



The Scottish Parliament
Pàrlamaid na h-Alba

Official Report

FINANCE COMMITTEE

Tuesday 29 June 2010

Session 3

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FINANCE COMMITTEE
17th Meeting 2010, Session 3

CONVENER

*Andrew Welsh (Angus) (SNP)

DEPUTY CONVENER

*Tom McCabe (Hamilton South) (Lab)

COMMITTEE MEMBERS

*Derek Brownlee (South of Scotland) (Con)
*Malcolm Chisholm (Edinburgh North and Leith) (Lab)
*Linda Fabiani (Central Scotland) (SNP)
*Joe FitzPatrick (Dundee West) (SNP)
*Jeremy Purvis (Tweeddale, Ettrick and Lauderdale) (LD)
*David Whitton (Strathkelvin and Bearsden) (Lab)

COMMITTEE SUBSTITUTES

Gavin Brown (Lothians) (Con)
Lewis Macdonald (Aberdeen Central) (Lab)
Stewart Maxwell (West of Scotland) (SNP)
Liam McArthur (Orkney) (LD)

*attended

THE FOLLOWING ALSO ATTENDED:

Dave Thompson (Highlands and Islands) (SNP)

THE FOLLOWING GAVE EVIDENCE:

Rt Hon Danny Alexander (Chief Secretary to the Treasury)

CLERK TO THE COMMITTEE

James Johnston

LOCATION

Committee Room 2

Scottish Parliament

Finance Committee

Tuesday 29 June 2010

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[The Convener *opened the meeting at 17:00*]

United Kingdom Budget 2010

The Convener (Andrew Welsh): Good afternoon, and welcome to the 17th meeting of the Finance Committee in 2010, in the third session of the Scottish Parliament. I ask everyone present to turn off their mobile phones and pagers please.

The only item on the agenda is for the committee to take evidence on the United Kingdom budget of 2010. I am very pleased to welcome the right hon Danny Alexander MP, Chief Secretary to the Treasury. Welcome, minister. This is a first for the committee, and I thank you for taking the time to come to Holyrood. I invite you to make an opening statement.

Rt Hon Danny Alexander (Chief Secretary to the Treasury): Thank you, convener. I start by introducing my colleagues from the Treasury: Robert Woods is our director of macroeconomic policy, Helen Bailey is our director of public services, and Mark Parkinson is our senior policy adviser focusing on Scotland.

I thank the committee for inviting me to come here today. It is a great pleasure to be here. I believe that it is the first time that a Treasury minister has come to Holyrood to give evidence to the Finance Committee after a number of invitations over a number of years. I certainly hope that it will not be the last such occasion. In all seriousness, I think that the fact that Scottish devolution shares out some economic powers for Scotland between Edinburgh and London means that it is vital for us to work in partnership to create economic prosperity for everyone in Scotland. I hope that my presence today reflects the new spirit of co-operation between our institutions that the Prime Minister set out during his visit here during the first week of the coalition, which I was also fortunate to attend in another capacity.

I do not want to take up too much time before questioning, but I thought that it might be helpful to set out briefly the main themes of the budget. The coalition Government's first priority has been to deal with the record peacetime budget deficit. The situation that we inherited and the sovereign debt crisis in Europe have left us with no choice but to go further and faster in tackling the deficit. The big judgment that lies behind the budget is that the biggest risk to the UK would be from failing to act

in the circumstances in which we find ourselves. The budget therefore sets out the actions that we will take to eliminate the structural deficit and get debt falling by 2015-16. Indeed, the independent Office for Budget Responsibility, which we established, forecasts that we could meet those objectives a year earlier, in 2014-15.

Of course, some of the measures will be tough, including for Scotland, but, frankly, it would have been tougher still to have the cuts forced on us because we did not have the deficit under control. That really would not have been a progressive choice.

The majority of the consolidation that we are planning will come through spending not through taxation. We will consult the Scottish Government fully during the spending review. We have announced a wider consultation exercise, and I hope that public sector workers and other people in Scotland—including this committee—will engage with that process before we announce our conclusions on 20 October. I would be very happy to answer in detail any questions that the committee might have about that process. I noted that the committee's most recent report set out the importance of preparation and planning ahead when dealing with spending reductions; I welcome that and share that sentiment.

The second theme of the budget is that sustainable recovery needs to be led by the private sector. The budget also sets out a path for reducing corporation tax to 24 per cent over the Parliament, which will benefit many businesses in Scotland. The budget also introduced a national insurance contributions holiday for new businesses that will help more than 59,000 new firms in Scotland. We are determined to use the budget to free the private sector so that it can lead the recovery.

The final theme is fairness. A number of measures in the budget mean that it delivers the difficult choices that we need to make in a fair way. For example, the £1,000 increase to the income tax personal allowance will lift almost a million people out of income tax across the UK. By increasing tax credits, we have offset some of the tougher measures so that there will be no measurable increase in child poverty as a result of the budget. Likewise, uprating the basic state pension in line with earnings with a triple lock means that pensions will always go up by earnings, prices or 2.5 per cent. As a result of those measures, the richest decile will contribute most as a proportion of their income, and that is before changes to capital gains tax, the banking levy and so on are taken into account.

I will finish my opening remarks with a word on the Calman Commission on Scottish Devolution. The budget confirmed again the coalition's

commitment to implement the Calman commission's proposals. We are eager to work with the Scottish Parliament and the Scottish Government to ensure that the commission's recommendations are implemented in a way that benefits both Scotland and the United Kingdom. The commission represents an independent assessment, drawing on extensive consultation with and contributions from business and academia, of how best to deliver improved fiscal accountability within the union. I believe that the commission's recommendations represent a substantial increase in the Scottish Parliament's accountability, and our Government is committed to implementing them. However, the Government is also keen to listen to the views of the Scottish Parliament and the Scottish Government before legislating, to ensure that the new arrangements are implemented smoothly and work well in practice.

I look forward to questions from the committee.

