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Pre-budget 2027-28 report The affordability and sustainability of the Scottish Government's tax and spending plans

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Finance and Public Administration Committee

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b. any report made by a committee setting out proposals concerning public revenue or expenditure;
c. Budget Bills;
d. any other matter relating to or affecting the revenue or expenditure of the Scottish Administration or other monies payable into or expenditure payable out of the Scottish Consolidated Fund;
e. any other matter falling within the responsibility of the Scottish Administration relating to the National Performance Framework, public inquiries, and public administration; and proposals for the formation and budgets of officeholders established by the Parliament.



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Introduction

1. This, the Finance and Public Administration Committee's first pre-budget report in Session 7, considers the affordability and sustainability of the Scottish Government's tax and spending plans for 2027-28.

2. Our scrutiny took place amidst significant financial pressures facing the Scottish Government, including an anticipated fiscal gap of £2.624 billion in resource and £2.146 billion in capital by 2029-30 [1] and a weakening global economic outlook arising from the Middle East conflict. Increasing energy prices and higher-than-forecast inflation is further squeezing household incomes and placing added pressure on public spending. [2]

3. The financial year 2027–28 looks particularly difficult for the Scottish Government, with both day-to-day and capital spending estimated to fall in real terms. The UK Government's prioritisation of defence spending is estimated to reduce capital funding for the Scottish Government by a further £87 million. [2]

4. The Scottish Government also faces its highest ever negative reconciliation of £720 million in 2027-28 due to weaker-than-expected income tax performance relative to the rest of the UK in 2024–25. This reconciliation exceeds the Scottish Government's borrowing limit for forecast error for the first time, placing more pressure on day-to-day spending. [2]

5. Our report therefore considers the evidence we heard on how the Scottish Government plans to meet these fiscal challenges. This includes prioritising public spending and reform, economic growth and a strategic approach to tax revenues—the three pillars in its Fiscal Sustainability Delivery Plan (FSDP) [3] . We also consider how the Scottish Government is using its fiscal flexibilities to help manage Scotland's public finances effectively.

6. The Committee received 66 written submissions to our call for views, which ran from 29 June until 14 August 2026. [4] We also heard from a range of witnesses during September including economists, representatives from business and higher and further education, public sector bodies, tax specialists and the voluntary sector. We concluded our evidence sessions on 30 September 2026 by hearing from the Cabinet Secretary for Finance and Local Government. [5] The findings set out in this report are therefore based on evidence we received before the UK Government's Autumn Budget announcements on 28 October 2026.

7. The Committee thanks those who took the time to provide written and oral evidence, which helped shape our findings and recommendations.

Fiscal Sustainability

Overall approach

8. The fiscal pressures set out in the introduction to this report are well documented in the Scottish Government's 2025 MTFS [1] and Scottish spending review 2026 [2] and the more recent fiscal update from the Scottish Fiscal Commission (SFC) [6] .

9. The Scottish Government's FSDP published in June 2025 includes the following three pillars which aim to address the fiscal challenges and ensure sustainable public finances—

    - Pillar 1: ensuring public money is focused on delivering government objectives, underpinned by reform and prioritisation to maximise impact.
    - Pillar 2: supporting sustainable, inclusive, economic policies with the greatest potential to grow Scotland's economy, expand and broaden the tax base to fund public services.
    - Pillar 3: ensuring a strategic approach to tax revenues which considers the longer-term impact of our tax choices and competitiveness. [3]

10. Some of the themes in our report are broadly structured around these pillars, while this section explores the Scottish Government's overall approach to fiscal sustainability.

11. Much of the evidence we received suggested that all three pillars would need to be delivered to meet the fiscal gap and that lasting fiscal sustainability will depend on meaningful public service reform, and stronger economic growth, rather than simply adjusting spending allocations. [7] The Chartered Institute of Taxation (CIOT) was also keen to see fundamental tax reform to grow the tax base "in a fair and effective way" and to contribute to raising more revenue to support public services. [8]

12. The Committee also received evidence on the robustness of the Scottish Government's key financial planning documents to support fiscal sustainability, including—

    - the 2025 MTFS setting out the economic, funding and spending outlook to 2029-30 [1] ,
    - the accompanying FSDP including cross-government actions and reforms to manage fiscal pressures and secure long-term financial sustainability [3] , and
    - the Scottish spending review 2026 outlining multi-year public spending and investment plans up to 2028–29 for day-to-day (resource) spending and up to 2029–30 for capital infrastructure [6] .

13. The evidence we received suggests that the MTFS recognises the scale of the financial challenges, but that more detailed delivery plans, clear milestones and performance measures are needed to support delivery of the actions and reforms in

the FSDP. There were also demands for greater transparency on progress with delivery and evidence of outcomes.

14. We heard from the Institute for Public Policy Research (IPPR) Scotland that the wider policy framework, including the FSDP and spending review, "does not provide a credible and coherent plan" for addressing the fiscal challenges over the parliamentary session. [9] While noting that the measures identified in the FSDP "are all relevant", Professor David Bell questioned "whether the FSDP provides a sufficiently credible route from identifying that problem [in the MTFS] to resolving it". [10]

15. Scottish Borders Council told the Committee that the MTFS and spending review "do not seem to be particularly well linked at the moment" and suggested that reconciling "the different pieces of the jigsaw would be hugely helpful to us in our longer-term financial planning". [11] We heard from the Institute for Fiscal Studies (IFS) about seven risks to the Scottish spending review 2026, including tax revenue uncertainty, income tax reconciliations, UK Government decisions, inflation and pay pressures, and benefits spending uncertainty. [12]

16. There was widespread support for the move towards multiyear financial planning through the recent spending review. Amongst others, Scotland's Regeneration Forum, COSLA and Colleges Scotland noted that a multiyear approach can maximise the impact achieved from limited resources. [13]

17. While the Committee's discussion with public sector bodies, representative organisations and local authorities mainly focused on public service reform, they each raised financial pressures affecting their sectors. Some, including Colleges Scotland and Police Scotland, expressed concern about their ability to continue to deliver public services effectively within flat-cash settlements. [11] COSLA highlighted a projected £1 billion gap for local authorities by 2027-28 and spoke of "a mismatch" between available funding and the delivery ambitions of key policies. Aberdeenshire Council also warned that demand and public expectations are outpacing the funding available for local authorities. [11]

18. Broader concerns were raised regarding the impact of inflation, rising costs and wider economic uncertainty, which were seen to place additional strain on public services and the Scottish Government's ability to deliver reform.

