—like you, I am optimistic, and I hope that, at some point next year, we will be out of this and moving into recovery—we are very mindful that there will be on-going effects of Covid for a long time, even, for example, with regard to the administration of business grant schemes by councils. There are pressures in and around our normal work, and none of that is going to go away, so we need to engage constructively with all parties and Government to ensure that local government is covered to do the best job that we need to be doing, as well as all the additional stuff that we have had to cope with over the past seven months and might have to cope with going forward.

Health and social care will be big issues. Pay will certainly focus a lot of people's minds, particularly given the role of key workers within councils and the national health service and emergency services. Obviously, we are still looking to plug a fairly significant loss-of-income gap, so the pressures around service delivery in those areas could escalate going forward. We are going into a perfect storm with Brexit as well, so we need to look at exactly what we need to deliver and how it needs to be delivered, to ensure that our communities get what they need, without putting local government in a position where we simply cannot afford to deliver some vital services.

Patrick Harvie: Do either of the other witnesses want to add anything?

Eileen Rowand: I will add to that from a council context, as a director of finance. We know that there is a lot of pressure in the system. I see the impact on councils' budgets and how we have been able to perform in recent years. It is becoming more challenging and it is getting harder and harder for services to deliver on agreed savings and come forward with new propositions. We are looking at how we can use innovation and technology to change how we deliver our services. However, the pandemic has slowed some of that down, simply due to our capacity and capability to do that given the way that we have had to operate and the focus that has had to be placed on other areas in supporting businesses and communities in these trying times.

We know that there will be a continuing role for local government in supporting the economy. We are a major employer, but we also have an important role in supporting businesses. When I look at my pressures for next year, I know that

there will be a legacy of Covid into the next financial year. We have been hit dramatically by a loss of income and we know that we will not recover next year; it might take a couple of years for us to get back to where we were before. That will be a major impact. There will also be the costs that we are incurring just now. We are obviously having to deliver our services differently and there are personal protective equipment costs and energy costs in relation to how we are having to operate. As I said, we therefore know that there will be impacts from Covid. Although we are obviously looking at the fiscal flexibilities, as I have said before, that door might not be open to all councils, depending on what they start off with.

Gail Macgregor already touched on health and social care. We know the demographic pressures that there are in the system, which will increase. The aim in relation to health and social care is to try and keep more people at home, which means that it is really important that we invest in health and social care. That goes back to parity of funding between health and councils in order to allow us to transfer the balance of care to more home settings.

The Convener: I thank Murdo Fraser for taking over the role of chair. For some reason that I do not understand, I became disconnected for some time. We move to Angela Constance.

Angela Constance (Almond Valley) (SNP): I will start by picking up on a point that Gail Macgregor raised in response to Patrick Harvie. Ms Macgregor said that COSLA made a call on the UK Government to have a repayment holiday with respect to the Public Works Loan Board. Is COSLA still pursuing that with the UK Government, and is the Scottish Government supporting it in that call and making representations to that effect on its behalf?

Councillor Macgregor: We have not pursued the Public Works Loan Board call since. Leaders recently made the decision to park that one for now. It is one that we will keep up our sleeve for if the financial landscape shifts even further. We will certainly pursue it if we have to, as it would generate significant savings for councils. However, the UK Government would prefer to give additional cash to cover that, which I will certainly be holding it to.

The Scottish Government was working with us on the capital-to-revenue element. Ms Forbes wrote to the Treasury specifically in order to support us in our bid to be able to use capital to revenue. The initial response is back and it is not particularly positive. I understand that Ms Forbes has since gone back to the UK Treasury; however, as I said earlier on, I suspect that she is still waiting on a response. That is all still there and in play, but having to work through different

mechanisms to get different outcomes is very complicated.

Angela Constance: Given the UK Government's ability to borrow money, I appreciate the attractiveness of access to cash to both the UK Government and local government.

Moving on to the issues of economic recovery and development, the witnesses will have seen this week that there is still a lot of to-ing and fro-ing around the furlough scheme. What is the importance of the furlough scheme continuing at 80 per cent after 2 December to ensure that businesses have support available when they need it in relation to the impact on jobs and the local economy?

The converse question is what the impact on the local economy would be if restrictions in Scotland were heightened not for public health reasons but to enable people to access the furlough scheme in line with what is currently available in England.

I put those questions first to the local government representatives, who in their submissions have spoken about economic development.

Eileen Rowand: I will come in first, then I will hand over to Gail Macgregor.

The furlough scheme has provided assistance to businesses that has enabled them to continue to pay their staff. We had been aware that it was due to end at the end of October, but it has now been extended until 2 December. The concern in local government—as it is across society—is about the impact that the end of the scheme will have on employment rates. We want to ensure that we can provide support to individuals who might become unemployed, among whom we expect there will be a lot of people who have never previously been in that position. Along with money advice and other services, we are trying to tailor our support to ensure that when there is a peak in unemployment we can help such individuals—for example, with accessing universal credit. In councils, a lot of work has been done on community provision, to ensure that if people are in hardship we can continue to offer them such services. In the background, we are planning for a peak in activity and are trying to ensure that we can continue to provide support.

The question about how long the furlough scheme should continue is quite challenging. It has to be responsive to where we are with the virus, but affordability certainly comes into the picture.

Councillor Macgregor: The furlough scheme has seen significant investment being made in individuals, which has been vital over the past few months. I hope that any Government across the

UK would wish for that to continue while sanctions are still being imposed such that people cannot go to work, albeit for good reason.

My view of the position beyond 2 December would depend on the measures that we might be under at that time. As Eileen Rowand has said, COSLA's role is in the areas of economic sustainability, employability, and skills support for those who are struggling or are losing their jobs. As I have said, furlough has been a lifeline for that.

Apart from a few exceptional cases, we were not able to furlough council employees, so councils themselves have not used the scheme. Our role has been more about providing overall support for our communities and the individuals within them.

One of the most important schemes in which we have been involved is the management of business grants. Councils played an exceptional part in administering the initial business grant scheme: we hit the ground running and got money out to businesses as quickly as possible. We are now seeing such schemes being expanded or extended—for good reason—to support businesses as we go through the setting of various tiers and lockdowns. I suspect that those will continue into the new year. Our role will be to ensure that businesses get the grants that they require as quickly as possible.

However, I have a slight concern about councils' capacity to deliver that. Back in the early days of the first furlough scheme we were able very quickly to second members of staff over to a business grants team so that we could get those payments out of the door. As the rest of council services return to relative normality, some of those staff will not be available for secondment so there might be pressures on councils as they try to continue to deliver such grants.

A combination of an on-going furlough scheme to support individuals who are being told to stay at home and not go to work—for good reason—and proper business grant support to our local businesses is absolutely imperative.

09:45

Angela Constance: In its submission, Audit Scotland spoke about how Covid

"will change the way that public services need to be delivered".

COSLA also spoke about the importance of "public sector reform". We all know that Covid has necessitated a different way of doing things, including service delivery.

In both the short and long term, how can we advance public sector reform and what are the

challenges and opportunities for the budget, given the importance of human rights and wellbeing?

Mark Taylor: We should start with the understanding that a requirement in a number of areas of public services—we have talked about the health sector—existed before we came into the pandemic. The Accounts Commission had indicated the need for local government to consider how it provides services, so the underlying need for public service reform and consideration of how services are provided was already there.

The pandemic has changed our mindset across the public sector on the speed at which those changes can be achieved—we have had to switch to remote working overnight in places for example—and we have had to adopt different ways of doing things. Although those ways have perhaps not been as efficient as they might have been, the pandemic has provided a paradigm shift in how we can deliver services. We need to think about how to put that learning and energy into public service reform.

The other point to consider is the reality of the economic and financial situation. We have so far focused on the here and now, but a degree of economic scarring and continuing pressures on public finances are likely. All public organisations—councils and other public sector bodies—need to review how they do things. Part of that process is about prioritisation and another part is about innovation, which different ways of using information technology, big data and so on could support. Fundamentally, organisations need to consider how they deliver their services and respond to the environment that we face.

I want to touch on one of the previous questions, which is pertinent here. As colleagues have referred to, there will be a legacy from Covid, which will impact on healthcare, social care, schools and education, and there will be a need to invest in recovery in those areas. There will also be an opportunity to rebase how public services operate and consider the sort of country that we want to be and how we want to move towards that in the aftermath of Covid.

Eileen Rowand: Mark Taylor has highlighted quite a lot of points about what the pandemic has taught us about the pace of change. Our capacity for change has however been impacted. My colleagues in education, children's services and communities are under a lot of pressure just now as well. There is a desire to ensure that we can release capacity to drive forward innovation, because that drive has been impacted in the past few months.

It is also important to highlight that we often require one-off investments for change. We

referred earlier to the role of reserves: we tend to use reserves for those investments. We would use our reserves to take spend-to-save initiatives if we needed them—we would not be able to take those initiatives from our core budget.

It is really important, given the challenges that we face, that we redesign how we deliver public services, but we require one-off funding to do that, which we get through reserves that have obviously been eroded, and I know that some councils are in challenging positions.

The public sector also needs capacity. A lot of change is happening in the health and social care sectors as they try to use digital technology a lot more and to consider how they can keep people at home—those factors are often problematic for them as well.

The Convener: You mentioned the issue of business grants and the exceptional performance of local authorities, particularly for the first roll-out. Before I go to Alex Rowley, I want to make clear, as far as my own local authority in the Stirling area is concerned, that I wholly endorse that—it has done a remarkable job and I am sure that it is the same across Scotland.

