FINANCE COMMITTEE

Tuesday 24 February 2009

Session 3

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FINANCE COMMITTEE
5th Meeting 2009, Session 3

CONVENER

*Andrew Welsh (Angus) (SNP)

DEPUTY CONVENER

Jackie Baillie (Dumbarton) (Lab)

COMMITTEE MEMBERS

*Derek Brownlee (South of Scotland) (Con)
*Linda Fabiani (Central Scotland) (SNP)
*Joe FitzPatrick (Dundee West) (SNP)
*James Kelly (Glasgow Rutherglen) (Lab)
*Jeremy Purvis (Tweeddale, Ettrick and Lauderdale) (LD)
*David Whitton (Strathkelvin and Bearsden) (Lab)

COMMITTEE SUBSTITUTES

Murdo Fraser (Mid Scotland and Fife) (Con)
*Lewis Macdonald (Aberdeen Central) (Lab)
Liam McArthur (Orkney) (LD)

*attended

THE FOLLOWING GAVE EVIDENCE:

John Swinney (Cabinet Secretary for Finance and Sustainable Growth
John Williams (Scottish Government Finance Directorate)

CLERK TO THE COMMITTEE

Mark Brough

SENIOR ASSISTANT CLERK

Lewis McNaughton

ASSISTANT CLERK

Allan Campbell

LOCATION

Committee Room 1

Scottish Parliament

Finance Committee

Tuesday 24 February 2009

[THE CONVENER *opened the meeting at 14:00*]

Interests

The Convener (Andrew Welsh): Good afternoon. Welcome to the fifth meeting in 2009 of the Finance Committee in the third session of the Scottish Parliament. I ask everyone present to turn off mobile phones and pagers. I welcome Lewis Macdonald, who is here today as a substitute for Jackie Baillie.

All members will be aware that Alex Neil recently resigned from the committee. I thank him for his contribution to the committee's work and wish him well in his new ministerial role. Replacing him is Linda Fabiani, whom I welcome to the committee. As this is her first meeting, I ask her to declare any interests that are relevant to the committee's remit.

Linda Fabiani (Central Scotland) (SNP): I have no interests to declare.

Decisions on Taking Business in Private

14:01

The Convener: The next item on today's agenda is a decision on whether to take in private item 5, which is consideration of our plans for strategic scrutiny of the 2010-11 budget and involves discussion of individual witnesses. I recommend that we take the item in private. Is that agreed?

Members *indicated agreement*.

The Convener: I also invite members to discuss in private at a future meeting the evidence on public sector pay that we have heard to date. Is that agreed?

Members *indicated agreement*.

Subordinate Legislation

Budget (Scotland) Acts 2007 and 2008 Amendment Order 2009 (Draft)

14:01

The Convener: The next item on today's agenda is consideration of the Scottish statutory instrument that provides for the spring revision of the 2008-09 budget. The draft Budget (Scotland) Acts 2007 and 2008 Amendment Order 2009 is subject to the affirmative procedure, which means that the Parliament must approve the instrument before it can be made and come into force. We have before us a motion in the name of the Cabinet Secretary for Finance and Sustainable Growth, John Swinney, which invites the committee to recommend to Parliament that the draft instrument be approved.

Before we debate the motion, we will hear evidence to clarify technical matters and to explain detail while officials are at the table—officials cannot participate in debate once the motion has been moved. Members will be aware that the Subordinate Legislation Committee has already considered the instrument: an extract from its ninth report of 2009 is included in the papers for today's meeting.

I welcome to the committee John Swinney MSP, the Cabinet Secretary for Finance and Sustainable Growth; John Williams, head of finance co-ordination in the Scottish Government; and Stuart Dickson, who is also from finance co-ordination. I invite the cabinet secretary to make an opening statement explaining the instrument.

The Cabinet Secretary for Finance and Sustainable Growth (John Swinney): Today's spring budget revision is the last opportunity for us to amend the budgets for the current financial year and to include a number of transfers between budget lines to align them with predicted spending for the rest of the year.

Table 1.3 on page 4 of the supporting document shows the latest budget, which was agreed in the autumn budget revision, and the changes that are sought in the spring budget revision. Although the table suggests an increase of £1.9 billion, most of that is due to a technical adjustment for national insurance contributions, about which I will say more later. Table 1.4 on page 5 shows the changes by type.

