Scottish Fiscal Commission

# Scotland's Economic and Fiscal Forecasts
# February 2020

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# Foreword

The Scottish Fiscal Commission is the independent fiscal institution for Scotland. Our statutory duty is to provide independent and official forecasts of Scottish GDP, devolved tax revenues and devolved social security spending to inform the Scottish Budget.

This report contains our third set of Scottish Budget forecasts, covering the years 2020-21 to 2024-25. It is also the first set of Budget forecasts we have produced where the Scottish Budget took place before the UK Budget, and in which there was not a UK fiscal event in the autumn.

Our forecasts represent the collective view of the Scottish Fiscal Commission, comprising the four Commissioners. We take full responsibility for the judgements that underpin them.

The deadline for new data to be included in our forecasts was on 15 January 2020 and our Brexit assumptions were finalised on 17 January when the economic forecast closed. The deadline for Scottish Government policy measures was on 23 January. The forecasts set out in this report were provided to the Scottish Government on 28 January. We expect to produce our next forecasts in May 2020 to support the Government's Medium Term Financial Strategy.

As with each fiscal event, our relationship with the Scottish Government evolved further as we prepared this set of forecasts and we will continue to learn from what works well and what could be improved. In producing our forecasts we have put into practice the revised Protocol agreed with the Scottish Government in September 2019.

Our forecasts rely on data from a range of providers and we are grateful for their support. In particular we would like to thank Revenue Scotland for their work to ensure that we were able to incorporate as much of their data as possible in the forecasts. We would also like to thank officials from the Scottish Government, Revenue Scotland, DWP, HM Treasury, HMRC and the OBR for their constructive challenge of our judgements and for ensuring that we considered all the available evidence.

We would like to thank once again the hard-working staff of the Commission for their support in the production of our forecasts and underpinning analysis.

Dame Susan Rice DBE

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6 February 2020

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# Scotland's Economic and Fiscal Forecasts February 2020

## Economy

| Economy | 2019 | 2020 | 2021 | 2024 | % growth |
|---|---|---|---|---|---|
| **GDP** | 0.9 | 1.0 | 1.1 | 1.2 | Growth in 2020 is supported by reduced Brexit uncertainty, while the long-term outlook remains subdued. |
| **Trend Productivity** | 0.3 | 0.6 | 0.9 | 1.3 | Productivity growth remains low in the short term, then starts to gradually increase. |
| **Nominal Earnings** | 2.8 | 3.0 | 3.1 | 3.3 | Nominal earnings growth forecasts revised up to reflect outturn data and the tight labour market. |
| **Real Earnings** | 1.0 | 1.1 | 1.0 | 1.2 | Real earnings growth expected to be positive but still low by historic standards. |

## Tax

| Tax | 2019-20 | 2020-21 | 2021-22 | 2024-25 | £ million |
|---|---|---|---|---|---|
| **Income Tax** | 11,677 | 12,365 | 12,897 | 14,722 | In 2020-21, income tax revenue is expected to be £80 million higher than our December 2018 forecast. |
| **Non-Domestic Rates** | 2,806 | 2,749 | 3,012 | 3,590 | New data reduced our forecast every year but measures in the NDR Bill increase the forecast from 2022-23 onwards. |
| **LBTT** | 613 | 641 | 666 | 749 | In 2020-21, revenue from LBTT is expected to be £39 million lower compared to our December 2018 forecast. |
| **Scottish Landfill Tax** | 124 | 116 | 110 | 66 | Delay to the ban on biodegradable municipal waste increases revenues until implemented in 2025. |
| **Policy Announcements** | | | | | |
| **Income Tax** | | 51 | 54 | 63 | The higher rate threshold has been frozen at £43,430 in 2020-21. |
| **Non-Domestic Rates** | | -7 | -7 | 0 | New Intermediate Property Rate lowers the tax rate for properties with a rateable value between £51,000 and £95,000. |
| **LBTT** | | 10 | 11 | 12 | Non-residential leases above £2 million will pay 2 per cent on the portion above £2 million instead of 1 per cent. |

## Social Security

| Social Security | 2019-20 | 2020-21 | 2021-22 | 2024-25 | £ million |
|---|---|---|---|---|---|
| **All devolved social security assistance** | 458 | 3,435 | 3,578 | 3,959 | Total spending on social security assistance devolved to the Scottish Government. |
| **Policy Announcements** | | | | | |
| **Child Disability Assistance** | | 217 | 250 | 312 | The new Scottish assistance opens for applications in summer 2020 to replace Disability Living Allowance for Children. |
| **Scottish Child Payment** | | 21 | 65 | 162 | New Scottish Child Payment launches for children under 6 in 2020, and for all children up to sixteen years old in December 2022. |

# Summary

## Introduction

1 This report contains our official economic, tax and social security forecasts along with policy costings for the changes in tax and social security proposed in the Government's Budget. Our forecasts are just one component of the Scottish Budget; we also discuss how the Scottish Budget is set and the effect of the devolution of tax and social security benefits. Within this context we provide our assessment of the reasonableness of the Government's borrowing plans.