Alex Rowley (Mid Scotland and Fife) (Lab): I will begin by asking Mark Taylor a question: in your submission, you say that

“under the current circumstances, accurate forecasting will be particularly challenging”.

If we look at previous forecasting and the fact that we have a £550 million deduction to come from the budget and you say that it will become more difficult, that could stack up even more debt. I sort of laugh when I hear Eileen Rowand talk about a fiscal framework that will bring stability, because the fiscal framework that we have in place for the Scottish Government and the UK Government does not seem to bring stability; if you were designing a financial system for Government, I am not sure that you would come up with what we currently have. What is your view on that?

Mark Taylor: The committee, along with the Social Security Committee and the Government, has set out its views on areas for review around the fiscal framework. The fiscal framework has operated for a number of years, but some aspects of it have yet to fully price through—for example in relation to social security, including the full spend and the reconciliation process around all that. It is important that in looking at how that operates, the experience of those years plays into that and is reflected on as we go on.

On forecasting, and I am sure that you will have spoken to the Scottish Fiscal Commission about this, those early forecasting errors resulted from not really having actual administrative data on

Scottish income tax for the first number of years of forecasts; normally, as that data comes through, we would expect forecasting errors to drop off, and we have seen evidence of that. Incidentally, that £550 million has been firmed up and you will have seen from the outturn report that the adjustment to next year's budget will be in the order of £309 million now that the actual numbers have come through.

I recognise that the fiscal framework was not built for Covid. We did not have Covid in mind when the fiscal framework was established and the levels of volatility and uncertainty that we are experiencing as we look towards 2021-22 and, importantly, in-year, as things have adjusted throughout the year, are far ahead of what anybody envisaged when the framework was established. It is important that all those things play in to the review.

Alex Rowley: Eileen Rowand mentioned the risks for councils and you talked about the risk to income from council tax as a result of Covid. I ask more generally about the loss of income, which you also mentioned; do we have a picture of what kind of figures we are looking at? Increasingly, over the years, as you well know, local authorities have looked at raising their income to substitute for some of the cuts from central Government, so what does that position look like and is there a balance there? In Fife, which we both know, I noticed during the early period of Covid that car parking charges, for example, were off, which was good in one sense for the local town centre economy. Is there a connection between, for example, local football teams getting shut down because they have no income and the councils increasing charges for the hire of the pitches?

Eileen Rowand: I have some information on that. It varies from council to council and it depends on the level of income incorporated in each council's budget. I have looked at the situation in several councils. In some councils, the loss of income compared with the total impact of Covid could be 50 per cent, whereas in other councils it could be as high as 86 per cent. The loss of income is what is having such a significant impact, while the costs are less significant.

In Fife, we have seen a loss of income over a wide range of areas. Parking has been mentioned and for Fife, we are forecasting a loss of parking income of £3 million this year. We are seeing a huge impact on our leisure sector, including in the arm's-length external organisations. That is in the region of £6 million if we include our halls and centres and community use. Our council tax income has been impacted by roughly £2 million. Another significant item is internal trading charges. The impact is right across the board. The loss of income that we were projecting for Fife when we

did our last forecast was £46 million in this financial year. I expect that there will be a legacy in the next financial year. If we compare that with the total impact of Covid that we were forecasting at the time, which was £78 million, the loss of income accounts for roughly 60 per cent.

There is a balance to be struck between where we charge income and the use of our services. That income is already budgeted for, so we would have to come up with a financial strategy to meet any loss of income that would impact our budget in the current year and the next year. I have a financial strategy for the council which means that I think that I can deal with the impact of Covid this year—although it depends on what happens in the next few months. However, I am really concerned about the financial position of all councils next year. That is dependent on the level of funding from the Government, the pay policy that is agreed and what we need to do.

At the end of the day, it all comes down to choices and where the priorities are. I expect my council to give consideration to charging and income and what impact that has on access to services. It will also come down to affordability.

Alex Rowley: Are councils projecting a gap in their budgets in the current financial year, or are they predicting that they will meet their budgets or put money into reserves? Where are we in this financial year?

Eileen Rowand: The position varies from council to council. As directors of finance, we have discussions about the position that councils are in. A number of councils will be able to find their way through this year. In my council, a report in August highlighted that there would be a net impact of £78 million, and we agreed a funding strategy that meant that we would be short by £13 million. As part of that strategy, I agreed that we would use reserves up to £10 million. That would take me down to a very low level of reserves, but that was something that I would have to deal with going forward. That is what I mean when I say that we had an agreed financial strategy.

There are several councils that are not in that position for the current year because of the impact of loss of income and other costs in comparison to the level of reserves that they have and the funding that has come in. Although I am saying that I am fairly comfortable and we have a financial strategy for this year, that is not the case for all councils. We have plans to use reserves. What has changed since my August report is that there are now fiscal flexibilities. We are looking at how we can use those to deal with the impact of Covid. However, as I said, what worries me most is the next financial year and the year after, given the impact on public funding. We do not yet have a clear picture of what that will be.

Alex Rowley: Convener, it would be useful for us to ask COSLA at some point to give us a picture of the position of the 32 local authorities in the current financial year. That information will be useful when considering finances in the future.

10:00

In the submission from COSLA and the finance directors, you say that councils are

“well-placed to employ local people and, in turn, support economic recovery.”

Are councils—is COSLA—actively having discussions with the Scottish Government? Youth unemployment in Scotland will perhaps reach 100,000 by the end of this year, and we need to look at measures to guarantee people’s jobs, and apprenticeships and training. Do councils have the capacity to run those types of employment programme, given the cuts in many of the budgets from which you would build it?

Councillor Macgregor: I will touch very briefly on your previous point, about the updated position on loss of income. As you will be aware, councils have been doing a very comprehensive cost collection exercise, so we should be able to get that information to the committee fairly quickly. We have certainly been tracking and mapping where the deficits are across all 32 councils.

On economic recovery and the ability to support individuals in our communities who require that, we already have very good systems in place, and good collaborative working with third sector local organisations, Scottish Enterprise and Business Gateway. Councils are very strong in their ability to signpost individuals and give them appropriate support from employability and skills teams. As councils look at priorities and at supporting their communities, I would expect them to put in place additional measures to do that. Again, that discussion will continue with the Government, particularly on business grants, business support and, as Mark Taylor touched on, innovation and digital—that is another part of my brief that we are working on very strongly at the moment with Ben Macpherson.

There is a lot of innovation and potential in councils to support individuals. Working across sectors, we will be pivotal in our communities to ensuring that individuals get that support. Eileen Rowand might have some specific examples from Fife.

Alex Rowley: Before we go to Eileen Rowand, what I am specifically asking is whether councils are in a position to employ people directly and create training teams directly to address the unemployment tsunami that is coming our way—not just to enable others and signpost people. Are you in a position to start taking on young people?

Councillor Macgregor: Personally, I have not had a discussion with Government on schemes that we could put in place at council level. Such work may be going on in other COSLA teams so, again, I can get that information to you. I do not have knowledge of individual cases.

In the current climate, I do not imagine that councils will be in a position to employ a huge number of people or to put them into apprenticeship schemes. Certainly, if funding is available through the Government, we would look to help deliver that.

Eileen Rowand: I know that Fife Council is currently looking at the kick-start scheme for support for 16 to 24-year-olds.

I suppose that the ability to employ more people in councils comes down to the level of funding that we receive. We will already have agreed savings proposals from former years; that is balancing our budget at the moment. We have certainly had discussions in Fife on whether we need to advance those agreed savings proposals, given what is happening in the wider economy, on employment.

For me, whether we can grow our workforce will come down to the level of funding that we receive, and how the pay award compares to that. If the level of funding does not increase to the level of the pay award, for instance, our funding reduces in effect and that then reduces the number of staff that we can employ. Therefore, there is a limiting factor; councils will do all that they can, but it will be within the resource envelope that we receive.

John Mason (Glasgow Shettleston) (SNP): I will follow that up, especially with COSLA. Councillor Macgregor, in your paper and what you have said so far, there is an emphasis on local government not getting sufficient funds. As you probably know, the Scottish Government spends most of its money on the NHS or local government. Is your argument that we have been too generous to the NHS and that we have given the NHS too much money in recent years?

Councillor Macgregor: Sorry—you dropped off at the end of that sentence.

John Mason: If we have not given enough to local government, have we given too much to the NHS?

Councillor Macgregor: I am not going to pit local government against the NHS; that would be very unfair. As you are aware, health spending is also protected, so money that is designed to go to health goes to health.

As you are aware, in recent years there have been a number of large-scale policy commitments from the Government that local government has had to deliver on. The difficulty for us is that, at the

time, they had full funding, but they do not continue to have that full funding, so we have to absorb some of the base costs of those commitments, such as early learning and child care.

We need to understand the role of local government which, over the past few months, has been evidenced as pivotal in our communities—there is no question of that. We must also ensure that the priorities between local government and Scottish Government marry up. You will also be aware that we deliver on more than 60 per cent of the national performance framework. We are co-signatories on a huge amount of joint work with the Government. However, we require funding to enable us to do that work.

Further to that, local government's role in health and wellbeing is now well evidenced, and our role in social care and care at home has been touched on today. Taking that pressure away from acute services and putting it back into community services is perhaps where a realignment of funding—where the policy fits—could be more valuable than simply saying that we should give more money from the NHS to local government. Those discussions are happening with Ms Freeman and others across the Government. It is about alignment of budgets to ensure that we deliver the services that our communities require and to give us a bit of flexibility around how that service is delivered.