The Convener: Thank you. Having served over a long time in both the UK Parliament and the Scottish Parliament, I echo your sentiments regarding communication and understanding between our Parliaments. I thank you for your statement. Before turning to questions, I remind committee members that, as a UK minister, the chief secretary is here to provide us with information in advance of our Parliament's scrutiny of our own budget and that he is accountable to the Westminster Parliament. We will of course have the opportunity to scrutinise our own Cabinet Secretary for Finance and Sustainable Growth in the autumn.

I will ask the first question. Can you provide more details on the process for the Scottish Government's contribution to the UK spending review and the extent to which the discussion that you have with the Scottish Government will be made public?

Danny Alexander: The first thing to say is that by announcing the date on which we will publish the spending review—20 October—we have already given a degree of certainty that there has not been in this sort of process before. I hope that that timetable in itself is helpful for the Scottish Government's budgetary planning process and the Parliament's engagement with the process.

Clearly, the final Scottish Government settlement is determined by applying the Barnett formula to the decisions that we make for each department of the UK Government. It is therefore impossible to say with certainty now what the precise parameters of the Scottish Government settlement will be. However, as we go through that process and come towards the end of it, we will have a clearer idea of precisely what the figures are. You may have further questions on that. We

are committed to engaging with the Scottish Government, to hearing any concerns that it has and to ensuring that, as far as possible, the process is an iterative one in which we work with the Scottish Government to ensure that it has as much information as we can give it.

Clearly, negotiating each department settlement within the UK Government is in itself a detailed process and no doubt sometimes a difficult one, given the scale of the reductions that we are looking at, so it may well not be possible for the Scottish Government to have final certainty on the figures until the very end of the process. In addition, by the nature of the process, most of those discussions will happen in private.

Derek Brownlee (South of Scotland) (Con): I welcome you here, minister. Certainly, I think that all of us, of whatever political affiliation, welcome the fact that we have a UK cabinet minister here to take questions. Unfortunately, many of our previous requests must have got lost in the post.

The Scottish Government has indicated that it wants to participate in the engagement process that you are talking about, which is welcome. However, in reality, the allocation to Scotland is driven by the application of the Barnett formula, which is being retained, and it is only really once a decision is made on comparable programmes in England that the Barnett formula consequences for Scotland can be worked out. Is the Scottish Government in effect being asked to check that the Barnett formula has been correctly applied, or is it being asked for some greater insight into the decisions on what is spent or not spent in England that drive the formula? Where in the process is the engagement likely to happen?

Danny Alexander: I do not foresee the Scottish Government's role as being one of checking that the Barnett formula is properly applied. I said to John Swinney, and I have made it clear to the Scottish Government, that I am happy to meet Scottish ministers whenever they would like so that they have a chance to air their concerns. Clearly, as part of the wider consultation that we are doing, they may have views on individual measures or on some of the trade-offs that are involved in the spending review process. For example, we have set out very clearly that what we presented in the budget implies average cuts of 25 per cent in real terms across unprotected departments. Equally, if we can find further savings on cross-Government issues such as welfare reform, pensions and efficiency across Government, that will have the effect of reducing the cuts that are needed to front-line Government programmes. The Scottish Government may wish to make suggestions in those areas that it would be useful to discuss. You are right to say that the

Barnett formula can be applied only once all the settlements have been made.

The other point that I will make in that regard, which may be of interest to the committee, is that the UK Government has made it clear that we wish to protect national health service spending in real terms and to meet our overseas aid commitments. Clearly, health spending is one of the major spending areas to which the Barnett formula is applied, so that ought to be of some comfort in understanding the direction in which things are moving and how it might affect Scotland.

Derek Brownlee: That is probably the key question because people will be interested in whether we are talking about a reduction of 15, 20 or 25 per cent in Scottish departmental expenditure limits. Obviously, the protection for health is helpful to an extent. Given what you said earlier about the process that will enable you to become more definite about what the likely reductions in DELs are, if you were able to find extra savings in the annually managed budgets—let us say that by August or September you had identified additional savings in welfare spending—would you then be able to say that the reductions for unprotected areas would be 23 per cent rather than 25 per cent? Prior to 20 October, will you be able to give an indicative range of what the reductions in the Scottish DELs are likely to be?

Danny Alexander: It would be very difficult to do that in a precise way. We do not intend that the process will involve us continually making daily announcements about how we are getting on. As you will understand from engaging in the process here, it is not that sort of process. It is necessary to ensure that all the different departments' figures add up and that the total adds up and so on.

We are looking for a much more interactive spending review. We want to engage in those conversations to provide what information we can. Clearly, we will not give a running commentary on negotiations with other departments or devolved Administrations, as that would not be fair on anyone. It is possible to look at the overall figure for total departmental expenditure that is implied by the budget, which suggests average real-terms cuts of 13 per cent. If we take out health and overseas aid, that gives us a figure of 25 per cent.

I just do not think that we will be able to get to a position in which we can give the Scottish Government week-by-week iterations, but the more engagement there is between the Treasury and the Scottish Government, the more the Scottish Government will be able to start to plan in the way that the committee's report urged it to in advance of getting the final figure.

Joe FitzPatrick (Dundee West) (SNP): You might be aware of some of the allegations that have been made against the UK Government about the decision to do away with the proposed tax break for the computer games industry. In some papers yesterday and today, the allegation was made that that was the result of lobbying by foreign games development companies. Would you like to set the record straight on that point?

Danny Alexander: Our decision was certainly not the result of any lobbying by anyone. What we propose is a package of overall reform of the corporate tax structure in the UK. We have set out a number of measures, including lowering corporation tax 1 per cent year by year, from which the video games industry will benefit. Our decision to take the level of corporation tax for smaller firms down to 20 per cent—the previous Government had planned to increase it to 22 per cent—will benefit those firms.

The general objective that we have set out for the tax system, towards which we have taken one or two small steps in the budget, is that we want to have a simpler and clearer tax system, not least for business, because we think that it is important that all businesses, including those in the video games industry, are encouraged to contribute to what needs to be a private sector-led recovery.

17:15

Joe FitzPatrick: Businesses will be pleased to hear that they are not up against a big foreign lobbying bloc, which would be difficult for them.