2 The Scottish Budget continues to grow in size and complexity as more of the fiscal framework comes into operation for the first time. The Scottish Government will become responsible for a further £3 billion of social security payments from April 2020. The Government is also using its resource borrowing powers to manage the first income tax reconciliation.

3 The Scottish Budget has been set before the UK Budget has been published and there has not been an autumn UK fiscal event with its accompanying OBR forecasts. These circumstances introduce new considerations relating to the funding arrangements for the Scottish Budget including the Block Grant and Block Grant Adjustments.

4 Monitoring and management of the Budget through the course of the year will be increasingly important from 2020-21 onwards with more parts of the Budget being variable and harder to predict. As usual, during the year the Government will receive updated information on its tax revenues, the progress of its spending plans, any changes in funding from the UK Government and changes in the Block Grant Adjustments (known as reconciliations). Some of the magnitudes may be exacerbated by the Scottish Budget preceding the UK Budget.

5 The devolution of £3 billion of social security benefits from April 2020 will add to the risk of in-year spending variations given the demand-led nature of these payments. Spending will be determined by the number of eligible people who

apply for support, all of whom must be paid at the rate set in the legislation. The Scottish Government will have to meet this spending as it arises, even if it differs from the forecast used to set the Budget initially. The composition of the social security portfolio, with spending on three large payments dominating the total (as shown in Table 8), means that even modest forecast errors are unlikely to offset each other and may result in in-year spending differing from our forecasts.

6 The Scottish Government and Parliament will need to consider how best to monitor and respond to these in-year budget revisions.

7 Our next forecasts, published alongside the Scottish Government's Medium Term Financial Strategy (MTFS) currently anticipated in May, will be combined with the March UK Budget and updated OBR forecasts to provide an updated overview of the Scottish public finances.

## Fiscal Overview

### Funding arrangements for the Scottish Budget

8 A large part of the Scottish Government's funding is based on the Barnett-determined Block Grant and Block Grant Adjustments (BGAs), usually updated at the UK Budget based on the UK Government's policy and OBR forecasts. In the absence of this information, the Scottish Government has reached a number of funding agreements with the UK Government. At the same time decisions on the use of borrowing and the Scotland Reserve by the Scottish Government affect the total level of funding available for the Scottish Government to spend in 2020-21.

9 Table 1 summarises the Scottish Government's funding included in Budget 2020-21. We discuss each of these components in turn.

**Table 1: Funding and spending plans for the Scottish Budget 2020-21**

| £ million | | 2020-21 |
|---|---|---|
| Resource | Barnett-determined Block Grant – resource [1] | 29,569 |
| | SFC tax revenue forecasts [2] | 13,123 |
| | Tax and non-tax BGAs | -12,991 |
| | Social Security BGAs | 3,203 |
| | Reconciliations [3] | -207 |
| | Other [4] | 639 |
| | Total resource funding | 33,335 |
| | Resource borrowing | 207 |
| | Drawdown from Scotland Reserve | 106 |
| | Other [5] | 269 |
| | Total resource spending | 33,917 |
| Capital | Barnett-determined Block Grant – capital [1] | 4,408 |
| | Financial Transactions (FTs) [1] | 606 |
| | Other [6] | 326 |
| | Total capital funding | 5,340 |
| | Capital borrowing | 450 |
| | Drawdown from Scotland Reserve (capital and FTs) [7] | 37 |
| | Other [8] | -10 |
| | Total capital spending | 5,817 |

Source: Scottish Government, Scottish Fiscal Commission.
The table does not include non-cash budget. Figures may not sum because of rounding.
All components of the Budget will vary in 2020-21 reflecting changes to the Barnett-determined Block Grant following changes in UK Government spending, changes in our forecasts of tax revenues, changes to the BGAs, and changes in the Scottish Government's plans for borrowing and the use of the Scotland Reserve.
[1] Agreed with HM Treasury based on September 2019 Spending Round.
[2] Scottish Fiscal Commission tax revenue forecasts cover income tax, Land and Building Transaction Tax, and Scottish Landfill Tax. Non-Domestic Rates are not included in the revenue forecasts as these are used separately to set the distributable amount for Non-Domestic Rates.
[3] Includes final reconciliations for: 2017-18 income tax revenue and BGA (-£204 million), 2018-19 Land and Building Transaction Tax BGA (-£3 million), 2018-19 Scottish Landfill Tax BGA (-£2 million), 2018-19 fines, forfeitures and penalties (FFFPs) BGA (£2 million), 2018-19 Carer's Allowance BGA (£0 million).
[4] Includes Pillar 1 Farm payments (£472 million), anticipated Barnett RDEL consequentials (£142 million), and Scottish Government's forecast of revenues from FFFPs (£25 million).
[5] Includes Rail Resource Grant (£80 million), fiscal framework administration costs (£66 million), Migrant Surcharge (£22 million), In-Year Reconciliations deferred from 2019-20 (£30 million), deferred consequentials from 2019-20 Supplementary Estimates (£58 million), Queen's and Lord Treasurer's Remembrancer (£5 million), and Machinery of Government Transfers (£8 million).
[6] Anticipated Barnett CDEL consequentials, (£326 million).
[7] Includes planned drawdowns of £5 million for general capital spending and £32.2 million for FTs.
[8] Includes Glasgow City funding (£15 million) and repayment of Financial Transactions to HMT (-£25 million).