John Mason: When you say “alignment”, do you mean that you have taken over responsibilities, perhaps from the NHS, but the money has not gone with them?

Councillor Macgregor: There have been instances of that within integration joint boards, which have not been in existence for long, so we are still ironing out some creases. A number of years ago, through the set-aside scheme, funding was set aside for that transition from acute into community, but it has not always been recognised that the money for some of that work did not follow into the community—it stayed on the acute side. However, discussions around that are more positive than they were a couple of years ago. Eileen Rowand might be able to touch on some examples in Fife.

It is about embedding in people's minds the value that councils can give in respect of complete health and wellbeing and that the health service is more than just the NHS—alongside a lot of our third sector and charity partners, local government is part of the health service.

John Mason: I completely accept that. I was a councillor for 10 years and I am a great fan of local government. Does Ms Rowand want to come in on that point?

Eileen Rowand: Yes. I will pick up on the point about health and social care. Our ability as a council to invest in health and social care is dependent on the level of resources that come to councils. Last year, we received a flat cash settlement, so we had to fund inflation and go beyond that, which limits our ability to put funding into social care.

Funding has come through health for social care, too, but there are significant challenges in the sector to redesign and keep more people at home, which places a lot of pressure on local government to find the resources for that.

Councillor Macgregor has already picked up on the role of local government in wellbeing, and we know the importance of housing, leisure, culture and other services in ensuring wellbeing. It is about looking at the wider aspect and understanding the important role that local government plays.

John Mason: I do not want to interrupt you, but I am totally convinced of the value of local government, so neither of you needs to tell me that. I am wondering where the money is coming from. If the money is not coming from the health service, is another option council tax? I think that Comhairle Nan Eilean Siar has suggested that we remove the limit on council tax increases. Is COSLA's position that council tax should be allowed to rise by any amount?

Councillor Macgregor: I am happy to answer that question. I do not imagine that any council will want to put council tax up to a ridiculous level at the moment, as they will appreciate the pressures on households. COSLA has a long-standing position that there should be no cap on council tax whatsoever, and it should be for local councils to determine where that figure is set, based on local need. As you know, the Government has had a cap on council tax—the cap was lifted in recent years and has been fixed at 3 per cent plus inflation over the past two years. Our long-held position is that there should be no cap on council tax.

John Mason: I have one more question. My council, Glasgow City Council, feels that it is hard done by because it is bigger and has to deal with a lot of needs that other councils do not have to deal with. The folk in the north-east are always going on that the north-east is forgotten about, and the people on the islands and in rural areas have extra responsibilities, too. Is it COSLA's view that we should be looking at the allocation of funding among councils, or is COSLA happy that the present sharing of the cake is appropriate?

Councillor Macgregor: As you can imagine, distribution is always a challenge in COSLA, given the attitude of council leaders, who are all looking

after their own areas, as they should. We have had discussions about distribution recently. We are very aware that, when some allocations have been made, particularly in respect of Covid, there have been pressures on urban authorities that rural areas have not experienced quite so extremely. The distribution models that have been used to date, particularly through Covid, have very much stuck to the traditional models, but there has been some funding through education—the Deputy First Minister’s portfolio—in respect of which actual returns are being requested by the Government. That will ensure that the authorities that have experienced higher levels of pressure will receive more funding in that area.

As we go forward, distribution cannot be taken in isolation and the floor cannot be taken in isolation—it all has to be built around a strong fiscal framework. There will be discussions around how the funding is distributed. The settlement and distribution group has feisty conversations about how things are currently distributed, and probably will for some time. We need to ensure that, through other mechanisms, such as actual returns, individual local councils that are experiencing significantly higher pressures than others are appropriately recompensed.

John Mason: Does Audit Scotland have a view on the sharing of funding among councils?

Mark Taylor: The Accounts Commission is the body that is responsible for the audit of local government, and we assist it with that. In recent reports, the Accounts Commission has flagged that there is an opportunity to consider the distribution formula, but it recognises the challenges in doing so. It is about making sure that the formula is fit for purpose in the circumstances that are faced and is attached to need. To pick up on Councillor Macgregor’s last point, it is also important that that is done in the round, and alongside other aspects, such as the fiscal framework, which we have talked about, so that different aspects of local government finance are not unpicked and looked at in isolation. It is about looking at the overall package, and the Accounts Commission has been strong on that.

10:15

Dean Lockhart (Mid Scotland and Fife) (Con): Good morning, panel. I will ask about the budgets of the enterprise agencies and how they could and should be used in the context of the Covid crisis. The Scottish National Investment Bank has been allocated £500 million, and the annual budget of the other enterprise agencies is around £300 million a year. Given what we have heard about the urgent need for funding to support existing viable businesses and jobs to survive in the short term, could and should the budgets of those

enterprise agencies be prioritised to save existing viable jobs and businesses, as opposed to being used for more speculative investments in untested businesses or markets?

I will ask Audit Scotland to respond to that question first, because Mark Taylor will be aware of the investment write-downs that the Scottish Government has had to make in recent years in respect of some more speculative investments in new markets. I will also invite Councillor Macgregor and Eileen Rowand to give their views in the context of Business Gateway, and how the budgets for it should be used to help existing jobs to survive the crisis.

Mark Taylor: As the committee will understand, the first point to make is that it is not for Audit Scotland to decide and advise on priorities and policies. However, I can say a couple of things, particularly in relation to Dean Lockhart’s point about recent investment write-downs and the like.

There should be clarity around what money is trying to do, and the extent to which there has been success in doing that in individual cases should be demonstrated. We have previously reported on—and the previous Auditor General made a strong set of points around—visibility in relation to what money that is invested to support particular industries or businesses is trying to achieve and whether it is achieving that.

There is a broader point to be made about ensuring that all the spend across the enterprise agencies and all the different arms of Government is co-ordinated and joined up.

In the summer, we published a briefing paper about the impact of Covid on the public finances. One of the points that we made was about the real need for Scottish Government responses—through the enterprise agencies and elsewhere—to work alongside UK Government and local government measures. We touched earlier on support for furlough and business grants, and the activities and work that local government is doing locally to support businesses. There is a real need to co-ordinate and join all that up so that initiatives work together for an overall effect, while taking account—of course—of local circumstances and needs. I leave the committee with those two points about joining up and clarity of purpose.

Dean Lockhart: For clarification in terms of the technicalities—and not to make a value judgment on policy priority—is it right that there is nothing to stop the Scottish Government directing how the funds of the enterprise agencies and the Scottish National Investment Bank should be prioritised?

Mark Taylor: In proposing the budget in Parliament next year, the Government will need to make a judgment about where the money will go, and there are options as to where it can go across

the enterprise agencies and the SNIB. There are technicalities related to the SNIB, which is funded from a particular class of capital; there are restrictions on how that funding can be used. However, in an overall sense, that is one of the judgments that the Government—and, indeed, Parliament—will need to make on the balance of priorities and where money will go in the future.

The Convener: There is an R in the chat box from Eileen Rowand on that.

Eileen Rowand: I am sorry; that was there in relation to the last question. Mark Taylor picked up my points.

The Convener: I am sorry that I missed you.

Dean Lockhart: I will ask the same question of Councillor Macgregor and Eileen Rowand on the balance between investing to help viable existing businesses and jobs to survive in the short term, and making longer-term and more speculative investments.

Councillor Macgregor: I will defer to Eileen Rowand on that question; it is probably more appropriate for her to answer.

Eileen Rowand: To be honest, there is not a lot that I can say about that. I am perhaps not close enough to the matter to be able to comment.

However, it is important that local authorities work closely with Scottish Enterprise and Business Gateway, as has been happening even more during the pandemic. It is tricky to strike the correct balance. The focus has moved to the short term to ensure that existing businesses can still operate, although some businesses will fail. We have to get the balance right, but I cannot give you a lot of information about that.

Jackie Baillie (Dumbarton) (Lab): I want to ask Mark Taylor about the public sector consolidated accounts that are mentioned in the Audit Scotland submission. Such accounts were mentioned at least three finance secretaries ago: Audit Scotland has been pursuing that for a number of years. What is the reason for the delay? Why would those accounts be beneficial? Do you have any idea of a new date for publication?

Mark Taylor: I will start with why the accounts would be beneficial. We have touched on the overall pressures on public finance and on the impact of Covid. We all have an interest in ensuring the sustainability of the public sector and public finances.

I was involved in the initial work a number of years ago. We have long made the case that it is important to have a full picture of the accounts for all of Scotland's devolved public sector. We should look at all the aggregated figures—annualised figures and the underlying levels of debt. There

are underlying and contingent liabilities that might have to be met, and the public sector works from an underlying asset base.

It is important that such accounts be developed; the Government has agreed to that and has been working on it. The work has taken some time to do and it has taken a hit from Covid, but it is continuing behind the scenes and we are speaking to the Government about what might be possible. We continue to think that the matter is important, but we recognise the current pressure on the Government and officials. It is even more important now to have a picture of the overall public sector position, however, so we will continue to call for that.

Jackie Baillie: I could not agree more. Is there a planned timescale for that?

Mark Taylor: The safest thing for me to say is that we will get back to you with the detail. I am not sighted on current discussions. We have been talking to the Government about publishing such accounts in the coming months and will continue to engage on that.

Jackie Baillie: I have questions for Councillor Macgregor and for Eileen Rowand.