I will draw the committee's attention to a few of the major points in the spring budget revision. The changes that are proposed will result in an increase in the approved budget of approximately £1,901 million, from £31.101 billion to £33.003 billion. By far the largest part of the increase is accounted for by the £1,880 million technical change in the presentation of income from national insurance contributions. Following discussions with Audit Scotland, those resources will no longer be shown as a source of income in the health and wellbeing portfolio; instead, they will be shown as part of the funding total for the Scottish Government as a whole, as detailed below table 1.7 on page 7 of the document. The revised presentation is in line with the draft budget and the consolidated accounts and is part of our continuing efforts to ensure consistency in the presentation of financial information in all our budget documents and accounts. The committee will note, however, that we have revisited the Budget (Scotland) Act 2007 to make a similar change for the purpose of a previous-year comparison in the consolidated accounts.

There is also a technical change to the Scottish Water cost of capital that shows a reduction of £150 million. In 2007-08, Her Majesty's Treasury changed the methodology for reporting Scottish Water's cost of capital, which gave rise to a much higher cost-of-capital charge, and a departmental expenditure limit budget of £239.9 million was originally set for 2008-09, with HM Treasury providing the necessary additional cover. In accordance with the requirements of the financial reporting manual, the cost-of-capital calculation for the consolidated accounts remains unchanged at an estimated £90 million, which is in line with budgets that were set in the previous two years.

The reduction of £150 million reflects the requirement to align the budget that has been approved by Parliament with the consolidated accounts. There remains an issue of misalignment between budget and accounts, but it has no impact on the resources that are available to Scottish Water or the Scottish Government and is, in fact, a direct reverse of what happened on the national insurance treatment to which I referred a moment ago.

Other specific adjustments include annually managed expenditure adjustments of £96.8 million across portfolios to reflect revised estimates for the cost of capital for roads of £22 million, health impairments of £18.8 million and student loans of £56 million. HM Treasury provides full budget cover for those increases.

Members will see that table 1.4 of the spring budget revision document includes £83.6 million over and above those technical adjustments. That reflects more than £53 million of accelerated capital spend for roads, rail, enterprise, housing, the school estate and the Scottish Funding Council. We have taken the opportunity to make early repayment of £25 million of debt held by Strathclyde Passenger Transport, which will enable us for the next eight years to make recurring interest savings of around £2.5 million per annum, and will create headroom for additional departmental expenditure limits spending across the portfolio.

What appears to be a net transfer from within the Scottish block of minus £8.6 million mainly reflects the transfer of budget provision to support non-departmental public body capital charges, primarily in relation to the Scottish Police Services Authority. The committee will recall that, under current budget arrangements, NDPB budgets must be presented for parliamentary approval in simple cash terms. Details of their non-cash costs are provided in table 1.2 on page 3 of the budget revision document.

Scottish Government officials sent details on all significant changes in the revision to the committee prior to this meeting. Further information on the miscellaneous minor items can be supplied, if the committee requires it. I will conclude my remarks there, and am happy to answer the committee's questions.

The Convener: I thank the cabinet secretary for that clarification. I will start with a general question. We are all aware of the tightness of budgets in the present economic crisis, but given the increasing problems caused by the economic downturn and the current reduction in inflationary pressures, can you tell us how much current expenditure has been critically examined to free up resources to allow a greater response to the economic crisis? In other words, how much scope is there to squeeze out extra resources to address the current situation?

John Swinney: I will make two points in response to that question. First, the Cabinet started a process last summer whereby we re-examined all aspects of public expenditure to determine whether it was appropriately focused on having a sufficient impact on the economic situation that we face. We continually look at expenditure from that perspective to ensure that spending in individual programmes and areas of activity is undertaken with maximum effect in terms of economic recovery.

My second point is that in all portfolios the general approach—it is insisted on by ministers in all areas of Government activity, both in central Government and in the agencies that act on our behalf—is now that we must examine whether expenditure is justified in the current economic climate, and identify whether resources could be deployed alternatively with greater impact. That process is on-going in Government and is part of the routine business of ensuring that we are properly taking every opportunity to address the severity of the economic situation that we face.

There are, of course, two caveats to that. First, all that work must take place within a fixed departmental expenditure limit that cannot be breached. The approach that has been taken in the spring budget revision has been to ensure that we deliver financial performance within the DEL. Secondly, we must work within the powers of the Scottish Parliament.

The Convener: Thank you. I invite questions from members.

James Kelly (Glasgow Rutherglen) (Lab): I have a couple of technical questions on the cost-of-capital calculations. You said that the Scottish Water total has gone down by £150 million because of changes in capital charges. Has that £150 million in effect been returned to the Treasury?