## Barnett-determined Block Grant

10 The Scottish Government receives funding from the UK Government based on the UK Government's spending announcements. This is known as the

Barnett-determined Block Grant. While these spending announcements are normally in the UK Budget, the Scottish and UK Governments have agreed to base the Barnett-determined Block Grant on the commitments made in the UK Government's September 2019 Spending Round.[1]

11 As usual, we expect the Barnett-determined Block Grant to be adjusted throughout the year to reflect new UK spending announcements. These adjustments are known as Barnett consequentials. The Scottish Government have already included some anticipated consequentials on top of the agreed Block Grant within its Budget (see notes [4] and [6] to Table 1).[2] In our view, it is reasonable to expect there will be increases in UK Government spending announced in the March UK Budget, and for the Scottish Government to include some provision in estimating the total size of their Budget. The exact size of the consequentials will only be known following the UK Budget.

## Block Grant Adjustments for 2020-21

12 Block Grant Adjustments (BGAs) remove funding where the Scottish Government is now raising its own tax revenue and add funding where the Scottish Government is responsible for social security payments. The BGAs are based on OBR forecasts of UK Government tax revenues and social security spending. In the absence of updated OBR forecasts, the Scottish and UK Governments have agreed provisional BGAs in line with guidance in the fiscal framework.[3] These are based on the OBR's latest available economic forecasts, which were produced in March 2019.

13 Comparing these BGAs with our forecasts can illustrate how much more or less the Scottish Government has to spend, now the tax or benefit is devolved. In current circumstances, any comparison should be made with caution as the BGAs are set based on the OBR's March 2019 economic assumptions while the SFC forecasts include more up to date information. The BGAs are likely to change following the UK Budget in March. Table 2 and Table 3 show revenue or spend compared to BGAs for tax and social security respectively.

[1] HM Treasury (2019) Spending Round 2019 (link)

[2] Conservative and Unionist Party (2019) Costings Document – Manifesto 2019 (link)

[3] Scottish Parliament (2020) Letter from the Cabinet Secretary for Finance, Economy and Fair Work to the Finance and Constitution Committee (link) and The agreement between the Scottish Government and the United Kingdom government on the Scottish Government's fiscal framework (link)

**Table 2: SFC tax forecasts and provisional Budget-setting tax BGAs for 2020-21**

| £ million | SFC revenue forecast | Provisional BGA | Difference |
|---|---|---|---|
| Income tax | 12,365 | 12,319 | 46 |
| Land & Buildings Transaction Tax | 641 | 557 | 85 |
| Scottish Landfill Tax | 116 | 87 | 29 |
| Total | 13,123 | 12,963 | 160 |

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding. Differences are calculated as revenue subtract BGA to show the effect on the Scottish Government's funding. The remaining devolved taxes are not covered by BGA arrangements. The SFC revenue forecasts and provisional BGAs are calculated on different bases, so comparisons should be interpreted with caution.

**Table 3: SFC social security forecasts and provisional Budget-setting social security BGAs for 2020-21**

| £ million | SFC spend forecast | Provisional BGA | Difference |
|---|---|---|---|
| Attendance Allowance | 532 | 535 | 3 |
| Disability Living Allowance [1] | 718 | 669 | -49 |
| Personal Independence Payment | 1,583 | 1,601 | 19 |
| Carer's Allowance | 292 | 303 | 12 |
| Industrial Injuries Disablement Scheme | 80 | 85 | 5 |
| Severe Disablement Allowance | 7 | 9 | 1 |
| Total | 3,213 | 3,203 | -10 |

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding. Differences are calculated as BGA subtract spend to show the effect on the Scottish Government's funding. The other benefits being devolved to Scotland in April 2020 are not covered by BGA arrangements and instead are funded through the Barnett formula. The SFC spending forecasts and provisional BGAs are calculated on different bases, so comparisons should be interpreted with caution.
[1] SFC spend forecast for Disability Living Allowance (DLA) includes DLA working age, DLA for Children & Disability Assistance for Children and Young People (DACYP) and DLA Pensioners.