Local authorities have been at the forefront of the pandemic. A number of members have explored how much that has cost them. My understanding is that if councils did not have reserves there would be a gap of at least £100 million between what you have spent, or have forecast that you will spend, this year, and the grants that the Government has given you. If that is the case, do you expect that gap to be filled in-year? If there is no problem with that, I am interested to know whether you have forecast costs. Eileen Rowand said that the concern is about the coming year's budget. Have you forecast the on-going cost of Covid in that budget?

Councillor Macgregor: I will defer to Eileen Rowand on some elements of that question.

One key thing that councils have done is robust cost-collection exercises. Those have been repeated. We still have not done a full audit of the pressures on education and the shortfall there.

As you are probably aware, between councils and our arm's-length partners in culture and leisure there was a £400 million gap through loss of income alone. At the moment, the projection is that there will be £90 million to fill that gap. Eileen might have more up-to-date in-year figures.

The big pressures will come next year. Although councils are able to plug gaps and get through this period, at the front of our minds is that it will not be so easy to do that next year. We face a significant deficit in councils' budgets, and the lost-income scheme is focusing leaders' minds. If we cannot

plug that gap caused by loss of income and a lot of culture and leisure services are unable to get back up and running, the projections will be very difficult. Eileen will have specific examples.

Eileen Rowand: We predicted a gap of £500 million, but that was before £90 million for lost income and £49 million in consequentials came in. There has obviously been more funding since then. However, there have also been additional costs. I suggest, based on the estimates back then—they will have moved on, because this is a movable feast—that the gap is more akin to £340 million. Therefore, it is substantial.

Directors of finance are considering strategies to deal with that in-year. The ability to do so varies across councils. Gail Macgregor has already highlighted that the loss of income exercise that we did, which is being verified now, found a figure of £400 million. That includes items including capital, so we are quality assuring the figure. However, if it is compared with the £90 million that will potentially come through lost-income funding there is a significant gap. That means that councils are considering using their reserves and fiscal flexibilities.

Jackie Baillie: Okay—so there is a gap of £340 million for this year. Have you projected what the gap is likely to be for next year's budget, and have you shared that information with the Scottish Government? I ask because budget time is approaching, and a council that uses its reserves can do so only once. They will not be there to use again, so councils will face real difficulty in the next financial year.

I know that you have asked for flexibility to spread the cost of Covid over budgets so that you do not have to arrive at a settled budget in one year, but would instead be able to spread the cost over several years. Has that conversation gone well?

Eileen Rowand: The focus at present, for the information that we have consolidated across councils, has been on the current year. That is probably only because of the timing.

My council is looking at our budget assumptions for next year. We are trying to consider the legacy impact of Covid into next year and beyond, and we are obviously considering other factors that will impact on our budget and any potential budget gap that we forecast.

At this point in time, that information has not been consolidated across Scotland, but I know that COSLA is working with the Scottish Government in discussions about next year's budget. That will, through time, include the legacy impact of Covid into next year. That will be partly about looking at whether the fiscal flexibilities are enough to deal with that for this year and next

year. I am sure—based on feedback that I have had from directors of finance—that it will not.

As you said, our reserves will have been impacted this year. That will vary across councils, but there will be things that we cannot fund into next year using reserves or flexibilities, which will no doubt impact on our ability to deliver our budget.

Jackie Baillie: I will move on to the timing of the budget. From a response to Patrick Harvie, we now understand that the UK Government will announce the outcome of its spending review on 25 November. From your perspective in local government, is it better to have an indication of the budget earlier, with the understanding that for the Scottish Government things might still need to change? Is it preferable to have an idea of the range of options that might be available, or would you prefer the frenetic rush that would come with a definitive budget at the end of January or the beginning of February?

10:30

Councillor Macgregor: We reported to leaders last week and we are now getting into budget discussions with the Scottish Government. The leaders have been very clear that the earlier we get estimates or projections the better, as long as there is some form of reconciliation down the line. One of the dangers of waiting for the last-minute rush is that it does not allow directors of finance and teams within councils to plan and give certainty—or even any remote possibility of certainty—to third sector partners and organisations that we fund to deliver services within our communities. The danger of waiting for an absolute budget in March is that it does not enable councils to prepare.

At this stage of the discussion with the Government, our preference is for estimates and projections first, with reconciliation after that.

Eileen Rowand: We are trying to work on establishing what our starting point would be for local government and what a fair base would be. We are looking at last year's settlement and at the agreed Scottish Government priorities that will have additional costs this year, as well as at the Scottish Government's pay policy, including the living wage. Those discussions will take place between now and the turn of the year. It would help us enormously to have an indicative position before the formal budget. I hope that there we will be able to have that discussion and get more of a feel for what will happen.

Jackie Baillie: I agree with that.

Dr Alasdair Allan (Na h-Eileanan an Iar) (SNP): I have a question for Councillor Macgregor.

I appreciate what you have been telling us about feeling the impact of Covid and the pressures on the public sector generally. You have made your case for that funding issue to be resolved in the longer term. In the immediate term, do you support the Scottish Government proposal that capital underspend should be utilised on revenue?

Councillor Macgregor: We support that principle because we asked for it. There is a recognition in local government that, due to Covid, many projects were held in abeyance or put on the back burner for a short period, and they will probably be picked up next year. That has left an underspend in capital budgets that could be used as a one-off in this year and transferred to revenue. That would certainly help councils to plug the gap.

Dr Allan: In response to Mr Mason, you said that you did not think that it was your place to answer the question about where the Scottish Government should find extra funding. Whatever you feel about that, any rapid response to the Covid situation by the Scottish Government implies borrowing. Can you confirm COSLA's position on borrowing powers for the Scottish Government?

Councillor Macgregor: There is no COSLA position on borrowing powers for the Scottish Government—there was a motion on it several weeks ago that was not agreed to, so the leaders did not come to a position on that.

Dr Allan: Does Eileen Rowand have a view on the proposal to use capital underspend as revenue spending?

Eileen Rowand: There were four asks in relation to the fiscal flexibilities that we wanted. It started at five asks, and then there was a note of the PWLB loan interest payment holiday. We got agreement to advance three of those asks, but the one that Treasury did not agree to was flexibility to use capital grant to fund revenue. Our proposition was based on the impact of Covid on capital spend within the year. We had hoped to be able to use an element of the capital grant to fund revenue, but we have not been granted that ask. Some of the impacts of Covid are related to capital, so I would make a strong call for us to continue to push on that fourth flexibility and to make a case to ensure that it happens, because it is required.

Dr Allan: Finally, Councillor Macgregor acknowledged that there is a lot of variation in the levels of reserves that local authorities have available to them. The situation is not easy for a number of local authorities. Can you give us an indication of the range?

Councillor Macgregor: I do not have those figures in front of me, but that is another thing that

we can provide to the committee—that is not a problem.

The Convener: Before I bring in Tom Arthur, I will ask Mark Taylor to pick up on one of Alasdair Allan's questions about fiscal flexibilities. It is not just a borrowing issue; it is about the other issues that Kate Forbes has pushed on, around flexibilities for borrowing payments and tax reconciliations. Does Audit Scotland have a view on that? Would such flexibilities be helpful in the circumstances, in response to the Covid pandemic and all the turbulence and volatility that it is creating?

Mark Taylor: I start by recognising the scale of the task and the volatility, as well as the challenge for Government in managing finances against a moving target, given all the moving parts and the difficulty of operating a balanced budget in these circumstances.

As you would expect, it is difficult for Audit Scotland to get drawn into specifics when judgments and decisions are made on different aspects of the fiscal framework and the different ways in which that can be managed. I also recognise that, for example, the guarantees that the Treasury offered play in here as well. That rounded package of how all those things operate is the important aspect.

The other reflection that I would offer—I know that this is understood, but it is worth saying—is that those fiscal flexibilities, as with the ones that we have been talking about for local government, are not about additional spending power in aggregate; they move spending power across years and between years. Those two things are often conflated. Borrowing to spend more is a different thing from the sort of flexibilities that have been asked for. As part of the discussion between the Governments, there is a need to recognise the volatility that is being experienced, and whatever package of measures is discussed and agreed needs to be able to respond to that.

I will take the opportunity to make a final, related point about the 2021-22 budget. The flexibilities in the fiscal framework, particularly around the reserves, have previously been used to carry spending from one year to another. There is a question in my mind about whether, given the pressures on spending in the current year, a change of approach or mindset is needed, which the committee might want to explore, about how reserves are used specifically in these circumstances. You will be aware that carry-forwards have been a big thing for previous Governments of all complexions with regard to managing the budget. It strikes me that there is something different this year with regard to how those may or may not be used.

The Convener: Does Eileen Rowand want to comment?

Eileen Rowand: There is one point that I want to stress about fiscal flexibilities. It is great that we have that flexibility in comparison with other devolved Administrations, but such measures are there to be used as a last resort. We would not normally want to borrow or use capital moneys to fund revenue; that is no substitute for funding. However, we understand that the funding that is coming to the Scottish Government and then on to local authorities is limited. To pick up on the point that Mark Taylor made, that pushes costs back and could increase on-going revenue costs. That is why we are trying to use other means before using the fiscal flexibilities. Obviously, we are trying to survive.

Tom Arthur (Renfrewshire South) (SNP): My question is about Brexit, and I will direct it to Councillor Macgregor. I refer to paragraph 54 of the submission from COSLA and others, which refers to some of the unknown impacts. Part of it caught my eye, and I will read it out for clarity and for the benefit of the *Official Report*.