19. The Cabinet Secretary described the fiscal pressures as "long term and structural", requiring informed debate, cross-party collaboration and difficult choices on priorities and trade-offs. She highlighted she had convened a recent cross-party roundtable to build a shared understanding of the economic and fiscal outlook and plans to repeat this after the UK Government's Budget on 28 October. [14]

20. **The Committee recognises the significant fiscal pressures facing the Scottish Government, including those outside its control such as inflation and rising energy prices.**

21. **The Committee welcomes the Scottish Government's efforts to set out the scale of the challenge, along with the actions, multiyear plans and reforms it intends to deliver to place Scotland's public finances on a more sustainable footing.**

22. **However, based on the evidence we heard, we are concerned there are substantial risks to the Scottish Budget should any element of the FSDP not be delivered in full and on time. We therefore make recommendations later in this report to improve transparency and scrutiny around progress with delivery.**

23. **While we welcome cross-party discussions to build shared understanding of the economic and fiscal outlook led by the Cabinet Secretary, these must not be a substitute for parliamentary scrutiny. We therefore ask that any economic and fiscal data presented at these discussions is also provided to Parliament for transparency and scrutiny.**

Future financial planning publications

24. The Committee notes that HM Treasury's Charter for Budget Responsibility - Autumn 2025, which passed into law in February 2026, requires UK spending reviews every two calendar years. [15] These reviews will set departmental spending limits for a minimum of three financial years of the five-year forecast period, making the timetable more predictable. This frequency also makes it easier for the Scottish Government to conduct more regular spending reviews.[i]

25. Concerns were expressed regarding the Scottish Government's decision not to publish the annual MTFS in 2026. The Auditor General for Scotland stated, "given the scale of the [fiscal] challenge, it would have been better if an MTFS had been prepared this calendar year - one of the key documents that allows the Parliament to question and challenge ministers' tax and spending plans". [16]

26. The IFS suggested that the Scottish Government should instead publish an update to the FSDP to report progress against key workforce reductions and efficiency targets for each portfolio, either in the planned September fiscal statement or alongside the Scottish Budget. The IPPR also considered this suggestion "entirely reasonable". [17]

27. On 21 September, the Committee wrote asking the Cabinet Secretary to publish an FSDP update alongside the Scottish Budget on 3 December and to confirm the timing of the fiscal statement. [18] In her response, the Cabinet Secretary said she

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[i] The Scottish spending review 2026 was the first full spending review in Scotland since 2011.

was "currently considering the supporting publications" for the 2027-28 Budget and would consider the Committee's suggestions before finalising her decisions. She referred to forthcoming parliamentary appearances and debates but made no mention of a fiscal statement. [19]

28. The Committee further pursued the reasons for not providing an MTFS or a fiscal statement when hearing from the Cabinet Secretary on 30 September. [14] She suggested it would be unhelpful to use March forecasts from the Office for Budget Responsibility which predated the Middle East conflict, that a change in UK Prime Minister and Chancellor could alter the UK Government's spending approach, and that alternative publications could be used for scrutiny[ii].

29. **While the Committee recognises that the opportunity to publish an MTFS before the end of the year has now passed, we were not satisfied with the Cabinet Secretary's explanation for not providing the document in 2026. As set out in our letter of 21 September, our expectation is that the MTFS will be routinely published on an annual basis from 2027 onwards. We would also appreciate more candour if commitments, such as making a fiscal statement, are not to be met.**

30. **The Committee reiterates our request for the Scottish Government to publish an update to its FSDP alongside the Scottish Budget 2027-28, detailing the progress made towards bridging the fiscal gap, through each of the three pillars in the FSDP.**

31. **The Committee notes the UK Government's commitment, approved by the House of Commons, to hold UK spending reviews every two years.**

Transparency of budgetary information

32. While improvements in recent years regarding the transparency of budgetary information were highlighted by a number of witnesses, there were also calls for greater progress across a number of specific areas of the budget.

33. The Committee heard from the SFC that "the improvement in data over the past 10 years and in the ability to get it in Scotland has been quite significant", highlighting an example of "excellent work" by the Scottish Government and Social Security Scotland to obtain robust data on social security. It further noted that the Scottish Government has made good progress by baselining routine in-year budget transfers directly into the budget, making year-to-year comparisons easier, but more work on this is needed. [20]

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ii Such as the Scottish Fiscal Commission's September fiscal update, the 2025 MTFS and Scottish spending review document published in January 2026.

34. Professor Bell agreed with this position, noting "ultimately, you want the budget to reflect what money is being spent on what service". Using local government as an example, he said that while a substantial portion of its budget is spent on social care, this is not obvious by looking at the main 'local government' budget line. [17] Similarly, the IFS highlighted regular transfers in-year to move health funds, where the policy lies, to education to pay for training of health professionals, making it difficult to track in the budget. [17] Making similar points, CIPFA called for more transparency so "we could look at the situation from a much more holistic perspective, which would be helpful". [11]

35. The Cabinet Secretary suggested that "there is an opportunity through the budget to reset some of the work on the transparency angle, and I would welcome the Committee's views on how you might want data to be shared in that regard". [14]

36. **The Committee welcomes the progress made by the Scottish Government in recent years to improve the presentation of budgetary information, which has enhanced transparency and supported more effective scrutiny.**

37. **In the first instance, we call on the Scottish Government to take the opportunity in its first Scottish Budget of the parliamentary session to baseline all regular in-year transfers, to better support the tracking of budget lines and provide a true picture of Scotland's public finances.**

Impact of public service reform on the Scottish Budget

Overview

38. The Scottish Government aims to achieve £1.5 billion in cumulative efficiency savings over the three-year period from 2026-27 to 2028-29, including £563 million in 2026-27. A significant element of these savings is to come from NHS Boards which are expected to deliver 3% recurring efficiency savings annually. The Scottish Government also aims to reduce the public sector workforce by an average of 0.5% each year between 2025-26 and 2029-30 and to reduce corporate costs within the Scottish Government and public bodies by £1 billion over five years.[iii]

39. During our inquiry, the Scottish Government published proposals to replace the 14 territorial NHS boards with two large strategic boards and explore reducing Scotland's 32 local authorities to six. [21] Due to timing, our inquiry did not include scrutiny of these proposals. We note however that initial comments from COSLA mirrored those of public bodies regarding wider reform, including that restructuring should be driven by improved outcomes rather than reduced funding, developed "from the bottom up, not the top down", and supported by upfront investment where required. [11]

40. The broader evidence we received showed widespread support for public service reform in principle. However, concerns were raised about whether the savings are deliverable or realistic within the timescales proposed. The IFS noted that NHS boards had already missed less-demanding targets [17] and the Scottish Trades Union Congress (STUC) warned that reform risks becoming a disguise for spending cuts [11] .