14 Almost all the social security forecasts reflect current UK Government policy because the DWP will continue to administer the benefits during 2020-21.[4] This is important because once the forecasts are based on Scottish policy, we expect the forecasts of Scottish spending to increase given Ministerial announcements and the passage of the Social Security (Scotland) 2018 Act. Any differences between spending and the BGAs will have to be managed within the Scottish Budget. In contrast, the SFC revenue forecasts in Table 2 include Scottish Government tax policy changes since devolution.

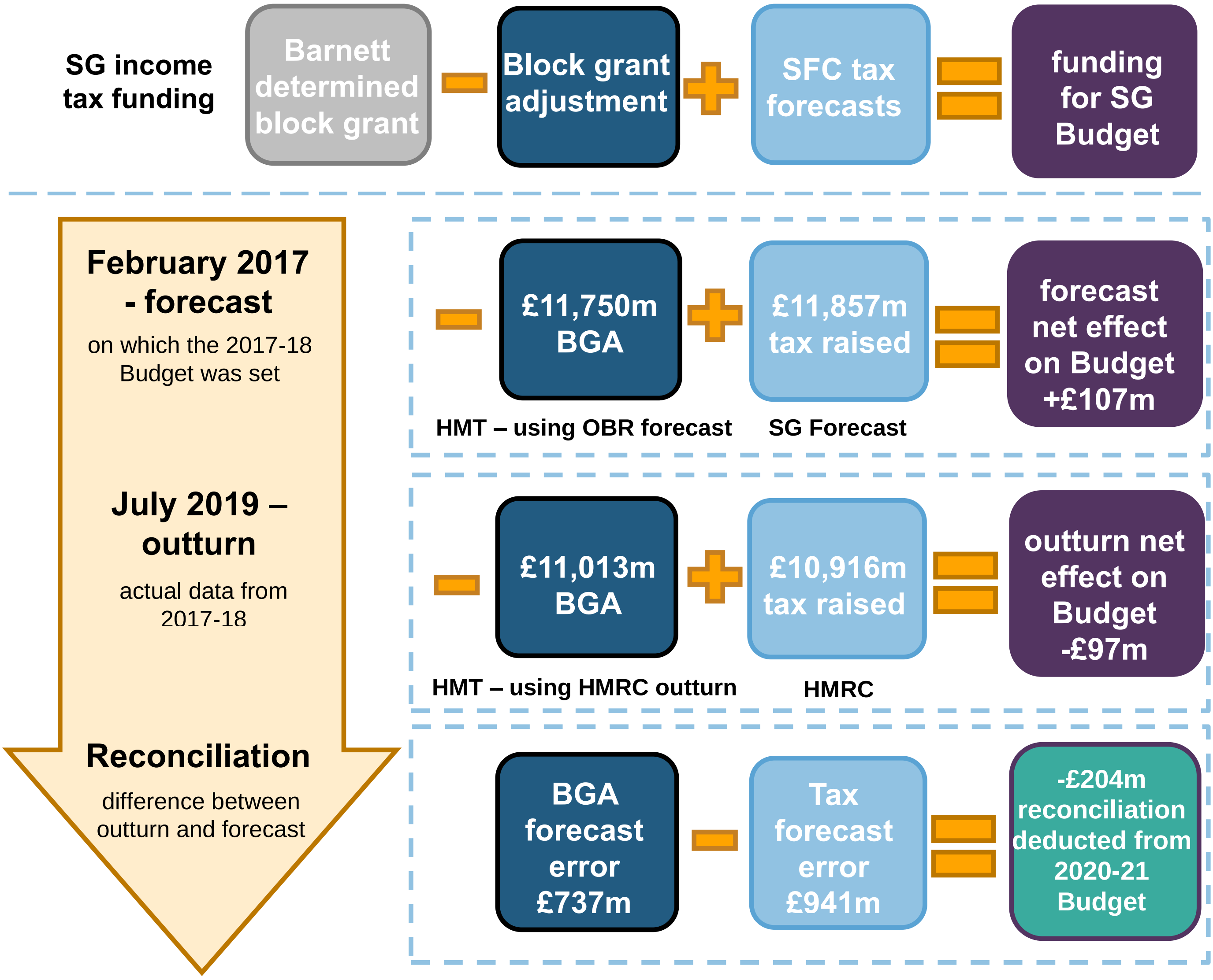
[4] Our Disability Living Allowance forecast includes the introduction of the new Disability Assistance for Children and Young People but does not include any future changes made to the working-age adult or pensioner benefits.

### Reconciliations

15 Reconciliations will have a significant effect on the Scottish Budget this year. The Scottish Budget is set based on forecasts and as information on actual revenues and spending becomes available the Scottish Government's funding is altered in response. These changes in funding are called reconciliations. Depending on the tax or benefit, reconciliations are applied in-year or as adjustments to future Budgets.