"It is already anticipated that there will be additional work required for Environmental Health and Trading Standards officers for Export Health Certificates (EHC), but the exact scale and level of input is not fully detailed yet. Environmental Health Officers for instance have been supporting Test & Protect but it is unlikely that such small teams could support both work streams."

That is clearly concerning. I read the paragraph as suggesting that Brexit may have a detrimental impact on our ability to fight the pandemic. Could Councillor Macgregor unpack that paragraph for me and outline some of the broader risks to local government finance that are associated with Brexit?

Councillor Macgregor: We have perhaps moved on since that written submission was given to the committee, in that some decisions have been made, particularly on environmental health officers. Some funding has been put forward to enable us to take on more environmental health officers, in recognition of the impact that Brexit will have, particularly around licensing and certification.

One of the challenges that we face in that respect is that council trading standards teams and environmental health officer teams have been depleted, year on year over the past decade, due to budget cuts. We cannot suddenly employ a whole load of environmental health officers if they are simply not there or have not been trained. We may now have the funding to put those people in place to assist, but the training takes three years. There are some practical problems around that. The funding is very much needed, and we are

grateful for it, but it will be incredibly challenging simply to get those people on the ground.

Between them, the impacts of Brexit and Covid will put an awful lot of pressure on the budgets of councils that have ports in their areas in particular. I think that about £1.2 million was set aside for health officers, but it is not as simple as putting money towards that; we have to go through a full training programme. We are now looking into flexibilities so that we can bring people in to assist while they are training on the job, working alongside other people in those areas. There are quite a lot of challenges there, but the situation has moved on since our submission was originally made.

Tom Arthur: Are there any other examples where Brexit could have a detrimental impact on our ability to fight the pandemic that were not contained in your submission but which have come to light since then? Are there any scenarios that you think are unlikely but possible?

Councillor Macgregor: I will defer to Eileen Rowand, who may have some specific examples from Fife.

Eileen Rowand: We know that, given the pandemic, there will be demands on social care, early learning, childcare and teachers. Depending on what happens with Brexit—we are obviously getting closer to December—there may well be a supply issue and then a demand issue. We will have to try and manage that so that we can continue to deliver our services.

We are having discussions about the issue in my council. We had an incident management team for Covid, and we now have an incident management team examining the impacts of Brexit. It is the combined impact that is concerning for us.

10:45

As Gail Macgregor highlighted, we currently need staff to have qualifications if they are to undertake certain functions, so we are considering whether parts of their roles could be done by staff without those qualifications. We are also exploring how we could use our resources more flexibly, but we are doing so at a time when there is increasing demand for those resources to provide business as usual while continuing to respond to the pandemic.

Tom Arthur: In your submission, you have given examples of situations in which members of staff might have to choose between dealing first with either Brexit issues or pandemic ones. Can you give other examples of those?

The Convener: To whom are you directing that question, Tom?

Tom Arthur: I am happy for any of the witnesses to answer it. Perhaps Councillor Macgregor could go first.

Councillor Macgregor: Eileen Rowand is probably better placed to answer that. Council staff are very adaptable. I go back to the example of the business grants scheme. Councils have been incredibly good at just picking up the bat, running with it and doing their jobs. If there are pressures between Brexit and Covid, council departments will manage that appropriately, which they are good at doing. Eileen Rowand might be able to give more examples.

Eileen Rowand: I have already given a couple of examples in social care and in early learning and childcare. If I had to go beyond those, I would look at the role of communities, which have been playing an important role in our response to the pandemic by ensuring that support is provided to vulnerable people and those who are self-isolating.

When Brexit is fully in effect, there might be more individuals who have no recourse to public funds. There could then be an increase in the number of vulnerable people in our communities, which could stretch local authorities' capacity to respond.

During the pandemic, we have demonstrated our ability to be agile and to switch our resources, but that will become more difficult as we return to business as usual, which we are doing. When two incidents involving the effects of Brexit and Covid come together, that will be challenging for local authorities, but I am sure that we will continue to endeavour to support people who require it.

Tom Arthur: Thank you very much. I have no further questions, convener.

The Convener: No other member has indicated that they would like to ask questions, so I thank our witnesses for giving us so much of their time. This has been a helpful and useful evidence-gathering exercise for the committee.

I suspend the meeting for about five minutes, to allow for a change of witnesses.

10:48

Meeting suspended.

10:53

On resuming—

The Convener: I welcome the second panel to the meeting and thank the witnesses for their written submissions. Charlotte Barbour is the director of taxation at the Institute of Chartered Accountants of Scotland and John Cullinane is the

tax policy director for the Chartered Institute of Taxation.

Murdo Fraser: I have a question about income tax. We know that the Scottish Government has to set a budget, part of which includes income tax rates. We also know that the UK budget will now not be set until the spring, so the Scottish Government will not have sight of UK income tax rates when it sets its budget. We also know that the fiscal framework protects the budget of the Scottish Government from declines in income tax revenue to a large extent, providing that those are in line with the UK average.

We do not know what the UK chancellor might do with tax rates; there might be an expectation that, in the longer run, income tax will be increased to repay borrowing, but people would be surprised, in the short term, if there were to be increases in taxation. If anything, as a disciple of Keynes, the chancellor might look to reduce tax to provide an economic stimulus.

In the light of all that, what do you want to see from the Cabinet Secretary for Finance when it comes to setting tax rates in the Scottish budget for next year?

Charlotte Barbour (Institute of Chartered Accountants of Scotland): I thank the committee for inviting us to give evidence, and I thank you for your question, Mr Fraser. It is a difficult question because, as an institute of chartered accountants, we tend to comment on operational aspects and on how policy plays out, but we do not tend to comment on rates, per se.

Having said that, as we have discussed before in the committee, one of the most important impacts is from the level of the personal allowance, which is set in the UK, because it dictates the size of the tax base and how many people fall into tax. That is a major consideration.

In the broader terms of what we would like in the forthcoming budget, business always wants certainty and consistency and to have a feeling of where we are going. I hope that your tax policy can find the balance between raising taxes, which we will obviously need for spend, as discussed in the previous evidence session, and a recognition that there will probably be a weaker base from which to raise taxes. There is a need to support the economy, because our long-term aim must be to grow the tax base—to have more taxpayers and to ensure that they are paid better—as that is the way to contribute to the desire to spend.

John Cullinane (Chartered Institute of Taxation): I broadly agree with Charlotte Barbour. As an institute, we are in the same boat: we tend to view rates as a matter of political choice, rather than a reflection of technical expertise.

I agree with Charlotte in flagging up the role of the personal allowance and the fact that it is set at Westminster. There is a concern regarding the way in which the tax system at the UK level is geared around individuals, whereas many policies on the tax credit and benefits side are, quite rightly, geared at households, as it is the wealth or poverty of households that determine how people live. There is a growing question as to whether the tendency to increase the personal allowance is well targeted—it also costs a lot of revenue—which might come to the fore after Covid.

It is difficult to translate that into what exactly the Scottish Government could do with its powers, but it is certainly the case that the impact of tax policies that are decided in Scotland can be accentuated or blunted by set-offs. In other words, you could reduce somebody's tax, but they might end up losing more in credits, which is already being seen. In making a careful balance, the Scottish Government needs to consider what, in practice, the impact will be on households, bearing in mind the automatic set-offs that will come about through the credit system, particularly for lower-paid people.

Murdo Fraser: John Cullinane's written submission refers to the land and buildings transaction tax, in which there has been a temporary reduction in Scotland, as there has been a reduction in the equivalent tax down south. Do you have any reflections on the impact of that reduction? Has it provided good value for money and achieved what was intended? Should it be extended?

John Cullinane: For at least one of the changes to LBTT—the one that gave more time to buy to people who were selling one house and buying another—I do not believe that it was an expensive policy. In that case, it was more a question of trying to be fair to the people involved.

Obviously, things have moved on since March. We now see, in Scotland and throughout the UK, that dealing with the pandemic will be more complicated than we thought. The way that we all tended to view it was that there would be an initial period of lockdown and then we would move out of it. The Scottish Government will probably need to keep that policy under review, as will the UK Government, both because of fairness and to try to stimulate the market, which become more of a concern in March.

11:00

Anecdotally, there have been a lot more signs of activity in the property market throughout the UK. Indeed, some industry bodies are lobbying at UK level for the stamp duty holiday to be extended, and they are actually giving the reason that some

practitioners might find it hard to cope with getting everything through by the time that the temporary arrangements expire.

That implies that the change has had an impact, but not necessarily that it should be continued, because you do not want to overdo it. It is quite a difficult balance to strike, and it will need watching as you go along. That goes a little bit to the process that has to be adopted. I understand that that is very difficult, in terms of how evidence based it is and how much public understanding of it there is, and also because there might be an element of fits and starts in it, as there inevitably seems to be with Covid-related measures generally.

Murdo Fraser: I ask the same question of Charlotte Barbour.

Charlotte Barbour: I sympathise with a lot of what John Cullinane has just said.

One issue with the additional dwelling supplement is that the change that was made to it because of Covid-19, around when it could be reclaimed, was much more about fairness. I do not imagine that a lot of people are affected by ADS, and it is not overly costly. The real issue with ADS is that it tends to be a really emotive tax and probably causes more grief than you would expect, relative to the importance of the amount of money that it raises and the number of people who it affects.