The computer games industry is particularly important to Scotland, and 10 per cent of it is based in Dundee. The industry was clear that the tax break was required to put it on a level playing field with companies in countries such as Canada and France. Has the Treasury considered the particular implications of the decision for Dundee and Scotland? The report that TIGA—the Independent Game Developers Association—has produced on behalf of the computer games industry suggests that a mere £192 million investment in tax breaks would reap £415 million in tax receipts.

Danny Alexander: The implications of all the measures in the budget are considered. The objective was to have a simpler tax system overall for business, and we are setting out a programme of cuts that, on reflection, the video games industry, in common with other sectors of the economy, will view as beneficial.

My right hon friend the Secretary of State for Scotland has made it clear that he is willing to meet industry representatives at the appropriate time to discuss these issues. That is probably a

good way for them to make representations on the matter.

Joe FitzPatrick: The computer games industry, throughout Scotland and the UK but particularly in Dundee, was disappointed about the decision but it is keen to work constructively with the Government to see whether it can make progress on the issue as quickly as possible. We will send an invitation from Dundee as soon as possible, but you or any other ministers would be most welcome to come to Dundee to engage with the industry and the University of Abertay Dundee, which has been at the forefront of developing Scotland's computer games industry.

The second area that I want to discuss is the fossil fuel levy and Scotland's renewables potential. Everyone will have been pleased to hear the initial noises from the new Government suggesting that that will be considered. When will we get a decision on that and when can we access that money? It is Scotland's money, which we want to be used to benefit Scotland's renewables industries in order to create jobs and boost the economy.

Danny Alexander: Meeting the Secretary of State for Scotland is the appropriate way for the video games industry to take the issue forward. I have a spending review to take care of, so it might be a bit difficult to fit in a meeting between now and then, as I am sure the member understands.

What we have said on the fossil fuel levy is a bit more than noises. The commitment to investigate how we can solve that historical problem, which goes back some time and was not even addressed by previous Governments, was in the coalition agreement that we negotiated and have published as a Government to set out our plans. The member can take it from that that the issue is being considered very seriously.

We have set out our wish to be the greenest UK Government ever, and it is clear that renewable energy is important to that. On the timescale, the committee will be aware that a number of issues to do with the fossil fuel levy need to be resolved. We intend to examine those in the proper context of the spending review.

I had discussions with John Swinney when I was in my previous job, and he also discussed the issue with my predecessor. We have engaged in correspondence, and I am happy to have further meetings because I recognise the importance of the issue. If we work it through in the spending review process, Scottish ministers can engage in that, which will—as I said in response to the earlier set of questions—be the most helpful way forward.

Joe FitzPatrick: On an issue that goes hand in hand with that, the previous Government talked about having a £60 million offshore wind

infrastructure competition. Is the new Government committed to that? Will you and your office ensure that, if it goes ahead, it is a fair competition? There were a lot of rumours that the previous Government had precommitted that money to certain politically convenient locations in the north of England.

Danny Alexander: I do not regard myself as being bound by any commitments that were made by the previous Government, but that competition is being progressed by the Department of Energy and Climate Change. There are issues to do with European state aid clearances and those sorts of things. We are continuing to work on the competition, but I am not in a position to make an announcement about it today. I do not think that—sorry, but I am not sure how one addresses an MSP; in Westminster we say “the honourable member”. Do I call you Mr FitzPatrick?

Joe FitzPatrick: Joe is fine.

David Whitton (Strathkelvin and Bearsden) (Lab): We call him lots of other things.

The Convener: We stand on ceremony, but don't stand on ceremony.

Danny Alexander: Okay.

I think that the most that I can say at the moment is that the issue is being looked at.

Joe FitzPatrick: I think that, hand in hand, those two things are particularly important to driving our industry forward. I have been told by the convener to finish there, so thank you very much.

Danny Alexander: Could I make one further point on the matter, convener?

The Convener: Yes.

Danny Alexander: This may be of interest, in the light of the questions. One of the other commitments made in the coalition agreement is to establish a green investment bank. That may have been the subject of your next question.

Joe FitzPatrick: It was not.

Danny Alexander: The idea of the green investment bank is to use some public resources to try to lever in private resources to invest in the green technology and infrastructure that the country needs. Clearly, there is a lot of work to be done on how it would work and how it would be set up, but it could make a major contribution to taking forward the Government's green agenda, which I know the Scottish Parliament shares.

Joe FitzPatrick: Where will the money for that come from?

Danny Alexander: That is to be resolved.

Malcolm Chisholm (Edinburgh North and Leith) (Lab): I would like to ask you about end-year flexibility, but it would be remiss of me not to briefly challenge two of the points that you made in your introductory statement. You started by saying that you had no choice but, in almost the next sentence, you said that the Office for Budget Responsibility said that you could meet your objectives a year early. I think that most people expected you to go a bit further than the previous Government had proposed, but why on earth did you need to go for overkill? I think that you are even going beyond eliminating the structural deficit. That is the first question that people would ask.

The second is on the issue of fairness. Obviously, you flagged up one or two measures that might appear to be fair but, as the Institute of Fiscal Studies said,

“the most important omission in any distributional analysis of this sort is the impact of the looming cuts to public services, which are likely to hit poorer households significantly harder than richer households”.

Taking that on board, Landman Economics, in a study that you may have seen in *The Observer* on Sunday, estimated that

“the poorest 10% of households, earning under £14,200, will see a cut equivalent to more than one fifth of their income. By contrast the richest, those earning over £49,700, will suffer a cut of just 3.6%.”

We must flag up those two basic concerns. There was a choice and it is not a fair budget.

Danny Alexander: Would you like me to answer those points before you come on to your questions?

Malcolm Chisholm: Yes.

Danny Alexander: First, I do not believe that it is “overkill”, to use your word; it is quite the opposite. As I see it—I appreciate that this is a subject of political debate—the choice facing the country is a very simple one. Do we go further and faster to reduce the deficit in the way that we have set out, which I believe is necessary to restore confidence in the economy, or do we fail to do so and, as a consequence, risk higher interest rates, which have the effect of increasing people’s mortgage costs, reducing employment, reducing economic growth and putting us at much greater risk of the sorts of problems that we have seen occurring in other countries in Europe and elsewhere that have failed to deal properly with the financial position in which they find themselves?