John Swinney: The figure has absolutely no meaningful cash equivalent; it is purely and simply about the rules governing the treatment of the cost of capital. The Government must ensure that we spend within our departmental expenditure limit. Beyond that, there will be a multiplicity of different accounting treatments of different aspects of the work of Government, including the cost of capital. Those are technical processes that we follow in response to changes that are directed by Her Majesty's Treasury. They have no practical effect on the ability to spend in that respect.

James Kelly: I accept that. I am just trying to understand where the other side of the entry is. There is a £150 million reduction. Where is that £150 million going? I accept what you say about its being an accounting adjustment, but I do not fully understand—

John Swinney: Perhaps I did not answer the question properly. The other side of the equation is in the Treasury's books.

James Kelly: Thank you. That is absolutely clear. In the roads budget, there was an increase of £22 million in the cost of capital. What resulted in that increase?

John Swinney: An annual assessment—maybe more frequent—will be undertaken of the value of the trunk-road infrastructure for which the Scottish Government is responsible. A cost-of-capital figure is derived from that estimate, and that is provided for through annually managed expenditure that is in a different category from the expenditure that I control directly. That provision comes from the Treasury as part of the financial arrangements under which we operate.

James Kelly: So, in effect, it is a methodology—

John Swinney: It is a methodology. A computer programme calculates road length, road conditions and the various other imponderables that are involved. At the end of that, a number comes out—if only it were as simple as that—which forms the basis on which the cost of capital for roads is calculated.

James Kelly: Okay. Thanks a lot for that. Finally, on European structural funding, can you give detail on what the £17 million is going to be spent on?

John Swinney: I wish that it were going to be spent on something more productive than what I fear it will be spent on. Essentially, the Government is, as I feel is prudent at this stage in the financial year, making provision to deal with the settlement of outstanding financial issues related to European regional development fund programmes from 1994 to 1999. The European Commission has expressed concerns about appropriate application of some funds that were spent during that period. The matter has been hotly contested for some considerable time, but we are reaching a point at which the issue will need to be resolved and settled with the Commission, so we are making provision for that in the accounts. Discussions are still under way, so I am unable to give the committee a final position on where we will end up with the negotiations. However, I will be happy to provide the committee with an update when the discussions are complete.

14:15

James Kelly: Are you able to say how many projects that will affect?

John Swinney: I do not have that information in front of me today, but I will be happy to provide it. From recollection, I think the number was not significant.

The Convener: Is £17 million the overall amount that is involved?

John Swinney: It might well not be £17 million. Obviously, a process of negotiation is under way to try to avoid the need to provide £17 million, but that provision has been made. The Government is taking a step that we think is appropriate at this stage, based on discussions on that expenditure that have gone on for some time.

Lewis Macdonald (Aberdeen Central) (Lab): If I heard the cabinet secretary aright, he mentioned an adjustment to the Scottish Police Services Authority's capital budget. What is the nature of that adjustment and what are the reasons for its being made at this stage? Presumably, the adjustment relates to the SPSA's building programme.

John Swinney: Essentially, the changes reflect a classification change to take into account the fact that the SPSA operates as a non-departmental public body. The changes relate to the non-cash budget and the capital budget of the SPSA. None of it alters the SPSA's overall ability to spend.

Lewis Macdonald: Given that the SPSA was an NDPB before now, is there a particular reason why the adjustment has been made at this stage rather than earlier in the financial year?

John Swinney: I suspect that we are merely catching up by putting in place for the first time those arrangements for the SPSA within the Government's accounts.

Lewis Macdonald: My other question is on the virement between portfolios that appears in the enterprise, industrial affairs and tourism budget, which gains an additional £6.1 million. Is that real money, or is it simply a technical adjustment? If it is real money, what is the money intended to address?

John Swinney: The money provides support for the roll-out of the pathfinder broadband initiative in the Highlands and Islands, where work is still under way. The objective is to conclude that initiative by the summer of 2009. The Government is putting in place provision for commitments that were made by the previous Administration on that project, which continues to be rolled out across the Highlands and Islands.

Lewis Macdonald: So, it is in response to demand.

John Swinney: That is correct.

The Convener: Are there any other questions?

Jeremy Purvis (Tweeddale, Ettrick and Lauderdale) (LD): I want to follow up on James Kelly's questions about Scottish Water. Am I right to understand that the information that appears in the Scottish budget is required to be clear about the money that the Scottish Government lends to Scottish Water and the repayment that Scottish Water makes for interest charges? Is the £161.9 million the amount that the Scottish Government is lending to Scottish Water? Is £89.9 million the amount that the Scottish Government is receiving back in interest payments from Scottish Water?