16 For the first time, an income tax reconciliation will be applied to the Budget. This relates to income tax from 2017-18 and will be applied in 2020-21. Reconciliations relate to the differences between how much revenue was forecast and how much was collected in Scotland and in the rest of the UK. They do not directly relate to the relative performance of revenues in Scotland and the rest of the UK. Figure 1 shows how the income tax reconciliation was calculated.

**Figure 1: 2017-18 income tax reconciliation**




Source: Scottish Fiscal Commission

17 A number of other devolved taxes and social security benefits have reconciliation processes, which are different to income tax.[5] So far these reconciliations have been small, but with further devolution of £3 billion of social security spending, these may become more significant in future years.

18 Table 4 shows all final reconciliations applied in 2020-21. These are based on outturn information and will not change.

**Table 4: Final reconciliations applied in 2020-21**

| £ million | Final reconciliation applied in 2020-21 |
|---|---|
| 2017-18 Income tax | -204 |
| 2018-19 Scottish Landfill Tax | -2 |
| 2018-19 Land and Buildings Transaction Tax | -3 |
| 2018-19 Carer's Allowance | 0 |
| 2018-19 Fines, forfeitures and fixed penalties | 2 |
| Total | -207 |

Source: Scottish Government

Figures may not sum because of rounding. The negative reconciliations sum to -£209 million. These negative reconciliations allow the Scottish Government to access £209 million resource borrowing in 2020-21.

## Managing reconciliations

19 The Scottish Government now needs to manage reconciliations during the year for all benefits and taxes (except income tax), and to manage reconciliations across years – the most significant of which are for income tax. The process is slightly different this year as the Scottish Government and HM Treasury have agreed flexibilities to give the Scottish Government the option of updating the BGAs following the March UK Budget. These arrangements affect the timing of reconciliations.

20 The BGAs for the fully devolved taxes and benefits should have been updated during 2019-20. In the absence of a UK Budget, there has not yet been a 2019-20 in-year reconciliation. The Scottish Government has chosen to delay the 2019-20 in-year reconciliations until after the UK Budget; these will then be applied to the Budget 2020-21. The latest forecasts assume a £30 million positive reconciliation – this forecast has been included in the Scottish Budget 2020-21 and increases the available funding (see note [5] to Table 1). The actual size of the reconciliation will be known following the UK Budget.

21 The arrangements give the Scottish Government the option of updating the 2020-21 provisional Budget setting BGAs following the March UK Budget. For

[5] A description of the reconciliation process for fully devolved taxes and social security can be found on our website (link). The Scottish Budget also includes revenues from fines, forfeitures and fixed penalties along with an associated reconciliations process. The revenues are forecast by the Scottish Government and included in Table 1, we report the final reconciliation applied in 2020-21 in Table 4 for completeness.

income tax, typically the BGA and revenue figures are fixed based on the forecast until the outturn data are known and a reconciliation is applied the following year; this will be in 2023-24. While updating the BGA could reduce the likely scale of the final reconciliation as it will include any income tax policies announced in the UK Budget and be based on more recent data, without updating the corresponding forecast of Scottish revenues it may not be the case that the final reconciliation is reduced.

22 Our updated forecasts of income tax revenues in 2018-19 and 2019-20 can be compared to the provisional BGAs, based on the OBR's March 2019 economic forecasts, to estimate the possible size of reconciliations in the future (indicative reconciliations). Based on these forecasts the reconciliation for 2018-19 income tax, to be applied to the Scottish Budget in 2021-22, would be -£555 million and for 2019-20 income tax, applied in 2022-23, would be -£211 million.

23 These indicative reconciliations can be updated following the March UK Budget.

24 As more of the fiscal framework comes into operation we will now see reconciliations affecting the Budget each year. How the Scottish Government chooses to respond to the reconciliations above should be considered, in part, alongside the possible future reconciliations.

### Borrowing

25 The Scottish Government is planning to draw down £106 million from the resource reserve in 2020-21 as well as borrowing £207 million. These plans are within the limits of the fiscal framework and we therefore consider them reasonable. Based on the information we have to date, which suggest £100 million will remain in the resource reserve at the end of 2020-21, it would seem that the Government is not building up its reserves to deal with the large income tax reconciliations expected to reduce the Budget in 2021-22 and 2022-23.

26 By the time of the MTFS, anticipated in May 2020, the Scottish Government will have updated information on the size of the indicative reconciliations and of any changes to funding from the UK Government following the March Budget. Based on this information the Scottish Government should consider how best to prepare for the future reconciliations.

27 The Scottish Government can also borrow to fund capital spending, as shown in Table 1. The Government plans to borrow £450 million in 2020-21, this is £100 million more than was planned in the MTFS in May 2019.