Those risks are highlighted if one looks at the comments about the previous Government’s plans that were starting to be made by some of the rating agencies before the election. One looks at the fact that long-term interest rates fell after the

election, partly in anticipation of what the new Government was going to do. I can go into that in more detail if the committee is interested. We can see the sorts of very serious—potentially disastrous—problems that would have resulted for the whole economy, which would have affected Scotland just as much as the rest of the UK, if we had failed to take the necessary action to reduce the deficit more quickly.

I also observe that the international consensus on the issue is that those countries with the greatest deficits have to take early and fast action to deal with them. At the G20 summit at the weekend in Toronto, there was a clear welcome for that and a clear welcome for our approach—I think that he used the word “courageous”—from President Obama.

If you look around the world for countries with big deficits that have to take urgent and rapid action, you will see that, within the European Union, only Ireland was in a worse position than the UK. That makes clear that we are at the top of the list where consolidation is concerned.

You will no doubt have seen in the budget red book that, for the first time, we have set out the distributional impact of the budget. In my judgment, the overall impact is fair. I am sure that members have it in front of them, but I draw the committee’s attention to the charts on pages 66 and 67 of the budget book, which show that, in both cash terms and income terms, the richest decile pay the greatest proportion—those with the broadest shoulders are bearing the greatest share of the burden. Sorry to give a long answer, but it is an important point.

In addition, in what is one of the toughest budgets that this country has had since the second world war and in the context of all the measures that we are debating today, we have still managed, through our decisions, to ensure that children in poverty are protected from the impact of the budget. That is a significant benefit.

The impact of spending cuts cannot be judged until we have had the spending review and decided where we are going to make savings and which areas we are going to protect. As I said in response to an earlier question, much of that depends on how we can make cross-Government savings that reduce the impact on departments and on the choices that we make. I assure the committee that the same principle of fairness that informed our choices on the budget will inform our choices on the spending review.

Malcolm Chisholm: We could have a protracted discussion about it, but I will just say that the Treasury’s distributional analysis is a matter of tax and benefits only and applies only until 2012. The Institute for Fiscal Studies has

pointed out that things get worse for the poorest people thereafter, because of several cuts including the benefit cuts.

You have highlighted one set of risks; the other set of risks that we are worried about is the effect on growth. Your projection is already lower than it was previously, and the Office for Budget Responsibility has pointed out that you are assuming that 0.9 per cent of growth will be from exports in 2012. Many people are worried about that, given the state of the European economies. We could spend our whole time on that.

However, I will move on to EYF. There is a feeling that EYF could at least alleviate what will be a very difficult situation for the Scottish budget. The Cabinet Secretary for Finance and Sustainable Growth announced that there is £348 million of EYF from last year. The question is whether the Scottish Government will be able to access that. Will you be making decisions imminently about access to EYF throughout the spending review period?

Danny Alexander: I will first address a couple of the observations that Malcolm Chisholm made at the beginning. Without getting into a protracted debate, as he suggests would be possible, I will give my side of that story. In the budget, we set out the distributions for 2012-13—that is where the key measures apply. This is not the only budget that will happen during this Parliament—there will be budgets on an annual basis, as always. There is plenty of opportunity for further measures to maintain the commitment to fairness that we have set out in this first budget of the coalition Government.

Mr Chisholm is right to say that the independent OBR's assessments—independent assessments, not our assessments and not a politician's assessments—show growth increasing over the course of this Parliament, and getting faster towards the end, with unemployment falling and a strong private sector-led recovery taking hold. Part of the reason for the measures that we are trying to take in the budget, as well as other measures that we have been announcing, is to try and ensure that that growth is more balanced than it has been in the past. One of the criticisms of what happened over the past 10 years was about the overemphasis on financial services, particularly the City of London. If we can have more export-led growth, with businesses developing across the whole UK including in areas that are traditionally more dependent on the public sector, that will be a good thing for the economy as a whole, particularly here in Scotland.

As I said in a statement to the House of Commons a couple of weeks ago, we have been reviewing access to end-year flexibility in the current year. When I took office in this role and

looked at the books, I discovered yet another problem with overcommitments of EYF and the reserve from the previous Government. Without remedial action, that would have meant not having any reserve left for future emergencies or any further needs that our troops might have in Afghanistan. I am sure that the committee will agree that it is important to have some prudent planning, rather than the sort of irresponsible planning that we saw in the past.

I am not in a position to make announcements yet, but I recognise that devolved Administrations view EYF as an important part of their flexibility. In the context of this review, I do not seek to challenge that assumption.

17:30

Jeremy Purvis (Tweeddale, Ettrick and Lauderdale) (LD): Good afternoon, chief secretary. I go back to an earlier point about relationship and timing with regard to the spending review and how the Scottish Government and Parliament can scrutinise the budget. As you will know, a draft Scottish budget is normally published for scrutiny. However, you have indicated that the spending review this year will not take place until the end of October. Do you have views on how proper scrutiny can take place both north and south of the border and how there can be interaction in that process?

Danny Alexander: It would not be appropriate, nor would it comply with the respect agenda that we have introduced, for me to comment on the internal processes of the Scottish Parliament and the Scottish Government. However, this committee can no doubt make its views known on those matters. I observe only that the extent of the savings that need to be made over the spending review period is now very clear.

I return to the observation that I made about the committee's previous report, because I assume—in fact, I know—that an awful lot of work has been, and is, going on in UK Government departments to plan for the areas in which savings can be made, to look at how efficiencies can be made and how front-line services can be protected, and so on.

The Scottish Government can look for itself at some areas on which we have made announcements, such as public sector pay. Again, being clear on such matters will give more certainty about departmental budgets. As the process goes forward, and given the amount of information that is already in the public domain, I hope that the Scottish Government will not have to plan from a standing start on 20 October.