41. A common theme raised in evidence was the lack of detail on the Scottish Government's efficiency and workforce targets and whether spending, workforce and savings figures are moving in the intended direction. Indeed, the SFC [20] and the Federation of Small Businesses (FSB) [8] each highlighted that the public sector workforce had increased in 2025-26. The SFC suggested that clarification be sought from the Government on whether this reflects a planned short-term increase ahead of future reductions in line with its targets. [20]

42. We heard that the Scottish Government should "set out progress on the planned efficiencies, developments on public sector pay and workforce, and how the spending pressures it faces have changed since the spending review in January 2026", ahead of the Scottish Budget. [20] The Committee was also told that more clarity is needed on the definition of 'front-line workers' who would be protected from workforce reductions and the implications of those reductions on public service delivery.[iv]

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iii As set out in the Scottish Government's Scottish spending review, FSDP and public service reform strategy.

43. Both the Scottish Council for Voluntary Organisations (SCVO) [11] and Enlighten [17] stressed that the third sector and local communities should help design reform rather than be consulted towards the end of the process. They also argued that sustainable funding, local flexibility and community-level delivery were essential to better outcomes.

44. The Committee heard from COSLA that, despite already making substantial savings, councils remain committed to reform and workforce change. [11] Local government witnesses pointed to practical examples of sharing services across councils where this suits local circumstances, such as national procurement arrangements through Scotland Excel, as well as insurance and administrative services. [11]

45. Police Scotland's experience has also shown that structural reform and digital transformation can generate substantial efficiencies, including savings of £2.5 billion of expenditure. 2.2 million hours had also been saved through its digital evidence-sharing programme. [11]

46. During evidence, the Cabinet Secretary described the Scottish Government's efficiency targets as ambitious but not unrealistic and pointed to public body consolidation, estates rationalisation and digital delivery as potential sources of savings. She, however, acknowledged that workforce reduction plans are currently "off course", with headcount higher than the planned trajectory. She said the Government would therefore need to reset its approach while continuing to protect priority front-line services. [14]

47. The Cabinet Secretary went on to say that clearer reporting on delivery against savings targets is "a fair ask" and undertook to consider how progress should be communicated to Parliament. [14]

48. **The Committee recommends that the updated FSDP to be provided with the Scottish Budget includes details of progress in delivering the Scottish Government's efficiency savings and workforce reduction targets, to enable Parliament to identify quickly whether milestones for delivery are being met. We would welcome six-monthly updates thereafter to support ongoing scrutiny of the fiscal risks to the Scottish Budget.**

49. **In the meantime, we also request details of the actions the Scottish Government plans to take to "reset its approach" to meeting its workforce reduction targets given recent rises in headcount.**

50. **The Committee seeks clarification on the Scottish Government's definition of 'frontline' and 'back office' workers under this policy.**

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iv Written submissions from Fraser of Allander Institute, UNISON Scotland, Scottish Women's Convention, and Colleges Scotland.

51. **We further ask for details of how Scottish Government is measuring the impact of workforce reductions on public service delivery.**

Public sector pay

52. The Scottish Government's public sector pay policy was described by several witnesses as being intertwined with its targets on workforce reductions because challenges meeting one would automatically impact the other. For example, a higher pay bill could require additional workforce reductions to meet savings targets.[v]

53. Both the SFC [20] and Professor Bell [17] noted that public sector pay makes up around 55% of the resource budget and that Scotland has both a larger public sector workforce and more generous pay awards than elsewhere in the UK. The SFC warned that higher-than-expected inflation means public sector pay settlements are likely to cost more than was budgeted for, creating additional pressure on the 2027-28 Budget. [20]

54. The Committee asked the Cabinet Secretary whether the Scottish Government intends to publish a public sector pay policy alongside the Scottish Budget this year, as the policy was not published every year last session prompting concerns about a lack of transparency. [14]

55. The Cabinet Secretary explained that the Scottish Government would review its public sector pay policy as the current three-year cycle comes to an end. She explained that she is currently taking advice on whether an updated policy would be published alongside the 2027-28 Scottish Budget and said future decisions would be informed by the UK Government's Budget in October. [14]

56. **The Committee urges the Scottish Government to publish a public sector pay policy alongside the 2027-28 Scottish Budget to ensure there is transparency around the size of the pay bill, and how it might impact on workforce reductions and spending on other areas.**

Prevention

57. Prevention is one of the three main pillars in the Scottish Government's public service reform strategy. [22] A Prevention Unit within the Scottish Government has recently been established to lead this work, including a prevention toolkit [23] and preventative budgeting tool[vi] which has been piloted and is expected to be incorporated into the Scottish Budget 2027-28. The Prevention Unit has also published a definition of prevention, which it states, "has been designed to build on

v Scottish Fiscal Commission and Fraser of Allander Institute written submissions.

existing definitions used in Scotland and other jurisdictions with a focus on meaningfully categorising different types of prevention activity". The definition has two components—

- an overarching definition of prevention – to distinguish what activity can be considered preventative as opposed to other types of activity (e.g. responsive activity), and
- levels of prevention – If an activity is preventative, it is assigned a level based on whether it aims to stop a problem (called "primary prevention"), address early emergence of a problem ("secondary") or stop an existing problem from escalating or recurring ("tertiary"). [24]

58. There was strong support for the Scottish Government's focus on prevention in its public service reform programme, with many witnesses arguing that Scotland's fiscal problems cannot be solved without shifting resources towards prevention. The challenges of investing for long-term benefits while meeting immediate financial pressures were also raised, although it was recognised that some preventative interventions, like vaccines, can deliver benefits quickly. [7]