28 In 2019-20 the Scottish Government and HM Treasury have agreed the drawdown limit for the capital and financial transaction reserves will be

waived, drawing down £181 million. This is considerably higher than the £46 million planned at the time of the 2019-20 Budget, and more than the £100 million limit which usually applies. This larger drawdown and the waiving of the limit has occurred following negative capital consequentials during the course of 2019-20. The Scottish Government is planning on drawing down £37 million in 2020-21, currently estimated to leave £6 million in financial transactions in the capital reserve at the end of 2020-21.

## Economy

29 Over the course of 2018 and 2019, Brexit negotiations have played a dominant role in the economic narrative of Scotland and the UK. Uncertainty about both the nature and timing of Brexit has resulted in subdued growth over the last year and greater volatility between quarters. Looking ahead in 2020, the UK has now left the EU, and the unwinding of some Brexit-related uncertainty may support some additional growth. However, Brexit remains a risk to continued economic growth.

30 Concerns remain about slowing global growth, particularly in the Euro Area, and this is expected to affect Scotland's trade prospects. The outlook for trade has been exacerbated by the potential for global trade wars and, more recently, the potential fallout from the coronavirus.

31 Table 5 summarises our economy forecast and compares it to our forecast from December 2018.

32 Our estimate of productivity growth in Scotland has remained low and below our previous forecasts. As a result, we have revised down our forecast of trend productivity growth at the beginning of the forecast period. Offsetting slower productivity growth and weaker global conditions, higher UK and Scottish Government spending is expected to continue to support growth in the Scottish economy.

**Table 5: Headline economy forecasts, December 2018 and February 2020, per cent growth rates unless otherwise stated**

| GDP | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 |
|---|---|---|---|---|---|---|---|
| December 2018 | 1.4 | 1.2 | 1.0 | 1.0 | 1.1 | 1.2 | |
| February 2020 | 1.5 | 0.9 | 1.0 | 1.1 | 1.2 | 1.2 | 1.2 |
| **Trend productivity** | | | | | | | |
| December 2018 | 0.3 | 0.7 | 0.9 | 1.0 | 1.1 | 1.2 | |
| February 2020 | 0.2 | 0.3 | 0.6 | 0.9 | 1.1 | 1.2 | 1.3 |
| **Average nominal earnings** | | | | | | | |
| December 2018 | 2.0 | 2.3 | 2.5 | 2.8 | 3.0 | 3.1 | |
| February 2020 | 2.6 | 2.8 | 3.0 | 3.1 | 3.2 | 3.3 | 3.3 |
| **Average real earnings** | | | | | | | |
| December 2018 | -0.3 | 0.3 | 0.5 | 0.6 | 0.9 | 1.1 | |
| February 2020 | 0.6 | 1.0 | 1.1 | 1.0 | 1.2 | 1.2 | 1.2 |
| **Employment (millions)** | | | | | | | |
| December 2018 | 2.64 | 2.65 | 2.65 | 2.66 | 2.66 | 2.66 | |
| February 2020 | 2.67 | 2.68 | 2.67 | 2.67 | 2.68 | 2.68 | 2.69 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link).
Shaded cells refer to outturn available at time of publication.

33 In Scotland, earnings growth has continued to exceed our earlier expectations. After a period of subdued growth, earnings finally appear to be responding to tight conditions in the labour market. Earnings are also being supported by public sector pay policy and faster growth in the minimum wage and national living wage. As a result, we have revised up our forecast of earnings growth and this will support greater household consumption. However, it should be noted that earnings growth, both nominal and real, remains below historical values over the forecast period.

34 Balancing all these factors, our forecast of headline GDP is similar to December 2018, with small upwards revisions from 2021 onwards.

## Tax forecasts

35 Tax revenues in 2020-21 will contribute around £16 billion to the Scottish Budget. Table 6 summarises our tax forecasts that currently affect the Scottish Budget.[6]

[6] Further detail and additional illustrative forecasts for taxes that may be part of the Scottish Budget in future can be found in Chapter 4.

**Table 6: Summary of tax forecasts informing the Scottish Budget 2020-21**

| £ million | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|
| Income tax | 11,677 | 12,365 | 12,897 | 13,447 | 14,059 | 14,722 |
| Non-Domestic Rates | 2,806 | 2,749 | 3,012 | 3,345 | 3,423 | 3,590 |
| Land & Buildings Transaction Tax | 613 | 641 | 666 | 692 | 720 | 749 |
| *of which, Residential* | 288 | 303 | 319 | 336 | 354 | 371 |
| *ADS* | 134 | 129 | 131 | 134 | 137 | 140 |
| *Non-Residential* | 191 | 209 | 216 | 222 | 230 | 238 |
| Scottish Landfill Tax | 124 | 116 | 110 | 94 | 79 | 66 |
| Total tax | 15,220 | 15,872 | 16,685 | 17,578 | 18,281 | 19,127 |

Source: Scottish Fiscal Commission
Figures may not sum because of rounding.