Jeremy Purvis: Thank you. I will touch on one of the elements to which you referred earlier. You

mentioned the green investment bank. I want to ask, too, about infrastructure UK, which was announced in the budget and which links with Calman's consideration of the Parliament's borrowing powers. The issue is about large infrastructure projects of sufficient scale, such as the Forth crossing project, having consequences across the UK as well as for the devolved budget. How do you envisage infrastructure UK working when it comes to the ability of the devolved budget to invest in Scotland? Will infrastructure UK be able to consider projects across the United Kingdom, or do you think that, as with the regional growth fund, infrastructure UK should apply just to England?

Danny Alexander: On the last point, given where the resource comes from, the regional growth fund will of course be an England-only fund. However, I would certainly encourage the devolved Administrations to consider whether there is a case for applying that idea within Scotland, Wales or Northern Ireland. The committee may be interested in considering that.

Infrastructure UK has a broader and more strategic role than was perhaps implied in your question. Its job is not to consider individual projects and work them up in detail; its job—initially, at least—is to take a strategic view of the infrastructure needs of the country as a whole. Its first task will be to produce a national infrastructure plan that will set out long-term goals for UK infrastructure. It is absolutely right to say that borrowing is a key issue within the Calman framework. It is clear that what we seek to deliver is within that framework; we are not looking to overturn that or set up something entirely new in its place. I am seized of the importance of the borrowing issue. We will look to take that forward when we set out in detail how we plan to implement the Calman proposals. That may provide some help in the areas that Calman talked about.

I understand that the previous Government offered a package of financial flexibilities to help with the funding of the Forth road bridge, but that that was not something that the Scottish Government wanted to develop—which is, of course, its decision.

We will take forward the issue of borrowing powers through the Calman process. We are setting up the consultation and engagement processes that we will use to develop the Calman recommendations. We will have a high-level group involving businesses and civic society in Scotland that will talk about the implementation of Calman; there will also be a more technical working group. The Scotland Office and the Treasury will work together on both groups, but the overall process

will obviously be led by my honourable friend, the Secretary of State for Scotland.

Jeremy Purvis: Thank you. My next point touches on an issue that others have considered: whether the budget is progressive or regressive. I do not necessarily want to go down that path; I want to ask about public sector pay where there are devolved and reserved parallels and some shared areas. There is a pay freeze in the budget for public sector workers in Scotland, but in UK bodies there is a pay freeze for those who earn £21,000 or more. Do you have more information about pay for those workers in UK bodies who earn under £21,000? Can they expect an uplift in their pay in the future? Has the Treasury had any discussions with the Scottish Government about Scottish Government pay? What will be the impact on local economies where there is a large amount of public sector employment, whether in UK bodies or in the Scottish Government?

Danny Alexander: You are absolutely right to draw attention to the pay policy that we have set out. In keeping with the emphasis on fairness in the budget, we thought that it was important that, for those workers earning £21,000 or less, there will still be some increase over the two years in which the freeze will apply to everybody else. Those workers will be entitled to a pay rise of about £250. Although there might be a little flexibility above that in certain cases, depending on the views of the pay review bodies, £250 is the figure. We went for that cash-floor idea partly because it is more progressive. Clearly, £250 is a greater share of income for someone who earns £10,000 a year than it is for someone who is on £20,000 a year.

I know that the Scottish Government is interested in our approach to pay, but there are people in Scotland who work for bodies that are responsible to the UK Government, such as the Department for Work and Pensions and Jobcentre Plus, where the pay policy that we have announced will apply. Equally, there are people who work in organisations that are responsible to the Scottish Government and for whom Scottish ministers will have to set out their own pay policy. I am sure that they are looking with interest at what we have set out. As I observed earlier, one of the effects of controlling pay is that there is less pressure on departmental budgets, which has the potential to allow jobs overall to be protected. I am sure that the Scottish Government is as aware as I am of the nature of those trade-offs.

Tom McCabe (Hamilton South) (Lab): Good evening. I echo earlier sentiments about how good it is to see you here this evening; it is positive that you accepted our invitation so early in your tenure. I think we all hope that your colleagues will follow your lead in their relations with this Parliament.

I take us back a bit to before the budget. There was an announcement of £6 billion of cuts and that Scotland had to take its share. However, you seem to have agreed with the Scottish Government that now would be the wrong time to implement Scotland's share of those cuts, which the Scottish Government felt would impede recovery. A few weeks later in the budget, you announced that VAT would rise to 20 per cent, which many people do not see as a stimulus. Do you agree with the Scottish Government's view that to implement the £300 million-odd of cuts would impede recovery? Do you not think that you are in danger of being seen as facing two ways at once?

Danny Alexander: It would be wrong to say that we reached agreement with the Scottish Government on that subject. We said to the devolved Administrations that they had the freedom to choose as part of our respect agenda.

It was up to the Scottish Government to decide whether it wanted to take those cuts in-year, as UK Government departments are doing, or next year. That was entirely a matter for the Scottish Government; we offered it flexibility and choice, which it chose to exercise in the way that it did. Tom McCabe may well wish to ask the Scottish Government about that decision. It is a question for the Scottish Government, rather than for me.

It follows from that that I reject—with the greatest of respect—Tom McCabe's second assertion. The VAT measure was not proposed by any party in its election manifesto, and it is not a tax rise that anyone wanted to make. However, we were faced in particular with an economic forecast for the structural part of the deficit that was £12 billion larger than the previous Government had forecast.

The committee will know that the structural deficit is not eliminated by economic growth; it can be removed only by Government policy action. We had to make a choice about whether to remove it through yet more spending cuts, or to find a tax measure to deal with it. In that context, the right choice was to increase VAT to fill that gap, rather than going for further spending cuts that had the potential to put essential services at risk. Given the big judgment that lies behind the budget, as I set out earlier, going for the rise in VAT was the right thing to do.

Tom McCabe: You are the chief financial secretary and are responsible for macroeconomic policy. Did you agree that not implementing £300-odd million of cuts in Scotland was the right thing to do for the United Kingdom's economic recovery?

Danny Alexander: It is not for me to agree or disagree. What I agreed to do, and what we as a Government agreed—

Tom McCabe: With respect, it is your responsibility. You are responsible for macroeconomic policy in the United Kingdom.