59. CIPFA suggested that the central challenge is to "break down funding and structural boundaries" and create the capacity to invest in prevention alongside current service delivery". [11] Enlighten also noted that shifting resources to prevention requires a discussion about "what will we stop doing?", adding "too often, that conversation is being ducked". [17]

60. The Committee heard from a range of organisations about how their work aligns with the prevention agenda. For example, the Chartered Institute of Housing in Scotland (CHIS) highlighted the preventative value of housing across education, employment, health and wellbeing, while noting that these benefits can often be harder to quantify than the direct cost of building homes. [11] SCVO stressed that the third sector is central to prevention but is constrained by rising demand, stagnant or reduced funding and short-term funding cycles [11] , while CPAG noted "there is no better example of preventative investment and spending than investing to reduce and eradicate child poverty" [11] .

61. We also heard about different models relating to preventative spending. While the Scottish Government uses a Prevention Toolkit, Enlighten recommends three tests to determine if spending is genuinely preventative, suggesting this model could better support broader transformation that shifts power to communities. [17] Public Health Scotland endorsed Enlighten's model [11] .

62. There were mixed responses from witnesses to the Government's preventative budgeting tool, with some witnesses questioning whether it will be sufficiently specific or capable of reducing the fiscal gap this decade. [7] Others, like IPPR, recognised that the tool "signals a degree of seriousness that perhaps was not there in the past" [17] and Scottish Care told us it "offers the transparency that the

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vi This tool provides a way of identifying spend within an organisational budget and following a structured approach to budget tag spend as preventative, and at what level.

system so badly needs to help us to follow the flow [and] enables us to take that longer-term plan that the system so badly requires" [11] .

63. Witnesses such as Public Health Scotland called for barriers between services to be removed and for a stronger "shared endeavour" across organisations working locally and nationally. [11] Colleges Scotland also highlighted the importance of breaking down "the silos in the Scottish Government", adding "we need to start looking at how that cross-portfolio approach works not only for [the college] sector but across them all". It went on to say that "we have four clear Government priorities, including poverty and the climate emergency; the start point for each portfolio should be the consideration of how its spend contributes to meeting those priorities". [11]

64. The Cabinet Secretary highlighted a "slimmed-down Cabinet" and said, "we have budget lines that have moved together for the first time, so I see an opportunity for us to better understand the preventative story between and across portfolios as a result of different areas merging". She also spoke about the Scottish Government's plans on preventative budgeting and argued that progress on prevention could help deliver the savings required through the public service reform programme. [14]

65. **The Committee welcomes the Scottish Government's prioritisation of prevention as a core pillar of its public service reform strategy. We look forward to using the new preventative budgeting tool during scrutiny of the 2027-28 Scottish Budget to assess how longer-term preventative outcomes are being measured.**

66. **We ask the Scottish Government to set out how it will take the opportunity of a smaller Cabinet and merging budget lines to direct spending towards preventative activities that deliver its cross-portfolio priorities of child poverty, climate change, economic growth and public services.**

67. **The Committee seeks further information on how the Scottish Government is working with public bodies and local authorities to create the capacity to invest in prevention against competing financial pressures, and to work collaboratively towards achieving preventative outcomes.**

Invest to save

68. The 2025-26 and 2026-27 Scottish Budgets have each included around £30 million for an 'invest to save' fund for reform projects that will deliver ongoing savings and support the delivery of the public service reform strategy.[vii] It is unclear whether this fund will continue into 2027-28.

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vii Scottish Budgets 2025-26 and 2026-27 .

69. The Committee heard that genuine public service reform will require upfront investment. The STUC warned that, without it, reforms would amount to cuts rather than sustainable service redesign [11] , a view echoed by SFE which said, "invest to save has to be part of the agenda" [8] . SFE explained, "you will hit a limit in how much you can save by simply being more effective and efficient, and you will have to invest in technology and artificial intelligence to change the way in which you deliver services to achieve a lower unit cost to address the increasing demand in certain parts of the public sector". [8] Police Scotland also highlighted that rising and increasingly complex demand had absorbed much of the capacity created through police reform, and further transformation in digitalisation and technology now requires investment. [11]

70. The Cabinet Secretary confirmed that portfolios are expected to identify and manage any up-front reform costs, supported where appropriate by the Government's invest-to-save fund. [14]

71. **The Committee seeks further details of how the Scottish Government has assessed value for money and outcomes arising from the projects it has supported through the invest to save fund to date.**

72. **The Committee believes there is a risk that without some form of upfront investment to support public service reform, the aims of transformational change and improved service delivery will not be achieved. We therefore ask that consideration be given to extending the invest to save fund into 2027-28.**

Outcomes

73. The national performance framework provides "a long-term, shared vision and direction to improve the wellbeing of people living in Scotland now and in the future". [25] It includes national outcomes and national indicators to measure progress against those outcomes. The Scottish Government has indicated it will finalise and launch a revised framework "soon". [26]

74. Evidence we received during pre-budget scrutiny suggests that policymaking and budgetary decisions are still focused on inputs rather than outcomes. For example, Enlighten told us that "the whole discussion [on reform] is still very much about the inputs […] but there has been nothing about how changing those structures lead to better output". It went on to say, "I have not seen anything that talks about how having two health boards is going to help somebody get to their GP, get an appointment, go through the waiting list", etc. [17]

75. Professor Bell argued that understanding the outcomes that people want and measuring them clearly is crucial to ensuring that the budget delivers the services they want "as efficiently and effectively as possible", but "we are not all that good at

doing that". [17] Enlighten made a similar point, commenting that budgeting is currently treated as a reactive exercise in cost-cutting rather than starting with communities' needs. [17]

76. **The Committee seeks clarification of when the updated national performance framework is being published and how it will be embedded within budget formulation to ensure spending decisions are driven by outcomes.**

Economic growth

Capital funding

77. The SFC confirmed that "the capital budget is already under significant pressure [and] is projected to decline in real terms", with the Scottish Government's planned investment currently exceeding the funding available by around £2.1 billion by 2029-30. It estimated that increased defence spending by the UK Government will further reduce Scotland's capital budget by £87 million in 2027-28. [2]

78. The SFC further noted that the Scottish Government's ability to offset future real terms falls in the capital block grant through borrowing is "now more limited" and that, "while the Government could borrow more in any one year, it would mean reaching the overall capital borrowing limit sooner". The Scottish Government plans to use bonds to fund some capital projects from 2027-28 [27] , an issue which is explored later in this report along with other fiscal flexibilities.