## Income tax

36 The Scottish Government has announced that in 2020-21 the higher rate threshold will be frozen at the same rate, £43,430, as in 2019-20. We expect this freezing of the higher rate threshold, relative to our baseline assumption of increasing it in line with inflation, to raise an additional £51 million for the Scottish Budget in 2020-21. This policy means there will be more higher rate taxpayers in Scotland than would otherwise have been the case. No other income tax policies have been announced. Table 7 shows our income tax forecast compared to December 2018. A more detailed breakdown of Table 7 can be found in the income tax section in Chapter 4.

**Table 7: Summary of income tax forecast compared to December 2018**

| £ million | 2017-18 | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|---|
| December 2018 | 11,008 | 11,452 | 11,684 | 12,285 | 12,746 | 13,242 | 13,805 |
| 2017-18 outturn | -92 | -90 | -98 | -110 | -119 | -129 | -140 |
| Economy | | 111 | 225 | 273 | 356 | 427 | 488 |
| Other | | -94 | -134 | -135 | -141 | -150 | -153 |
| February 2020 pre-measures | 10,916 | 11,378 | 11,677 | 12,314 | 12,843 | 13,390 | 14,000 |
| 2020-21 policy costing | | | | 51 | 54 | 56 | 59 |
| February 2020 post-measures | 10,916 | 11,378 | 11,677 | 12,365 | 12,897 | 13,447 | 14,059 |
| Change from December 2018 | -92 | -74 | -7 | 80 | 151 | 205 | 254 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link), HMRC (2019) Scottish Income Tax Outturn Statistics (link).
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

37 Outturn data for 2017-18 are now available, published by HMRC in summer 2019.[7] The outturn data were £92 million less than our December 2018 forecast, leading to downward revisions of, on average, £114 million across

[7] HMRC (2019) Scottish Income Tax Outturn Statistics (link)

the forecast period. We evaluated our 2017-18 forecast error in our September 2019 Forecast Evaluation Report.[8]

38 Since December 2018 improvements in the outlook for earnings growth has resulted in an upwards revision in our income tax forecast, by £273 million in 2020-21. Other adjustments result in downward revisions in 2020-21 of £135 million. Chapter 4 provides further detail on these adjustments.

39 Overall, our pre-measures income tax forecast for 2020-21 is broadly unchanged from December 2018, with an upwards revision of around £30 million. The extra £51 million revenue from the higher rate threshold policy results in a total upward revision of £80 million compared to December 2018.

### Other tax forecasts

40 We expect the fully devolved taxes, Land and Buildings Transaction Tax (LBTT) and Scottish Landfill Tax (SLfT), to raise £757 million in 2020-21, up from £737 million in 2019-20. This includes the £10 million estimated increase in LBTT because of the introduction of a new top band for non-residential leases.

41 Our NDR forecast is for £2.7 billion in 2020-21, down from £2.8 billion in 2019-20. The fall is mainly because of the timing of losses from revaluation appeals. The forecast includes a number of policies introduced in the Non-Domestic Rates (Scotland) Bill.[9] The Scottish Budget includes the creation of an Intermediate Property Rate, replacing the Large Business Supplement for properties with a rateable value between £51,000 and £95,000. This is expected to reduce NDR income by £7 million in 2020-21.

## Social security

42 In 2020-21 we estimate £3.4 billion will be spent by the Scottish Government on social security, around 10 per cent of total resource spending. This compares with the £458 million forecast to be spent on all social security in 2019-20.[10] This change is largely driven by the Scottish Government becoming financially responsible for disability benefits, such as Personal Independence Payments and Disability Living Allowance, from April 2020 onwards.[11]

[8] Scottish Fiscal Commission (2019) Forecast Evaluation Report (link)

[9] Information on our policy costings for the Non-Domestic Rates (Scotland) Bill can be found in Scottish Fiscal Commission (2019) Non Domestic Rates (Scotland) Bill – Supplementary Costings December 2019 (link)