Danny Alexander: What we agreed to do, on the basis that we thought that the UK financial situation could cope with the choice being exercised either way, was to offer the Scottish Government, as a devolved institution—and Wales, which has not yet decided which choice it will make—the flexibility to make that decision for itself. That was the right thing to do.

In the spirit of co-operation that we seek to establish under the respect agenda set out by the Prime Minister, we are allowing the Scottish Government to make that choice itself. It would have been wrong to try to impose that decision given the respect agenda.

Tom McCabe: You said earlier that you felt that you had done as much as you could to protect some of the most impoverished children in our society. We have seen alterations to child tax credits and the freezing of child benefit, and we are already seeing pretty substantial cuts in local government to some of the life-line services on which some of the most impoverished children in our society depend. What has been done specifically to protect those children?

Danny Alexander: The charts in the budget book show the targeted measure that we have taken to inject nearly £2 billion into the child tax credit to ensure that there is additional income for families on low incomes—particularly those in poverty—with children. The effect of that, in combination with the other measures in the budget, is that there is no impact on measured child poverty in the UK.

That measure in particular has been widely welcomed. Comments from the chief executive of Barnardo's, for example, made clear that such tax credit reforms—taking away tax credits from families on higher incomes and focusing the money on those who are most in need—are the right way to approach the situation to mitigate the impact of the budget on child poverty. It was right that we focused our attention on that area.

Tom McCabe: You would, I hope, agree that child poverty is worst among what some view as a growing underclass of children whose parents are not in employment and who live in very challenging circumstances. As I said, we are starting to see cuts at a local level to some of the vital services on which people in that situation depend. What has been done specifically to try to protect people in that position?

17:45

Danny Alexander: In the UK budget, we have also taken measures to increase work incentives. Clearly, getting a job is the best route out of poverty for anybody. Lifting the income tax allowance by £1,000 is a significant benefit to people on low incomes, and I hope that it will encourage people to seek work. Likewise, lifting the national insurance threshold for employers' contributions will encourage businesses to take on people on lower incomes in particular.

On local services, the local government spending settlement in Scotland is a matter for the Scottish Government, not the UK Treasury. I have seen in the Highlands, as I am sure other people here have, that savings are already happening in local government. However, those involve choices for the Scottish Government and local authorities, rather than for me as Chief Secretary to the Treasury. In the context of my evidence to the committee, it would not be appropriate for me to comment any further on that.

Linda Fabiani (Central Scotland) (SNP): Thank you for being here—it is appreciated. I have two issues to ask you about. The first is the Calman proposals, to which you referred in your opening statement. I have concerns about the financial aspects of the Calman proposals and their effect on the Scottish budget. You must have had such concerns at one time, because you called for full home rule and the implementation of the Steel commission proposals not that long ago.

I am sure that you will have read the latest paper by Professor Drew Scott and Professor Andrew Hughes Hallett, "Scotland: A New Fiscal Settlement", from which I would like to draw out two issues in particular. The first is about the direct linking of Scotland's budget to income tax raised in Scotland in times of recession, because it is obvious that the income tax take will go down. There is no capacity for Scotland to cover that deficit. If we couple that with the increase in tax allowances—although that is welcome in itself—that is a problem for Calman, too, because it reduces the total income tax revenue that is raised in Scotland and, therefore, the amount that is assigned to Scotland's budget from income tax. I understand from the IFS, among others, that there is a view that the rise in VAT to 20 per cent will cover some of that deficit. However, of course, Scotland does not receive any of that additional revenue from VAT, so Scotland has a double whammy here. We are losing through lower spending and higher taxes, but we must still pay the higher VAT. I am interested in your views on that.

I am also interested in your earlier reference to the Calman framework. I am quite heartened by that because it suggests to me that you are

considering some flexibility within Calman in the discussions that you intend to have. You said that a group will be set up in Scotland to consider some of that. What are your views on the bad effect on Scotland to which I referred and the potential flexibility of the Calman framework?

Danny Alexander: Thanks for the welcome to the committee and the welcome for the policy of increasing income tax allowances—I am grateful for that.

On the Calman process, the Calman commission's recommendations were the result of a great amount of deliberation and work, with contributions from people from a range of different political traditions in Scotland. The commission had expert groups, with academics and other experts. It is not our intention at all to try to overturn the Calman commission's proposals—as some have suggested—and replace them with an entirely different framework. The conversations that we seek to have—and which we are having—with Scottish Government officials are much more around the area that you suggested. We are asking whether there are particular, practical issues that arise in the context of the implementation of the Calman proposals. We are not saying that we should scrap the proposals and do something entirely different; we are asking whether there are ways within the Calman framework in which issues can be managed. That is a practical conversation about how Calman is implemented that we are keen to have quickly because we want to get on with the process of introducing legislation and implementing the Calman commission's proposals. I believe that the proposals represent a very important step towards additional responsibilities for the Scottish Parliament—an additional level of accountability and responsibility, if you like.

Clearly, we are seeking continued engagement on the volatility issue that has been raised. Likewise, the tax allowances point is a perfectly good one that I am sure can be accommodated within the Calman proposals. We are looking at precisely how that can be done. The engagement that we seek with Scottish Government officials is one of working through such issues on a practical basis. What I am not seeking to signal, which I think you may have implied, is that we are looking at getting rid of the Calman proposals and replacing them with something entirely different. That is certainly not what I intended to signal.

Linda Fabiani: I will make two points on that issue. I ask you to bear in mind first that times have very much changed since the Calman commission made its proposals and secondly that the expert financial group that fed into the commission did not recommend the financial measures that eventually came out in the full

Calman commission report. In fact, some members of that group are now very concerned about some of the proposals that have come forward, which did not come from the group.

My second issue has been a concern over almost the entire lifetime of this Parliament. When the Parliament first introduced free personal care for Scotland's elderly, the Department for Work and Pensions saved about £30 million a year. There was a bit of an uproar at the time across the parties in the Parliament—including even those in government—because the Treasury banked that saving. The same situation arose when the Parliament considered the abolition of the council tax. The Treasury said that it would also bank the saving on council tax benefit, which was estimated to be about £450 million.