79. The Scottish Government held a consultation on its Infrastructure Strategy 2027-2037 between January and May 2026. The Strategy, aimed at guiding infrastructure planning, investment, and delivery across Scotland, is scheduled for publication later in 2026. [28]

80. The Committee explored with witnesses the uncertainty surrounding Scotland's capital funding position, due in part to its dependence on UK Government decisions. The SFC noted that "historically, more money has flowed through [to the Scottish Budget] as we move through a spending review, but there is no guarantee of that". It warned that further pressure on Scotland's capital budget could arise given higher-than-expected borrowing costs, tight fiscal rules and increased defence spending, which it described as "a potential risk for the Scottish Budget in the next few years". [20]

81. Witnesses emphasised that the economic value of capital spending by the Scottish Government depends on how it is targeted. For example, the Royal Society of Edinburgh (RSE) suggested that economic growth can be supported through investment to enhance public sector efficiency or expand infrastructure. [17] The IPPR argued that "some public investment in port and transport infrastructure would definitely help to leverage in private sector investment", while "there is a social need for housing, but there is also an economic imperative". However, it went on to say that the delivery of infrastructure projects and their benefits are likely to emerge over the longer term rather than contribute to closing the fiscal gap during the current parliamentary session. [17]

82. The Cabinet Secretary told the Committee that capital funding could fall by £370 million in total by 2029-30 due to UK Government reprioritisation of departmental spend to its defence investment plan, adding "it will be challenging". [14]

83. **The Committee seeks an update on when the Scottish Government will**

publish its Infrastructure Strategy 2027-37 and how it will lever in the private investment needed to fund capital projects that best support economic growth.

Skills and employability

84. The Committee heard that investment in people is a critical driver of economic growth, including education, skills development, lifelong learning, workforce development and employability support. Universities Scotland further highlighted that Scotland's demographic outlook from 2030 means that growing the tax base in future will depend on the ability to increase participation in learning, work and reskilling throughout people's lives. [7]

85. The IFS noted, "essentially we want workers to be trained as well as possible and to be matched to the best jobs that they can [as] having such a match in the labour market is a key driver of productivity, […] and having a dynamic economy is part of growing the economy and the tax base". [17]

86. However, the Committee heard that Scotland's colleges face a significant decline in students, with 40,000 fewer students in learning than two years ago, and "a 7.5% real terms funding cut which threatens the viability of the sector and future workforce training capacity". Colleges Scotland told the Committee that "a flat-cash settlement would be a catastrophe", adding "the irony is that, at the very point that Scotland needs its colleges to train up the workforce for the future—and, as the independent research shows, to prevent people from falling into poverty—they are at huge risk". [11]

87. Professor Bell estimated that "the rate of NEETs[viii] in Scotland is not that much different from the rate in the UK as a whole, which means that about 13.5% of 16 to 24-year-olds are not in education, employment or training". He noted "we know from past experience that people who do not have a good entry into the labour market when they are young tend to suffer throughout their careers [and] therefore, […] the provision of services to that group seems to be incredibly important, because they are the potential taxpayers of the future". [17] SFE also referred to statistics showing that some young people leave Scotland because they cannot get places at university, and that most of those students do not return to Scotland when they leave university, adding this 'talent drain' is a challenge. [8]

88. The STUC called for discussions between the Scottish and UK governments on further devolution of powers relating to employability to help support labour market participation in a joined-up way alongside colleges and other bodies that support skills development. [11]

89. The FSB welcomed confirmation of the apprenticeship accelerator grant in the recent Programme for Government. It stressed that this grant should be focused on smaller employers rather than as a subsidy to large employers as "that will have the

viii NEETs stands for Not in Education, Employment, or Training.

biggest impact because […] small businesses tend to recruit from the local labour market and from people furthest from the labour market". The FSB further called for "a real budget for the business base: to be about expanding, broadening and strengthening the economic base". It cautioned against "chasing after unicorns and putting all your eggs in the basket labelled 'the next big thing'; instead, it is about thinking about the practical changes that could make it easier to set up and run a business in Scotland". [8]

90. Tax Justice Scotland, however, noted "it is vital to consider how, and for what purpose, we seek economic growth, what areas we seek it in and what we, as a society, value". It argued that key areas of social infrastructure, such as social care and childcare "need to be viewed in terms of both what they provide to society and their role in supporting economic growth". [8]

91. The Cabinet Secretary noted strengths in Scotland's economy, including growth in the last financial year that was 0.1 percentage points higher than in the UK, above-average monthly pay and a lower claimant count rate. She acknowledged the challenges posed by the wider economic outlook. [14]

92. She also highlighted data showing that more young people are going on to positive destinations along with the Government's commitment to increase the number of apprenticeships during this session of Parliament. She however noted "our approach to the economy needs to better reflect" many of the challenges young people face, including the housing market. [14]

93. **The Committee is concerned about the number of young people in Scotland and across the UK who are not in education, employment or training, notwithstanding the latest figures on young people going on to positive destinations.**

94. **We recommend that the Scottish Government steps up efforts to further expand the number of young people moving into positive destinations, to provide better futures for individuals, support economic growth, and grow the tax base.**

95. **The Committee seeks details of how the Scottish Government will support colleges and universities to match training and skills to Scotland's jobs of the future, as part of growing the economy and the tax base.**

96. **We request clarification on whether the apprenticeship accelerator grant is solely aimed at small businesses, which we were told would make most impact on increasing apprentice numbers within local communities.**

A strategic approach to tax revenues

Overview

97. The Scottish Government published Scotland's Tax Strategy: Building on our Tax Principles in December 2024, which set out "the next steps in the evolution of the tax landscape in Scotland, expanding on our Framework for Tax published in 2021". [29]

98. The Committee heard different perspectives from witnesses on what the Scottish Government's approach to taxation should be, with some making the case for progressive reform and maximising revenue generation, and others supporting the use of taxes to encourage economic growth and broaden the tax base. [8]