John Swinney: I would not characterise cost-of-capital charges in that fashion, Mr Purvis. The £161.9 million will be identified clearly as the Government's contribution to, and support for, Scottish Water's borrowing. Essentially, the presentation in the consolidated accounts is different to that in the budget document. My point was on the reversal of the situation for national insurance contributions: the budget document and accounts are now aligned in that respect, in what I would describe as a neutral fashion.

As a consequence of the decision on the classification of Scottish Water, a misalignment has arisen in the presentation in the accounts and the budget document. Things will not be set out as clearly as is the case with national insurance contributions.

Jeremy Purvis: Perhaps the Government will come back to the committee on that. Any constituent who reads about this may end up thinking that the £160 million that the Government is lending to Scottish Water is being lent on quite expensive terms.

John Swinney: I could not agree with Mr Purvis more on the difficulties that arise from presentation of all this. I assure the committee that we are working to try to harmonise and synchronise the presentation of information in the budget document and the consolidated accounts—the aim is to have a clear follow-through. That said, the accounting rules often thwart us in our efforts. If a more detailed explanation would help the committee, I would be happy to provide it in writing.

Jeremy Purvis: Thank you.

I turn to the £150 million that the Treasury will now have on its books for capital cover. Does the Scottish Government have at its disposal in its DEL the same amount to offer capital cover on devolved capital expenditure? Does the Scottish Government have £150 million of capital cover that it can now redeploy?

John Williams (Scottish Government Finance Directorate): We are talking not about capital but about the cost of capital—

Jeremy Purvis: Yes, but I think that the cabinet secretary said that the cover of the capital is now on the books.

John Williams: This is about the capital charges that result from the calculations on the assets that are now on balance sheet. If it is any consolation to the committee, I think the Treasury has it in mind to remove the whole notion of the cost of capital. All it seems to have done is confuse everybody. It has not achieved the original intention, which was better asset management. The idea was that putting a charge on assets would encourage people to manage them better in order to reduce charges. In practice, that has not materialised and we have simply been left with the notion of the cost of capital, which is not part of the UK's generally accepted accounting practice or of the international financial reporting standards. The difference has arisen in that way.

The Treasury asked for the costs of Scottish Water's capital borrowing to be calculated in a way that led to the figure of £150 million, which is more than the £89 million that is shown in the document. However, Audit Scotland insisted that the cost of capital in the accounts be calculated on the basis that has been used in the past. When we do our returns to the Treasury at the year end, we will have to make them on the basis of the calculation at the higher figure. No budget provision will be freed up as a result of that, however. The Treasury has simply covered the cost of doing the calculation in a different way. It is all non-cash; it gives no ability to spend capital.

Jeremy Purvis: I understand that the process began at the Treasury. Nevertheless, within the budget document, if the amount is part of the DEL limit and if £150 million has in effect been removed from that limit, you still have the same DEL limit, do you not?

John Williams: That amount is removed from the parliamentary approval process. The consolidated accounts for the Government need to be comparable before they can be approved by the Parliament. That said, the £150 million remains part of our DEL. It will be taken up by doing the calculation on the basis that the Treasury requires when making our return at the year end.

John Swinney: If I understand him correctly, the key point that Mr Purvis is trying to get at is whether any new capacity for capital cover is created. The answer is no.

Jeremy Purvis: Thank you. I noticed in the Scottish Government's brief guide to the budget revision that there is a virement of £28.4 million from rural affairs, but I am not clear where it is going.

John Swinney: It is going to a number of different places in the other portfolios, although it is difficult to give a precise pound-for-pound reallocation, because other sums of money are coming into the budget through accelerated capital and various other factors. It has been reallocated to other areas of Government expenditure, which are set out in the budget document.

Jeremy Purvis: It was helpful that the brief guide stated where the transfer of £16.7 million to local government was going to. It also stated that there was £600,000 for a pilot on food-waste collection. However, there is no other detail on the £28.4 million, which is a not insubstantial sum of money. Could you come back to the committee with more detail on that?

John Swinney: We can—although the changes that have been made as a consequence of the spring budget revision are all set out in the spring budget revision document. The virement that is going on between different parts of the Scottish Government's expenditure is essentially a zero-sum game.

Jeremy Purvis: I have a question on the additional capital that the Government has been able to accelerate. The brief guide notes that

"An additional £20.2m of capital was accelerated following further discussions with HM Treasury."

Is the town centre regeneration fund that you announced during the budget process related to the accelerated capital in the budget revision?