I know that the coalition is now reviewing local government finance for England and I also know that when the Department for Work and Pensions ran a consultation on care of the elderly in England, it proposed changes to the attendance allowance across the UK, so Scotland's disabled elderly would be paying for policy change in England. In the spirit of respect under which we now hold our discussions, will you reflect on the fact that such issues are not beneficial for devolution or for respect among Governments? Will you therefore consider letting the Parliament use its powers properly without being unfairly penalised by Westminster?

Danny Alexander: I hope that the new UK coalition Government has been clear that it wants to have a spirit of co-operation on a range of issues and that, if concerns are raised, we are happy to hear them and have discussions in a mature and respectful way. However, part of being respectful involves being honest. There will be differences of opinion, but I hope that those can be amicable differences of opinion within the spirit of a good relationship and that they do not result in the political rows that we perhaps saw in the past.

It is perhaps worth observing that, for example, council tax benefit is paid to people to offset the requirement to pay council tax, so if there is no council tax, it is clearly legitimate to ask why that benefit should continue to be paid. We have to look closely at the cost of such measures and at the interaction between policy choices and the benefits system. I will not give any blanket reassurance on that point, except to say that of course I welcome the opportunity to discuss such matters if they are raised. I am not sure that I can say more than that.

Linda Fabiani: Thank you for your commitment to a discussion.

David Whitton: I echo the general welcome from the committee to Mr Alexander.

I take you back to the first set of questions from Mr Brownlee and to the respect agenda that the coalition Government now has with the devolved Government. As you know, our budget timetable is slightly out of kilter with yours, in that we would usually start our budget discussions in September. We have a baseline figure to operate from and there is plenty of evidence from the budget and from our chief economic adviser, Dr Goudie, on the budget's likely impact on Scotland's budget. If John Swinney was to give you a ring at the beginning of September and say, "Danny, can you tell me what the indicative figures are for the Scottish Government budget for next year?", would you be able to tell him?

Danny Alexander: I doubt it very much because, as I explained in answer to earlier questions, the Scottish Government's final settlement is decided by the Barnett formula and will be a consequence of the precise settlements that are reached. For the first time, we have set a clear deadline—it is 20 October. In the past, the date of the spending review would have been mired in secrecy and uncertainty until the final few weeks before it was announced. The planning timetable is clear, and the fact that the broad parameters of the process are also clear provides UK departments and devolved Administrations with scope to start thinking hard about the choices that they want to make.

David Whitton: Forgive me for interrupting, but we would normally have a bit more time to consider the impact that budget cuts at UK level would have on the Scottish budget. I would have thought that it would be perfectly feasible for you to give Mr Swinney some indication in September of the cuts that we are likely to face.

Danny Alexander: I hope that the broad extent of what the cuts will be is clear from what I have said. As I said in answer to an earlier question, the average cut in departmental expenditure limits across all departments is about 13 per cent. When we take into account the protected areas, principally health, that takes the average departmental figure to 25 per cent. The Scottish Government has plenty of bright economists among its officials who will be able to work through the sort of forecasts that will be useful in planning ahead.

I look forward to having regular conversations with John Swinney as part of the process and to helping him as best I can, but I will not give an undertaking that I will be able to give him a precise figure. I am not sure that Mr Whitton wishes to get rid of the Barnett formula. Applying the Barnett formula properly means knowing what the departmental settlements are, and we will not know what the settlements are for every department until the very end of the process.

David Whitton: I asked whether you would be able to give Mr Swinney an indication of what the cuts were likely to be, rather than precise figures.

Putting that to one side, will you guarantee that the Barnett formula—I am not asking for it to be ended—will not be changed by your Government until such time as the Calman proposals go through the Westminster process?

Danny Alexander: We have said in the coalition agreement that there is no plan to review the Barnett formula while the current fiscal consolidation is going on. The fiscal consolidation process is a big enough challenge without reopening that issue, too.

Legislation on the Calman proposals will be introduced in the autumn and will be implemented following consideration in the House of Commons. The implementation timetable is to be discussed. Some of those discussions will take place in the high-level Calman implementation group, the establishment of which we are announcing today, which will include representatives of Scottish businesses and civic society in Scotland who can help us to work on such precise issues. I hope that by proceeding in that way we will be able to answer the member's question on the Barnett formula and set out how engagement will take place on the implementation of Calman.

David Whitton: I obviously missed the announcement of the high-level Calman implementation group, but I am not surprised that you have come to the meeting with an announcement.

You mentioned the red book and said, quite rightly, that the budget would impact on some of the richer people in the UK, but I am sure that you will admit that the IFS, in particular, has pointed out that the lowest 10 per cent of income earners will be hit extremely hard. In fact, they will be hit disproportionately hard if we take into account the impact of cuts in public services. How do you feel about making the poor poorer?

Danny Alexander: I made my position on that clear earlier. In my view, the measures that were announced in the budget are progressive.

David Whitton: They cannot be progressive if they will result in poor people becoming poorer.

Danny Alexander: I will not hide from anyone the fact that the measures are tough and that everyone will have to make a contribution, but the fact is that in terms of income share and in cash terms, which the IFS said is the best way to measure the impact of the VAT rise, in particular, the overall impact of the budget measures is progressive.

On the spending cuts, I will just give the reply that I gave—

David Whitton: The IFS did not say that, overall, the budget measures were progressive.

Danny Alexander: No, that is what I am saying.

David Whitton: So that is your interpretation.

18:00

Danny Alexander: The IFS said that that was a proper subject for debate; I think that the impact of the budget measures on people's income, as set out in the information that we have presented in the red book, is progressive. I am not trying to hide from the committee the fact that there is an impact across the whole of society. That is why we chose to take measures to mitigate the impact, particularly on children in poverty and pensioners. Those seemed to me to be the groups that it is most important to protect.

David Whitton: Well, the Prime Minister and Deputy Prime Minister—

The Convener: I remind members that this market day is wearing late—you should make this swift and short.

David Whitton: I remind the chief secretary that Mr Osborne and Mr Clegg have been keen to describe the measures as progressive, in the sense that the rich will feel more pain. However, the IFS said that that claim was debatable. Obviously, you do not agree with that view.