99. For example, CPAG argued that the Scottish Government should "make better use of the Parliament's devolved tax powers in order to harness the wealth and resources Scotland has". It advocates building on what it sees as a progressive approach on income tax in Scotland to fund delivery of statutory child poverty and net zero targets, calling for "a real conversation" about broader-based income tax rises. [11]

100. Future Economy Scotland takes a similar position. It proposes "four specific revenue-raising reforms": (1) replacing council tax and land and buildings transaction tax with a progressive property tax, (2) replacing non-domestic rates with a land value tax, (3) introducing a 'betterment levy' on planning decisions that change the denomination of rural land to buildable land, and (4) raising income tax. The income tax changes "would mean asking for a bit more from median earners, but, in exchange, it would fund stronger public services and ensure that Scotland can continue to deliver its proud social contract". [8]

101. In contrast, SFE suggested "we need to take a step back and look, given the devolved powers that we have, more holistically at what a tax strategy for Scotland that would stimulate economic growth and attract more well-paid jobs to Scotland would look like", adding "we should not simply be taxing the existing economy more". It further noted "from an investor point of view, it is not necessarily the rate of the tax but it is stability that is more important", and this is not currently present in Scotland or the UK. [8]

102. Several witnesses raised concerns about the complexities in the Scottish income tax system, including how it interacts with UK taxes and benefits. The IFS and Professor Bell highlighted the high marginal tax rate that employees earning between £43,000 and £50,000 pay as they are subject to the higher rate of national insurance contributions. Professor Bell suggested that this is "extremely punitive", noting that "when you combine [the income tax schedule] with national insurance, it looks like a camel with two humps". The IFS suggested "easing those distortions would support more economic activity, which would be good as a whole, period, even if it did not raise any more tax revenue, because people would be better off on average". [17]

103. In addition, the Chartered Institute of Taxation (CIOT) suggested that if the interactions between the income tax system in Scotland and the UK benefits system, particularly universal credit, were considered, it could lead to greater "participation lower down the income scale, which would potentially increase the tax base". [8]

104. There was some agreement amongst witnesses about the need for reform of other taxes. Both the FSB and SFE support reform of the non-domestic rates system, raising concerns about the current rateable value and how it is calculated, reliefs and how they are applied to the final bill, and the large number of assessors using different practices. [8]

105. Concerns were also raised regarding property taxes, with Professor Bell highlighting "we now have LBTT, council tax, mansion tax and, in some parts of the country, a second home premium; that […] is creating very strange incentives that are not consistent with improving economic activity overall in the country—obviously, some of that applies to the rest of the UK as well". [17]

106. Witnesses also argued that tax policy should be considered alongside wider economic objectives and not solely as a mechanism for raising revenue. Several contributors called for a clearer long-term tax strategy that supports competitiveness, investment, and sustainable growth in the tax base. [7] The Association of Taxation Technicians argued against making individual modifications such as new tax bands or minor adjustments to council tax, urging the Scottish Government to build cross-party consensus for fundamental structural reform. [30] CIOT commented on the absence of a regular legislative mechanism for maintaining and amending devolved tax legislation. [8]

107. The Cabinet Secretary confirmed that "the Government's approach to progressive taxation is rooted in the idea of the social contract, which means that people in Scotland benefit from a variety of different services that they would not be able to access if they lived in other parts of the United Kingdom". [14]

108. **The Committee asks the Scottish Government to update its tax strategy to provide a strategic and co-ordinated approach to raising revenues, rather than creating individual taxes in isolation.**

Behavioural responses to tax policy

109. The Committee explored with witnesses the impact of behavioural responses on tax revenues. Asked whether the Scottish Government's income tax policy has tipped over the Laffer curve[ix], the SFC noted "we would say that is not clear" [20] . However, some witnesses, such as SFE suggested "we have reached that point of the Laffer curve—if not beyond it", highlighting experience of behavioural change in the financial sector. It noted "given that our sector is growing at 3% to 3.5% a year, we think that further growth could be attained, but the tax regime is acting as a barrier to that, to a degree". [8]

110. CIOT also highlighted anecdotal evidence that tax is affecting decisions on whether "to take on extra work or accept higher pay". However, while use of increased pension contributions "is a definite thing", […] evidence on the use other behavioural options is more anecdotal and we do not have the actual data to support that". [8] The FSB further noted "we do not have good, reliable, up-to-date data on any sort of behavioural impact", while also highlighting that most of its members are basic-rate taxpayers who are "rooted in the community". [8]

111. It was also recognised that tax is one of several factors people consider when deciding whether to stay in or move to Scotland.[x]

112. The IFS noted that future tax policy should consider forthcoming HMRC reviews of behavioural responses, adding, however, each study should be viewed alongside wider evidence on how people respond to tax rates. [17]

113. Asked about potential behavioural responses from higher rate taxpayers paying more income tax than in England, the Cabinet Secretary said that "if we were to raise the higher rate threshold to the level that it is in England, that would cost us more than £800 million in this financial year alone". The Cabinet Secretary also acknowledged that behavioural change is "difficult to quantify". [14]

114. A Scottish Government official explained that "the nature of the data reporting for income tax—the self-assessment forms and so forth—mean that there is a significant data lag, which affects our ability to look at income tax data for the current year and work through the behavioural-change effects". She highlighted that the latest HMRC analysis on Scottish income tax and behavioural change involving evaluation of 2023-24 behavioural data is expected to be available "soon". [14]

115. **The Committee heard anecdotal evidence of negative behavioural responses to some of the Scottish Government's tax policies, in particular income tax. We also note the SFC's view that it is not clear whether the 'tipping point' of the Laffer curve has been reached.**

116. **While we recognise the delay in data reporting, we firmly believe that tax policy should be informed by accurate and up-to-date evidence of behavioural change.**

117. **In the first instance, the Committee looks forward to considering HMRC's analysis of behavioural responses to Scottish income tax in 2023-24 once published. We also ask the Scottish Government to explain how it will use this and future HMRC analysis to develop a more robust understanding of behavioural change to inform future tax policy.**

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ix The Laffer curve is an economic theory suggesting there is an optimal tax rate that maximizes government revenue without deterring productivity and economic growth.
x Various witnesses at 16 September 2026 Committee meeting.