The other issue that one needs to be careful with is that, because LBTT is the main tax devolved to Scotland, the messaging around it is probably more taken from that. Changes to it speak more loudly than changes to stamp duty land tax in the rest of the UK can do, simply because it is one of the biggest taxes for which Scotland has full responsibility. For that reason, it needs to be handled carefully.

We have been here before with ADS, and the committee has discussed the difficulties around it.

Murdo Fraser: Thank you both very much.

Jackie Baillie: I agree with Charlotte Barbour's comment about the need for an economic stimulus. The ICAS submission talked about the degree of autonomy that the Scottish Government has with regard to non-domestic rates. I am keen to know what she thinks the impact will be of the delay in revaluation for NDR until 2023, of course with the tone date set of 2022, which is a year later than that in England and Wales.

Charlotte Barbour: Non-domestic rates are one of the main taxes that businesses find expensive and difficult and that they complain about bitterly. We have discussed all of this quite often before, and it is a difficult topic, as is council tax. Those taxes are more within the Scottish

Government's control than some of the other taxes, so perhaps there is more scope to try to address them.

A lot of the other taxes, such as the Scottish income tax, are so interwoven with the UK taxes that Scotland has only some of the levers. Change to the Scottish income tax is quite difficult because of the mechanics of the tax and because of politics, whereas with NDR, there is only the politics to contend with—"only the politics" might not be the right way to put it, but you know what I mean. It perhaps offers more scope. It has sat there for a long time.

Jackie Baillie: Could you or John Cullinane address whether the delay is likely to have a negative impact on business, and therefore on the economy?

Charlotte Barbour: There will always be winners and losers with revaluing. There is a lag, and businesses that hope to gain from the revaluing will be disappointed by any delay.

Jackie Baillie: I turn to an issue that was in both your written submissions, which is your view that a new tax policy legislative process is needed in Scotland. Indeed, I think that one of you called for a tax committee of the Finance Committee. What would you like to see and when, and how important is that?

John Cullinane: I understand that we are now getting close to the Scottish election, so, given everything else that is going on, we might have to pick up on that issue after the election. We do not want to be unrealistic in the current environment, but nevertheless we think that a new tax policy legislative process is important. As the framework is negotiated for more powers for Scotland, it is all the more important for Scotland to be seen to be managing and scrutinising well the changes to the management of the powers that it has.

The evidence from the surveys that we have undertaken is that responsibility for tax policy in Scotland is poorly understood by the Scottish taxpayer. That is not just a Scottish problem, though, as understanding of all sorts of tax matters is low throughout the UK, for various reasons. However, it is a particular problem in Scotland because of the devolved set-up. People need to be able to understand what decisions are coming from where and what the rationale is for those decisions and the context in which they were made. Effective democracy in controlling tax powers requires the best tax processes.

Jackie Baillie: Does Charlotte Barbour have anything to add?

Charlotte Barbour: When the 2012 powers came through and we set up LBTT and the Scottish landfill tax, that tax legislation was seen

as fixed stand-alone legislation. However, we have found that LBTT in particular has changed regularly because we have brought in new measures such as first-time buyer relief, the additional dwelling supplement or more mechanical changes such as changing the rates. Some changes are about seeking to amend anomalies in the legislation, because some of it is quite difficult and technical and we cannot always pick them up on day 1—for example, group relief—and some changes come from tribunals. Revenue Scotland and the Scottish Government probably have shopping lists in that regard.

There is no mechanism by which to make those changes, some of which are quite technical and complicated, so they tend to be put to one side as if they are not important. However, for my money, anything that impacts on how much a taxpayer has to pay is hugely important and should be addressed promptly. We need to have a regular process for that. The jury is out on whether it should be an annual or biannual process, but it needs to be a regular one, because otherwise it will fall by the wayside. We want to see processes that can cope with all the changes. An interesting working party was looking at that, but Covid got in the way, so it would be great if it got picked up again.

Jackie Baillie: My last question is about the timing of the budget. You will have heard that COSLA would like as much information as possible as early as possible, even if it involves estimates. Is there a preference for a flurry of activity that brings certainty over a short timescale, or is there a need to start discussing some of the options for the budget just now, even though we will not know the spending review outcome until 25 November? I ask Charlotte Barbour to answer that first.

Charlotte Barbour: I thought that that was an interesting question when you raised it with the previous panel, and I still think that it is an interesting question. It is a catch-22 situation, though, as I am not sure which option is better.

We want time to discuss the possibilities—to consider the probabilities of where things might go. However, we also need the certainty of getting through some of the processes in order to get the Scottish rate resolution—vis-à-vis the budget bill—in place at the right time. That said, discussing lots of things that you do not know about and then having to come back and revisit them seems questionable.

It is a difficult question. I am sorry that I have not answered it for you.

Jackie Baillie: It was a politician's answer. *[Laughter.]* Does John Cullinane have anything to add?

John Cullinane: I do not disagree with anything that Charlotte Barbour said. Personally, I would be inclined to go for a budget with green tinges, as it were: whatever the formalities, give as much information as you can about political intention and explain some of the parameters that you foresee that might make you have to change things. It is in the nature of things that you cannot give more certainty than is there to be given, and we have a combination of what the UK Government might do and the situation with Covid.

In one respect or another, people will have to settle for less, and they would probably appreciate some overall directional guidance to the extent that the Government can give it.

The Convener: I will press the witnesses further about what Jackie Baillie asked, around non-domestic rates. It is a good question.

I was struck by Charlotte Barbour's answer on winners and losers. Where does the balance between disadvantage and advantage lie in delaying revaluation when we consider the impact on losers of the economic turbulence that has been created by Covid-19 and Brexit together? Perhaps John Cullinane could answer first.

John Cullinane: From a long-term point of view, you should have regular evaluations in a system such as the non-domestic rates system, because if you do not, it becomes increasingly unfair. That would be good thinking.

We know that revaluations are difficult, and there has always been an expectation that a revaluation leads to more increases than reductions. We do not know whether that will hold good in the current environment, but there tends to be a lot of political pressure against revaluation; there might also be practical issues, because so much is going on. However, for the system to work better, there probably should be more regular evaluations. That would be my starting point.

However, the current situation creates a number of complexities. People do not often appreciate the evidence that a lot of the economic burden falls on landowners. The level of non-domestic rates that an occupier of property may be expected to bear will be one of the big influences on the level of rent that might be achieved in the market. Post-Covid, we will see probably more negotiations of leases and fluctuations in rents. That angle—who will bear the economic burden?—complicates the analysis in what is an unusual situation.

I am almost saying that the question is even more difficult than one might have thought, because the current situation is fluid and difficult.

Charlotte Barbour: I have nothing to add. I agree with what John Cullinane said.

John Mason: I declare that I am also a member of ICAS, but I will still ask Charlotte Barbour—*[Inaudible.]*

I will follow on from one of the points that Jackie Baillie raised. We are touching on an issue that is in both the witnesses' submissions: ICAS mentions transparency, and the Chartered Institute of Taxation mentions public awareness.

How much understanding is there about basic things, such as the Scottish budget having to be balanced so that income and expenditure match each other? On a point that has already been made, do you think that people—not just the general public, but businesspeople—understand that income tax is partly Scottish and partly UK? Do people get that?

11:15

Charlotte Barbour: Good morning, John. It is good to see you.

That is a really difficult question. As you know, I find tax very exciting, so I often try to speak to people about it, but the topic is not always much appreciated. I think that it is very poorly understood, but I guess that that is partly due to the complexities across the UK.

There are a lot of studies on the issue. For example, Deloitte did a really interesting study a few years ago that said that very few people understand tax. That study also found that the more people knew about tax, the more they supported it. In ICAS, we think that it is important that people understand what they are contributing and how the package is made up, and that it would be helpful if people knew more.

I also think that the presentation of tax by the wider range of stakeholders could perhaps be better informed. For instance, in the media, folk home in on income tax rates and very little else.

I do not think that a lot of people understand the full Scottish package, although—everything has a silver lining—I think that, through Covid-19, there has been a lot more discussion about the funding package in Scotland. For those who want to listen to it, that discussion has been a lot more out and about in the news. I think that Kate Forbes has done an excellent job in trying to tell people where the problems are. That is not necessarily about tax per se, but it helps to explain the broader package, and it would be great if people knew more about it.

John Cullinane: I think that people understand at a general level that things have to be paid for. Murdo Fraser, I think, referred to Keynesian economics earlier. The public in general assume that things have to be paid for in a much more direct sense than is possibly really the case—or that some economists argue is the case.

However, when you get below that level to anything in more detail, it becomes very difficult. People do not always have a very good understanding of what is expensive or cheap, or what is a big revenue raiser or just a tinkering change. The discussion is also very taken up by the focus of political debate at the time.

Our survey suggested that, last year, 26 per cent of people could correctly identify that income tax was a shared responsibility. That was down from the previous year. I therefore do not think that there is much understanding of the way that the devolution settlement works as regards tax. That is maybe not surprising, because it is complicated and, as I have said, the context is one of a poor understanding in the UK in general of a lot of these issues.

We start from a very low base, unfortunately. People do not learn about tax at school; many people do not even learn about it at university. Understandably, the system tries to tax most people through pay as you earn, but that leads people to almost assume that it is something that is sorted out between their employer and the Government and that they know all about them. *[Inaudible.]*—to take an interest. Some people find it very dry. The level of understanding is just not good, unfortunately.

John Mason: It concerns me quite a lot that that figure on understanding had fallen.