Danny Alexander: I believe that the budget is progressive. Some of the measures that we have announced—for example, the increase in capital gains tax—were not taken into account in the assessment of the impact on income. It is striking that it was a Labour Government that set up a capital gains tax regime that enabled someone who took their bonus in shares to pay less in tax than the person who cleaned their office. We have set that anomaly right in this budget, and that is something that any progressive should welcome.

David Whitton: No—you have made the cleaner poorer than she was before. However, let us put that to one side.

During the election campaign, you helpfully issued a leaflet headed "Danny Alexander puts the Highlands first". It said:

"Danny is our man at Westminster, not Labour's man sent north to the Highlands."

Do you accept that you are now the Tories' man sent north to Scotland to inflict tax pain on all of us?

Danny Alexander: No, I do not accept that at all. I am surprised to hear that claim from a member of the Scottish Parliament, given that the Scottish Parliament has strong historical experience of coalition Governments and that it is

a Parliament of minorities, in which people from different parties regularly work together for the good of the country. That is exactly what is happening at Westminster, where the Liberal Democrats and Conservatives have recognised that the scale of the problems that face the United Kingdom is so great that it warrants two parties working together.

I closed the budget debate last night, and the one party that was responsible for the mess that this country is in was denying all responsibility for it, whereas two parties were taking responsibility for cleaning up the mess that it had created. It is a testament to the strength of the coalition that we can do that.

David Whitton: I am sure that Mr Alexander does not expect me to agree with anything that he has just said. However, in the spirit of consensus, I thank him for giving evidence.

The Convener: All committee members have now contributed. I invite some quick questions from Dave Thompson, who is not a committee member.

Dave Thompson (Highlands and Islands) (SNP): Thank you very much for allowing me to speak, convener. I welcome the chief secretary—it is very good to see you here today. We have put off the lights so as not to put too much heat on you—did you notice?

In these difficult times, many councils in Scotland have debt problems. For example, Highland Council's housing debt stands at about £136 million. I note from your website, which I checked today, that you stated in February:

"The huge Highland housing debt is a millstone around the council's neck. In these tough financial times, getting the Treasury to see the case for debt relief is a crucial part of our campaign for a fair funding deal for the Highlands.

'Last year, the council and I presented proposals to the government for temporary relief from the multi-million pound annual debt repayment ... Our original plan would have supported the building of an extra 330 homes and created 470 jobs.

'It was disappointing that this measure was not included in last year's budget'".

Given that Highland Council's housing debt is a "crucial" matter for the Highlands, to use your word, do you think that the write-off of the debt should have been included in last week's budget?

Danny Alexander: I am glad that the member is here—it is good to see a colleague from the Highlands taking part in these proceedings.

Since taking office as Chief Secretary to the Treasury, I have looked at the books and seen for myself the scale of the country's massive debt problem, which was in no small measure due to the actions of the previous Government—that

inheritance is the principal challenge that we face as a country.

On debt relief, the member is right to say that I have promoted that measure in the past. Considering the debt problem that we face, I cannot find the scope to do that right away. In the context of the challenge that the country faces, that is one of many things that, sadly, will have to wait until we have put right the country's overall financial situation. Of course, other avenues are open—I would hope that the Scottish Government, which has responsibility for housing in Scotland, would consider the claims of Highland Council in the context in which the member has quite rightly put them. Other financial mechanisms are available, too. In these straitened financial times we must look at all levels of government and consider different ways of doing things to tackle the problems that undoubtedly exist throughout Scotland and the UK.

Dave Thompson: May I follow up on that quickly?

The Convener: I must bring proceedings to a close. Derek Brownlee can ask a quick final question.

Derek Brownlee: It is a very quick question, which relates to some of the things that the chief secretary has mentioned with regard to Calman. I think that I picked him up correctly as saying that he wanted to consider issues within the ambit of the Calman proposals. Does that rule out looking at other issues?

In the budget document and in the coalition agreement, there was a commitment to publish a paper analysing the feasibility of a variability in corporation tax in Northern Ireland, for example. Is the new Government prepared to consider that for Northern Ireland but not for Scotland, or could that type of thing be part of the broader discussion to which the chief secretary referred?

Danny Alexander: Corporation tax was not one of the things that the Calman commission recommended to be changed for Scotland. The issue has been raised in Northern Ireland in the context of cross-border issues that exist between Northern Ireland and the Republic of Ireland. We have made no commitment to any specific change there; we have simply committed to investigate the matter in the context of the overall need to promote peace and prosperity in Northern Ireland.

We are seeking to implement the Calman commission recommendations, which apply to Scotland and not to Northern Ireland or Wales. We seek to have conversations on some of the practical issues in relation to the precise way in which the measures that Calman recommended will work. That seems to be the right way to ensure that we get the implementation of Calman right,

which should be what matters most to everyone in Scotland.

The Convener: Minister, I regret that time is now defeating us, but we have covered a range of useful topics. Do you wish to make any final comments to the committee?

Danny Alexander: First, I thank the committee for the welcome and for the very close questioning. I will certainly recommend the experience to ministers in other departments should other committees of the Scottish Parliament choose to invite them.

Secondly, I stress the importance of the implementation of the Calman commission recommendations. They are a major step for the UK Government to take—as it is quite right to do, given the consensus that was established behind them.

Linda Fabiani: It was not full consensus, minister.

Danny Alexander: There was a great deal of consensus in Scotland among parties that comprise a substantial majority in this Parliament, not to mention the Westminster Parliament. That counts as a pretty good consensus to me.

Of course we want to work on implementation, and the Treasury will work closely with the Scotland Office to establish the implementation group that I mentioned. It will bring together people in business and civic society in Scotland to work on precisely how we implement the Calman commission recommendations, to iron out any practical issues that may be raised and to ensure that we can get on as quickly as possible with passing the legislation. We will in due course implement that legislation, to the good of the people of Scotland and the accountabilities and responsibilities of the Scottish Parliament.

The Convener: Minister, the great thing about history is that just sometimes one actually gets to make it. I thank you for your presence and your contribution, and I hope that it will be the first in a continuing series of meetings as part of an essential dialogue and communication between our two Parliaments.

Meeting closed at 18:09.

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