Council tax reform

118. Many witnesses told the Committee that a priority for the Scottish Government should be council tax reform to match rates with actual property values across different parts of Scotland. For example, the IFS told the Committee that "with council tax, the system is now so bad that, in some sense, it is hard to imagine how a new system could be worse". [17] COSLA argued that "a review of council tax is absolutely critical" [8] and CIPFA agreed that "reform of council tax is urgently needed, because it is an outdated and unfair tax that is regressive in nature and that disproportionately impacts those on lower incomes". [8] Tax Justice Scotland supports a shift away from the current system for similar reasons. [8]

119. Witnesses also recognised that reform has proved politically challenging and that a sudden update to property values could cause council tax bills to soar overnight for some people. [8]

120. Some witnesses put forward suggestions for how to overcome some of these challenges, including the IFS which argued that a transitional relief could be introduced to phase in updated values slowly over time, similar to non-domestic rates. [17] We also heard from Professor Bell that the focus should be on fixing geographical unfairness where "some parts of Scotland have suffered economically relative to others that have prospered". [17]

121. COSLA told the Committee that "local tax reform should […] be considered as part of a wider approach to fair, sustainable and locally accountable public finance, rather than in isolation". It pointed to a joint working group with the Scottish Government on council tax reform which recently reported its findings, and plans to introduce two new higher-rate council tax bands through a Bill to be introduced later this year, as some progress with reform. [17] CIPFA stated that "it is vital that local government finance is included as part of the local authority reorganisation process". [17]

122. Asked to clarify how local taxes would work in a new model following local authority reorganisation, the Cabinet Secretary responded, "there are opportunities, through the consultation period, to listen and engage on those matters". She added that work is already underway including on the 'mansion tax' and "I am very open to working across parties on reform". [14]

123. **The Committee welcomes the joint working group between the Scottish Government and COSLA on the future of council tax reform and seeks clarification on next steps with this work following recent publication of the consultation findings.**

124. **We also seek assurances that local taxation will be considered as a key part of the recently announced local government reorganisation process. We further suggest that research is commissioned of local taxation models used in other comparable countries to inform final decisions.**

Additional fiscal flexibilities

Scotland's fiscal framework

125. Scotland's fiscal framework agreed between the Scottish and UK Governments sets out the funding arrangements, borrowing limits, and budget management flexibilities in relation to the Scottish Budget. [31]

126. First agreed in 2016, the fiscal framework was reviewed in 2023, when some flexibilities were updated and uprated for inflation.[xi] The framework provides resource borrowing powers for in-year cash management and forecast error and capital borrowing powers to invest in infrastructure, both within specified annual limits and cumulative caps. It also includes a Scotland Reserve to enable the Scottish Government to carry forward underspends or revenue surpluses between financial years to smooth out tax or spending volatility. A further review of the fiscal framework is due in 2028, and the Scottish Government has confirmed that it is currently in discussions with the UK Government regarding the scope and nature of the review. [32]

127. Witnesses welcomed the changes made as part of the 2023 review. They now consider that some additional fiscal flexibilities are needed for the Scottish Government to manage its Budget effectively, given its increasing size and the risk of forecast errors and subsequent reconciliations. The SFC for example said, "as the Government takes on more risk and as revenues rise, there is a genuine question about whether the Government's flexibilities to manage that are still as robust as they need to be". [20] The SFC also suggested that "it is worth looking again at whether the annual borrowing limits make sense". [20]

128. Other suggestions included giving the Scottish Government some flexibility to overspend slightly, which the SFC noted was "just good budget management" for a Budget of £60 billion. The SFC further suggested that the review should look at how more funding flexibility could be built in over a longer period, including through multiyear funding deals. [20]

129. The Committee explored with witnesses the reasons for forecast error and the extent to which this could be minimised in the future, given the £720 million reconciliation in the 2027-28 Scottish Budget. [33] It was noted that divergence in the forecasts of the SFC and Office for Budget Responsibility particularly relating to earnings growth had led to larger reconciliations in recent years and that this pattern was likely to continue as income tax revenues grow.[xii]

130. The SFC highlighted that although the reconciliation for the 2027-28 Budget "sounds like a big number, it is relatively small compared with £18 billion in income tax revenues, whereas, 10 years ago, when the [fiscal] framework was first set, revenues were £8 billion". [20]

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xi Using the Office for Budget Responsibility GDP deflator.

xii Scottish Fiscal Commission, Institute for Fiscal Studies, and Professor David Bell.

131. Professor Bell also questioned the Scottish Government's approach of spending positive reconciliations on long-term commitments and recurring expenditure such as pay awards. He described this practice as "a dangerous path to go down", because the Government would have to find the money from elsewhere in the Budget when the reconciliations became negative. [17]

132. The Cabinet Secretary described the £720 million reconciliation in 2027-28 as "a normal feature of the fiscal framework" and said it demonstrated the fragility of Scotland's finances and the difficulty of managing forecast volatility. She argued that the fiscal framework is "fundamentally flawed" and disproportionately weighted towards London and the south-east of England. She also identified improved information-sharing between the Scottish and UK Governments as a priority for the review, to support better planning, fiscal sustainability and a longer-term approach to the public finances. [14]

133. The Cabinet Secretary went on to say that the review should seek to create a more balanced approach that recognises the differing strengths and circumstances of economies across the UK and asked the Committee to contribute its views on priority areas to be considered as part of the review. [14]

134. **The Committee welcomes the forthcoming fiscal framework review as an opportunity to ensure that the Scottish Government's fiscal flexibilities reflect the growing scale of the Scottish Budget and the associated risks.**

135. **The Committee heard evidence suggesting that additional fiscal flexibilities should be sought within the fiscal framework. We will take further evidence in the coming weeks to inform our response to the Cabinet Secretary on priority areas for the scope of the review.**

ScotWind funds

136. The Scottish Government raised ScotWind revenues amounting to £755 million through the leasing in 2022 of Scotland's seabeds to companies to build offshore wind farms. These one-off funds were originally earmarked for environmental or climate activities. [34] The Scottish Government committed in its Programme for Government 2026-2031 to develop a ScotWind Wealth Fund by the end of the Parliamentary session, "ensuring investment that brings a fair return to the public purse and that all of Scotland receives the benefits our renewable energy resources can offer". [35]