I realise that neither of you wants to give a political angle, but, in practical terms, have we much room for manoeuvre on tax this year? Could we raise income tax a bit? There seems to be a public desire to help the NHS and so on. In practical terms, would that be very difficult?

The Convener: I ask Charlotte Barbour to pick that up first. I see from the chat box that she wanted to come in on the previous question, so she will be able to deal with that issue, too.

Charlotte Barbour: Thank you, convener—I wanted to mention something that relates to John Mason's previous query.

One of the things that makes it quite difficult to understand taxes is the bigger macro picture. If you pay Scottish income tax, you would probably expect that to go towards health and social care, which are the main responsibilities of the Scottish Government. However, in respect of coronavirus support, income tax is tied to the furlough scheme, which comes from the UK. That kind of thing makes you wonder what relates to what. The bigger picture creates quite a lot of mismatches, and the coronavirus situation has emphasised those mismatches, which makes things more difficult.

I will definitely duck John Mason's point about the option to raise the rate of Scottish income tax, I am sorry to say.

However, I hear a lot of our members say that we need a broad package that makes Scotland attractive. Again, with the coronavirus, we are all working from home. Some of our members say that, from a tax perspective, Scotland is less attractive for people if they are going to pay more tax here when they can work from home anywhere. Members of other committees based down south say to us that Scotland has a broad, attractive package, and a lot of people might work from home here rather than down south.

I really do not know how much tax in isolation would affect things, but it is part of the broader package, and—*[Inaudible.]*—looking for us to bring more well-paid individuals into Scotland and raise tax income in that way.

John Mason: That is helpful—I will press you a little on that point. I totally accept that you are not going to suggest that we raise or do not raise taxes.

A few years ago, it was suggested that if the gap between Scotland and the UK was too wide, it would lead to behavioural change and people moving. You have said just now that people might think about that, and that it would be a factor. Do we have evidence that it is having a behavioural impact so far?

Charlotte Barbour: We do not have any hard-and-fast evidence on that. I know that a lot of people have looked for that evidence, but it is really difficult to tell. There is more to life than just tax, and it is hard to know whether tax in isolation drives people's behaviour.

The possibility of working from home makes things slightly more fluid on that front. Perhaps our concerns ought to sit with people who are in the £50,000 salary bracket, because their income tax is significantly more expensive in Scotland than it is south of the border, which might make for low-level tax planning and lead to less productivity. If someone has the choice of going to a job in Edinburgh or Newcastle, they might pick Newcastle—I do not know.

There is another factor that we may need to look at. There are probably two categories: those who live in Scotland, who may be driven to do something else by a tax policy and everything else that goes with it, and the people whom we are looking to try to bring into Scotland, in which case we want to make it attractive.

John Mason: That was my last question, unless John Cullinane wants to come back in.

John Cullinane: To be frank, it is very hard to get evidence on the behavioural effects. We know

that there are behavioural effects, but we do not know the extent of them.

There was evidence—or a lot of debate, anyway—coming out of what happened when the UK-wide top rate of 50 per cent for income tax was in force, but much of that evidence was about what people were doing in trying to accelerate income or delay expenditure when it came in, and doing the opposite when it went out. It is hard to translate that and say that there is hard-and-fast evidence of what the impact would have been at an on-going level.

To go back to the original point, it is clear that the room for manoeuvre is very tight in the short term because of the way that the UK and Scottish decisions interact. One example is what the UK Government does with national insurance; it tends to gear that to mesh in with the levels of income tax in England rather than in Scotland. We have already mentioned benefits and so on at the lower-income end.

One is almost in a position of guessing what the other party will do or reacting quickly to what it does. Given how the Barnett formula works, you sometimes get help from that as well as hindrances but, overall, there is a kind of uncertainty caused by the interaction. You need to bear in mind the net effect of what you are doing and what the UK Government does, and how far you have taken your objectives forward. There are probably lessons to be learned in renegotiating the framework, but that is not an immediate thing by any means. It is a difficult situation.

Alex Rowley: I return to the subject of non-domestic rates. Is any work being done to examine the most recent revaluation? My understanding is that appeals are still on-going. I have dealt directly with a number of businesses that did not qualify for certain grants because of a revaluation of the rateable value, even though an appeal was still on-going.

Has any evaluation been done around all that? Is there confidence in the valuation system? To what extent are there still outstanding appeals?

John Cullinane: I do not know about hard evidence but I understand, anecdotally, that some appeals are going on.

There is a trade-off. Few people would say that the non-domestic rates system is the ideal way to raise tax, but it is the system that we have. It is nothing like a land value tax, which many economists favour. It gets to land values imperfectly—it is a highly imperfect tax—but more closely than many other taxes. For the system to work, it probably needs regular evaluations and the longer you leave it, the more grief there will be every time there is one. It is difficult to get it right.

Alex Rowley: You have made the general point about people having a greater understanding of taxation. My experience of dealing with appeals was that businesses were pulling their hair out trying get a clear explanation of how the valuation was arrived at. If you do not really have confidence in the system and if the most recent revaluation was a bit of a sham, with masses of appeals still going on, to proceed with the next valuation seems difficult.

The previous panel, and certainly the local government representatives, want two local taxes. They want the 3 per cent cap to be lifted, and they would like to get control over non-domestic rates and set the rate at the local level. Do you have any views on that? Would that mean a more democratic system? It would certainly be local. Do you think that that would result in the council tax system being even more discredited than it currently is?

John Cullinane: My views are a little bit coloured by experience in England, so my apologies if there are differences that I do not fully appreciate.

There is probably an issue around the fact that, because business rates are administered by local authorities and because of the structure that has always been there, the business rates system—in particular, the mechanics of the system, such as appeal rights and the other processes that are normally applied to a tax system—has not been updated. Business rates have not always been run like modern taxes, and there is a kind of trade-off there.

That is a different issue, however, from whether there is local autonomy in setting the rates; that is just about the mechanics. Sometimes the availability and extent of reliefs is different in different local authority areas, both in theory and in practice, and they can be interpreted differently. There is an issue around the mechanics and the application of some of the procedures that we apply to taxes more generally.

11:30

Charlotte Barbour: On council tax and the question whether it should be spent locally, we enter the same conversations that we have on councils and locality. If it is a local tax, it should be raised locally; on the other hand, what happens where there is a relatively poor area that needs more funding and cannot afford to raise it? Do we need redistribution within that? All the arguments that sit at that level are similar to the Scotland versus the UK situation with regard to how the communal aspects of tax collection and paying for communal services are balanced out. It is a difficult issue to balance.

Dean Lockhart: I come back to the discussion about protecting—and, it is to be hoped, expanding—Scotland’s tax base, and how, in particular, the budgets of the enterprise agencies can best be used for that purpose. What technical advice would the witnesses give on whether, during the Covid crisis, in the short term, the enterprise agencies should prioritise their spend on saving viable businesses and, by extension, existing jobs, as opposed to investing in more speculative new markets or new projects?

Charlotte Barbour: That is a difficult question, and I am not sure that the situation deserves simply one approach or the other. To a large extent, we are looking at the viability of all businesses, are we not? If we focus only on existing businesses, given that some of them are struck with Covid difficulties and might yet have some Brexit difficulties, who knows whether they will be viable, and whether they deserve money to keep them going and that they will then be viable again? Do we become a bit stagnant if we never look to the future? There needs to be a balance between the two. We always need to look at new industries to support them and to bring in innovation. It probably comes back to having an analysis of each business and putting proper resources into evaluating whether to support it or not, rather than a blanket approach of this or that.

Dean Lockhart: I appreciate that. However, in the context of limited resources and looking at the tax base, if the analysis shows that an existing business is viable, is it not a case of a bird in the hand being worth two in the bush when budgets are limited? If you must choose, perhaps the safer option would be the viable business.

Charlotte Barbour: You could make the argument either way. We have been looking closely at an approach of attracting individuals rather than business to broaden the tax base. There is a lot to be said for bringing working people into Scotland to create more individual Scottish taxpayers. Perhaps the focus should be on individuals, because it is Scottish income tax that we are looking for, if nothing else. Coming out of Covid-19, there might be more scope for people to work from home, so you could be working for an English business but working from home in Scotland. If those are well-paid jobs, that would help to broaden the tax base.

Dean Lockhart: John Cullinane, I would like to hear your views on those issues.

John Cullinane: I do not know whether our members are well placed in terms of expertise on the first issue about the spending side and how to spend limited budgets. I can certainly see the argument that, in a pandemic, it becomes a question of keeping what you have going, and, frankly, we just have to operate with less certainty

about what might be viable in future. It is not an area in which we have a great deal of expertise, to be frank.

On the point that Charlotte Barbour made, I agree that it is likely that the current situation will give rise to a great deal more potential for people to work from home. In turn, that has a lot of potential to affect taxing rights, which would affect the UK in general and Scotland within the UK.

For example, in the financial sector, which tends to involve highly paid jobs and bring in a lot of tax revenue, people are still predominantly working from home. That has been the case throughout the pandemic, and I am not sure that it will ever go back to how it was.

If people choose to work from home and are able to work from all over the place, that could have a big effect on taxing rights, and there could be a problem of leakage for the UK. That could give rise to swings and roundabouts, and one cannot over-generalise, but it is a big issue that all fiscal authorities will need to look at as soon as they can draw breath, as it were, from their current preoccupations.

Dean Lockhart: I have a brief follow-up on that point. It is fascinating that you say that the trend of working at home might impact taxing rights. Are the existing rules of residence regarding where someone is a tax resident, whether that is in Scotland, the rest of the UK or elsewhere, fit for purpose in this new environment? Do they need to be updated? What might be the practical outcome for the Scottish income tax base if there is a semi-permanent move to people working from home?