John Swinney: It is not. The town centre regeneration fund is expenditure in 2009-10, so there is no impact on the 2008-09 budget. The £20.2 million to which you refer is our proportion of the accelerated capital expenditure that the United Kingdom Government approved to accelerate affordable housing provision in England in, I think, September last year. You will recall that the Scottish Government had decided to accelerate affordable housing spending in August last year. After the UK Government's decision, we made representations to have the consequential on the decision that it took on the expenditure in England in September applied to our budget and were successful in those representations. In effect, that means that the £20.2 million comes into 2008-09 and the figure in 2009-10 is about £67 million.

Jeremy Purvis: Will that be used for the town centre regeneration fund?

John Swinney: Part of it will be used for that.

Jeremy Purvis: So, in effect, the Barnett consequential for affordable housing in England will be used for accelerated capital funding for the town centre regeneration fund in Scotland. That is a choice that the Government has made.

John Swinney: There is no direct comparability, because the Scottish Government is free to deploy resources as it chooses.

Jeremy Purvis: That is the source of that consequential. Is that right?

John Swinney: That is the source of the mechanism of the consequential, yes.

Jeremy Purvis: That money will have to come out of the 2010-11 budget, so where will the subsequent cuts in that budget be identified if you are not using it on housing?

John Swinney: The Government will address that question in the 2010-11 budget.

Jeremy Purvis: So, that has not been determined yet. We do not know where those cuts will be made.

14:30

John Swinney: We will determine that as part of the 2010-11 budget.

The Convener: One problem is that we are chasing relatively small amounts when we take into account technical and presentational changes and changes in responsibilities for capital acceleration. It is right to chase the changes, but they are small. We are getting into financial thickets, but I thank the minister for his answers and for guiding us through those thickets.

David Whitton (Strathkelvin and Bearsden) (Lab): I will begin with a more general question. You said that the Cabinet started to consider all expenditure last summer. When you appeared before us in November, I asked you about your determination to continue the council tax freeze. You said then that you were determined to continue that, which you have done. Did you consider not asking local authorities to introduce a 2 per cent cut through efficiency savings?

John Swinney: As part of the spending review, the Government set out the requirement on all public bodies to deliver year-on-year 2 per cent efficiency savings for reinvestment in front-line services. That has been part of the Government's overall financial approach. We have not revisited that question.

David Whitton: There is evidence, which you might not accept, that the 2 per cent savings are not being fed into the front line and that cuts in services are being experienced around the place. Is there any chance that you will revisit the issue?

John Swinney: The blunt answer is no. I have no intention of revisiting the efficiency savings programme. The definition of an efficiency saving is tough. That test must be applied and is reported on by Government departments, agencies and local authorities. That is an integral part of the financial architecture of the Government's approach to the fact that we are now operating in a spending framework of the lowest increases in public expenditure since devolution. It is clear from the Chancellor of the Exchequer's weekend television interviews that the Government's budget will experience a significant reduction in 2010-11 and 2011-12, so when we project what lies ahead in 2010-11, it is obvious that we must prepare for a much tougher climate of public expenditure.

David Whitton: I do not think that the words "significant reduction" passed the chancellor's lips in the interview that I saw, but perhaps you have more information than I have.

You say that the extra £10 million for local government is part of capital acceleration from 2010-11. Can you offer details on where that will be spent?

John Swinney: That is being discussed with local authorities. We expect to have the final position on that expenditure of £10 million in this financial year in early March.

The Convener: We move to agenda item 4, which is the debate on the motion. I remind members that although the officials can remain at the table with the cabinet secretary for the item, they cannot speak on the record.

Motion moved,

That the Finance Committee recommends that the draft Budget (Scotland) Acts 2007 and 2008 Amendment Order 2009 be approved.—[*John Swinney*.]

The Convener: Under standing orders, the debate on the motion can last no longer than 90 minutes. Do members wish to make contributions, or are we satisfied?

David Whitton: Tempted as I am, I will pass on that.

The Convener: I invite the cabinet secretary to wind up the debate, similarly briefly.

John Swinney: My only remark is that I was looking forward to Mr Whitton's 90-minute oration. Perhaps he has saved that for another day.

David Whitton: Another time.

Motion agreed to.

The Convener: The committee will communicate its decision formally to Parliament in a short report. Parliament will then be asked to consider a motion on the order. Are members content for our report to be circulated and agreed by e-mail?

Members *indicated agreement*.

The Convener: I thank the cabinet secretary and his officials for their attendance and for their evidence.

We will now go into private session to consider our approach to strategic scrutiny of the Scottish Government's budget for 2010-11.

14:35

Meeting continued in private until 14:57.

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