137. The SFC noted that the Scottish Government could supplement its capital budget through borrowing and ScotWind revenues, although these sources are limited and non-recurring funds. [20]

138. The Committee heard from witnesses that the Scottish Government has tended to use ScotWind income as a budgetary management tool to smooth spending and

manage fiscal volatility, effectively using it as a second reserve. Some ScotWind funds have been allocated in each Scottish Budget to "balance the books", with the commitment not to use the money should additional funds become available.[xiii]

139. The SFC confirmed that Scottish Ministers drew down £96 million of the ScotWind funds in 2022-23 and expects to spend a further £80 million this year and £328 million in 2027-28. It added that "there was a plan to use [this] money in [2023-24, 2024-25 and 2025-2026], but the Government did not do that, which is the second reserve element". [20]

140. The SFC explained that "the principle of trying not to use one-off revenues for day-to-day spending is good practice anywhere", while also recognising that the Scottish Government faces difficult choices given its limited borrowing powers. [20] The Auditor General for Scotland recently stated that the Scottish Government needs to be "much more transparent about their plans for how the ScotWind funds will be used across this parliamentary term and beyond" including on the purpose and operation of the ScotWind Wealth Fund. [36]

141. The Cabinet Secretary agreed that ScotWind "probably does currently work as a second reserve" and described it as another lever for managing volatility given the Government's limited borrowing powers. She noted that the Scottish spending review assumes some ScotWind contribution because of the scale of current financial challenges. [14]

142. The Cabinet Secretary confirmed that the Government's longer-term aspiration is to develop a wealth fund to "protect that budget for the next generations" and use the proceeds to support renewable-energy innovation and investment. [14]

143. **While the Committee understands the challenges in balancing the Scottish Budget, we do not believe that ScotWind funds should routinely be used as a second reserve.**

144. **We welcome the Scottish Government's commitment to develop a ScotWind Wealth Fund in the longer term and seek further details of the purpose of this fund, how it will be used, and when it will be established.**

Bonds

145. The Scotland Act 2016 included powers to issue government bonds for capital investment. [37] In 2023 the Scottish Government's Investor Panel recommended making bonds available to market as a way of raising Scotland's international profile and attracting investment. [38] In 2025 the Scottish Government was assigned an AA credit rating by S&P Global [39] and Moody's [40] , matching that of the UK Government.

xiii Scottish Fiscal Commission, Institute for Fiscal Studies and Professor Bell.

146. The Scottish Government aims to raise £1.5 billion in capital borrowing through its bonds programme over the next five years, an alternative to drawing from the UK Government's national loans fund, although existing borrowing limits would still apply. The Scottish Government's first bonds are expected to be issued as part of the Scottish Budget 2027-28. [41]

147. Many witnesses said they support the Scottish Government's plans to explore the use of bonds. However, some highlighted a lack of certainty and transparency around potential risks, opportunities, governance arrangements, administrative costs, economic impacts, and trade-offs such as potentially higher borrowing costs versus more flexibility with repayments. [7]

148. The IPPR suggested "there is a strong case that the process of issuing bonds can help build Scottish Government capacity by extending knowledge of and engagement with financial markets, [however,] the higher costs are difficult to justify when the fiscal challenge is so pressing". [17] We also heard from the RSE that administrative costs would be "substantial" and "potentially tens of millions of pounds", however, they do not appear in indicative spending plans in the Scottish spending review 2026. [17]

149. Professor David Bell noted that while bonds can alter when expenditure is paid and who supplies the capital, they "generate a stream of future payments that must be set aside before the annual budget can be allocated". He went on to set out some advantages of domestically issued bonds, including "greater maturity flexibility, development of a Scottish institutional-investor market, potentially greater visibility among international investors, and matching long-lived assets with long-term liabilities". [17]

150. Given some of these uncertainties and potential trade-offs, the IFS suggested that the Scottish Government could carry out a trial to gauge demand for bonds, which would prevent issuing a large amount of bonds that then become undersubscribed resulting in much higher interest rates. [17]

151. The Cabinet Secretary confirmed that bonds are "about borrowing better, not borrowing more" and that the programme is intended to diversify borrowing, establish Scotland in capital markets, attract investor interest and support capital spending. She recognised the evidence heard by the Committee that borrowing through bonds could be more costly than through the national loans fund and advised that the Government will only proceed with bonds if market conditions are favourable, taking account of current volatility and the cost of borrowing. [14]

152. **The Committee notes the Scottish Government's plans to explore the option of issuing bonds as part of the Scottish Budget 2027-28. We also note the suggestion from the IFS that the Scottish Government conducts a trial to gauge demand for Scottish bonds as a way of minimising possible risks to Scotland's public finances.**

153. **In the meantime, we have sought further details of the Scottish**

Government's bonds programme in writing, reflecting some of the evidence we heard during this inquiry. We also intend to hold further evidence sessions on the keys to delivering a successful bonds programme to support effective scrutiny of the Scottish Government's planned issuance of bonds as part of the Scottish Budget 2027-28.

Conclusion

154. **The Committee recognises the scale of the pressures on the Scottish Budget, particularly in 2027-28.**

155. **The Committee however has insufficient evidence to determine whether the Scottish Government's tax and spending plans are affordable and sustainable. We are also concerned that the Scottish Budget faces substantial risks if the three pillars of the FSDP, including ambitious public service reform targets, are not delivered in full and on time.**

156. **We therefore call on the Scottish Government to provide much greater transparency on progress in closing the fiscal gap and meeting reform targets. As a first step, the Scottish Government should publish an updated FSDP alongside the Scottish Budget 2027-28 on 3 December 2026. From 2027, we expect it to resume annual publication of the MTFS and commit to regular spending reviews, given the greater predictability of the UK review cycle. We also urge it to update its public sector pay policy and tax strategy at the earliest opportunity.**

157. **We heard from witnesses that the Scottish Government needs greater fiscal flexibilities and will undertake further work on this issue in the coming weeks to inform the upcoming fiscal framework review.**

158. **Collectively, the recommendations in this report aim to strengthen fiscal sustainability and support the effective management of Scotland's public finances. We therefore urge the Scottish Government to implement our recommendations in full.**

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