John Cullinane: It is too early to start using expressions like “fit for purpose”, but it is clearly an issue that will need to be reviewed.

The definition of a Scottish taxpayer is already a little bit different from the normal definition between different countries. It depends a lot on individual tax treaties, the interaction of national rules and treaties and so on. The current situation will certainly lead people to be a lot freer to choose where they are taxed than would have been the case prior to the virus. Even though we now know that it is physically possible to work differently, most employers would have assumed and expected that staff would turn up in the office as a base most days. The new situation will create more flexibility for people and it is bound to be something that Governments look at, but it is very difficult to see right now exactly how that will go.

Dean Lockhart: That is very interesting; thank you both.

Those are all my questions, convener.

The Convener: We come to Alexander Burnett. I apologise, Alexander—I have just noticed that it

is the first time all morning that you have had a chance to ask a question, and we are well down the question paper. I should have noticed that and got you in a bit earlier—forgive me.

Alexander Burnett (Aberdeenshire West) (Con): That is absolutely fine, convener. I have two questions, if that will make up for it. The first is Covid related and follows on directly from what John Cullinane said about definitions.

Many types of support, and the eligibility for that support, have been tied to financial and tax definitions: tax reporting points; furlough; payroll data, where people are on payrolls and the like; definitions of turnover; whether people have a business bank account; and general classification of types of business. I hope that there will be a more formal investigation into those matters, but I wonder whether you can see any potential changes around some of the definitions and timings, and how things are reported, that might improve how support is given in future.

Charlotte Barbour: That is an interesting question. We have learned such a lot in the past six to nine months about the tax system and how it works or does not work, and HMRC has done an amazing job in producing the furlough and self-employed schemes.

The self-employed scheme is quite difficult, and a lot of the issues that have crept in there relate to definitions; I am not sure exactly how one addresses them. The schemes have highlighted issues around national insurance, who pays for what and what people get back out of the system. One of the learning points from all that is that, broadly, the furlough scheme has worked well in targeting people and getting support to them. That has come from having up-to-date, real-time information in the PAYE system.

It points strongly to HMRC striking on with the making tax digital programme for the self-employed, because the issues that have come out for the self-employed are partly around what you are trying to replace, which is profits rather than, say, a turnover or a salary. There are difficulties there, but there are also difficulties with trying to base up-to-date support on ancient information. I appreciate that there have also been difficulties for those who have fallen between the two schemes, which is probably a problem that sits with the UK Government.

To go back to one of the things I said earlier, what is quite interesting is the mismatch between Scottish income tax being paid into Scotland for what I guess would be Scottish expenditure, and furlough, which comes directly from the UK. That probably highlights some of the difficulties in the devolution package.

John Cullinane: I agree. The thing about the furlough scheme and the other schemes was that they had to be introduced at incredible speed, so it was inevitable that the existing agencies, definitions, data and whatnot would be used. It remains an impressive achievement that HMRC managed to do so much in such a short space of time—it did particularly well in that.

Some issues are not about data, though; they are just decisions about crude cut-offs. For example, there is the issue of people being unable to get help under the self-employed scheme unless, historically, more than half of their income comes from self-employment. That is understandable—you want to help the people who rely on their business and not necessarily people for whom their business is a bit of a sideline. However, that is a crude measure.

In terms of who has fallen down the cracks, there will be a mixture of cracks, as it were. There are cracks that are very hard to deal with even now, because you do not have the data and do not know who people are. There is already some concern about fraud, which, again, was inevitable with the speed. Those things are very difficult, whereas other things are just crude rules. The longer this situation goes on—regrettable as that is—the more scope there is to look at some of those crude rules and plan for some of those gaps to be filled. There are some intrinsic difficulties, though, so it is unlikely to ever be perfect.

Alexander Burnett: If I can come to John Cullinane first for my second question, you have touched on the fact that people's understanding of tax and financial matters is not very good and, unfortunately, is diminishing. In paragraph 3.5 of your submission, you highlight the concern, which you have raised before, that there is a growing deficiency in people's understanding of tax and financial issues. You have talked about the solution. Without being too frivolous, if you were First Minister for a day, what would you do to educate Scotland on those issues?

John Cullinane: That is precisely one of the problems. If you are the First Minister, or indeed one of the other actors on the scene, you have all sorts of other preoccupations. You have to deal with all these issues and get things done, based on the state that people are in. You cannot be a kind of world educator. Frankly, there could almost be a political cost to going out of your way to be the one who just sits there saying, "I'm going to enlighten you", and not fighting your corner.

Drawing on the earlier discussion on the budget, one solution could be to point out the limits to giving any kind of certainty and to achieving objectives through the tax system. If you described how far one can make firm decisions at this stage and what some of the factors are that might

require the tax system to be altered later in the year, it would give people a bit of a flavour of what the interactions are. I cannot say it any better than that, I am afraid.

Charlotte Barbour: ICAS has called for efforts to try to broaden understanding. In fairness, I think that the Scottish Government was working on a project for a kind of communications package when Covid-19 came along. Hopefully, that one will be picked up again, because it is a really good project, and various parties have been asked to contribute to it. Again, part of the messaging needs to be that all the interested parties in tax and public funding should act, contribute and get involved in that.

11:45

In addition, I guess that tax needs a more positive messaging. In past years, there has been a lot of noise about anti-avoidance, which I understand—some people avoid taxes; not everybody wants to pay them—but there should be stronger messaging about the need for everybody to contribute. Perhaps Covid-19 illustrates that, if we want to support people, we all need to contribute, so now might be a good time to message that.

We also need to discuss the trade-offs. You cannot always hold down rates and expect to spend more, for example. If people want more to be spent on them, maybe the rates need to go up. That issue needs a broader discussion.

Alexander Burnett: Thank you very much. I have no more questions, convener.

The Convener: Finally, we come to Alasdair Allan.

Dr Allan: Ms Barbour quite rightly mentioned the need to grow the tax base after this difficult time. Conversely, is there an adequate estimation of the impact of the pandemic on the tax take, and, in turn, the consequences of that for public services? I am curious to know whether you think that there is enough information in the system about that.

Charlotte Barbour: That is a difficult one. I know that you have had evidence sessions in the past about the difficulty of knowing exactly how forecasts will pan out. Obviously, income tax is the biggest source of revenue coming into the Scottish Government, and getting back those returns takes the most time. The area with the biggest fluctuations is the self-employed. Again, those returns take the longest to get the reconciliation done fully.

I do not think that a lot of work is done on the detail of tax. You might be better asking the Scottish Fiscal Commission and HMRC about that

issue, because they will have the real-time data coming in.

Dr Allan: Do you have a view, Mr Cullinane?

John Cullinane: The only other point that I would make is to echo what Charlotte Barbour said earlier about making tax digital. Obviously, the system whereby people pay their taxes generates the data. The more digitalisation that you can get into the system, the more hope there is for more reliable data coming out earlier, particularly on the self-employed side, as it takes longer; there is more of a time lag. That is the way it is at the moment; it is a slow burn.

Dr Allan: I am also keen to ask you both about the Institute for Fiscal Studies questioning whether aspects of the Barnett formula are nimble enough to cope with an emergency such as the one that we are all living through. I take it that it was referring to borrowing. I will not ask you to recommend any solutions, including political ones, on borrowing powers, but do you recognise the problem that is being outlined?

Charlotte Barbour: The IFS has been doing interesting work. If you look at our written submission, you will see that one of our concerns is that there are so many moving parts. The Barnett formula is the baseline, then you have block grant adjustments, consequential, tax and spend. It is all quite difficult to put that lot together. Covid shows all those gritty bits and how they do and do not fit together.

The other interesting thing about the Barnett formula is that it is designed around spending, whereas all the adjustments that come through are designed around tax take, and it is not always easy to get that bit sorted out in your mind.

You have to start somewhere, and everybody is agreed that the Barnett formula is as good a baseline as any. However, the way in which it is adjusted perhaps does not help public understanding—or even my understanding.

John Cullinane: I guess that I am in the same boat. Even six months ago, I probably had the view that, frankly, the baseline was probably reasonably favourable to Scotland so, even though there were swings and roundabouts, and uncertainties caused, why would you want to alter that base? That might still remain the case, but the Covid situation throws up more difficulties.

The difficulties are not even necessarily with the formula—they occur with any scheme of devolution or with different levels of Government generally. How do you draw a sensible line? In the past, we have pointed to the example of an unincorporated business person in Scotland having to pay Scottish income tax but an incorporated business person having to pay UK

corporation tax and dividend tax. I note that people might decide to incorporate relatively easier for a whole host of reasons.

Those are technical tax differences. However, Scotland has control over health measures and the extent of lockdown and so on, but some of the financial aspects that are needed to go with that to support people is something different. That is not really anybody's fault; that is not something that anybody foresaw. It is just difficult to say where you draw the line and what the right way is to go about compensating one party or the other for decisions that are legitimately made differently—those are different sides of the line. Covid has thrown into focus what a difficult thing that is to achieve. Again, I do not have any instant answers, but I think that Covid will colour the extent to which that issue is looked at in the future.

The Convener: I do not see any more Rs in the chat bar, so no member wants to contribute further. I thank Charlotte Barbour and John Cullinane for giving us their time today and for their evidence, for which we are grateful.

11:51

Meeting continued in private until 12:20.

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