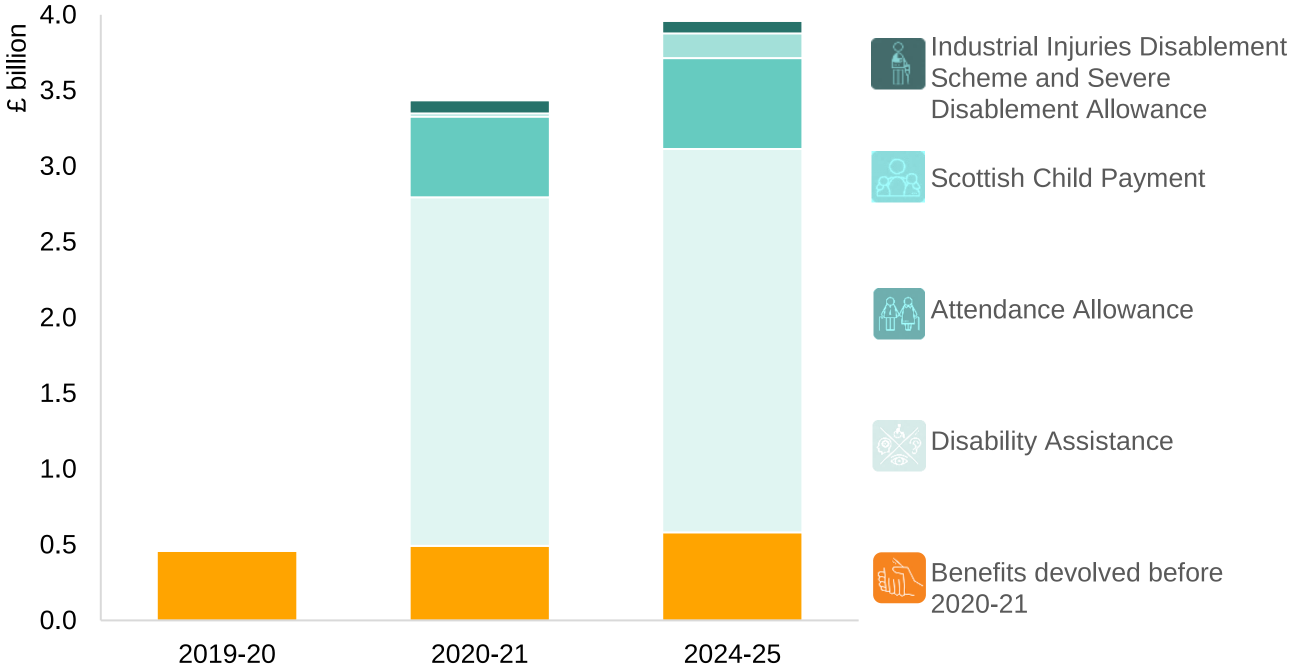
[10] As shown in Table 8, £458 million is the forecast spend on the Scottish Government's social security portfolio in 2019-20 plus spending on Best Start Foods and Employability Services.

[11] Cold Weather Payments and Winter Fuel Payments will be devolved at a later date.

43 Social security spending is variable and harder to control than other areas of spending. Spending will be determined by the number of eligible people who apply for support, all of whom must be paid at the rate set in the policy. The Scottish Government will have to meet this expenditure as it arises, even if it differs from the forecast used to set the Budget initially. Spending on three large social security payments, Personal Independence Payments, Disability Living Allowance and Attendance Allowance, is a significant component of total social security spend (as shown in Table 8). This means that even modest forecast errors are unlikely to offset each other and may result in spending differing in-year from our forecasts.

44 The funding received from the UK Government, via the BGAs, may also change during the year to reflect revised forecasts of spending in England and Wales. The Scottish Government faces a risk that if spending in Scotland increases and spending in England and Wales decreases, compared to the original figures used to determine the Block Grant Adjustments and the Scottish Budget, then there could be a significant in-year cash shortfall to manage.

**Figure 2: Total social security spending forecast**




Source: Scottish Fiscal Commission

Disability Assistance includes spending for Child Disability Assistance, Disability Living Allowance Adult and Personal Independence Payment.

Total social security spending includes all social security portfolio spending as well as spending on Best Start Foods, Employability Services and Scottish Child Payment.

45 Our forecasts include the costs for two new forms of social security assistance being launched this year, Disability Assistance for Children and Young People (DACYP) and the Scottish Child Payment. There are some policy differences between DACYP and the UK Government Disability Living Allowance for

Children benefit, which we forecast will lead to an increase in spending. Further details on our policy costing can be found in Annex A.

46 Scottish Child Payment is a new form of social security support without a UK equivalent benefit. The additional costs, which are expected to reach £162 million in 2024-25, will have to be met from the Scottish Budget; there is no funding transferred from the UK Government as there is no equivalent UK benefit being devolved.

47 Our forecasts for the Scottish Budget 2020-21 are shown in Table 8 and further information can be found in Chapter 5. Our forecasts show the total amount paid to, or in respect of, people receiving social security support in Scotland, and does not include any administrative costs.

**Table 8: Summary of social security forecasts informing the Scottish Budget 2020-21**

| £ million | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|
| Social security portfolio benefits previously forecast [1] | 437 | 465 | 491 | 522 | 547 | 573 |
| New social security portfolio benefits for 2020-21, *of which* | | 2,921 | 3,001 | 3,075 | 3,145 | 3,216 |
| *Child Disability Assistance [2]* | | 217 | 250 | 275 | 295 | 312 |
| *Personal Independence Payment* | | 1,583 | 1,650 | 1,714 | 1,776 | 1,841 |
| *Disability Living Allowance Adult* | | 502 | 470 | 440 | 410 | 380 |
| *Attendance Allowance* | | 532 | 546 | 562 | 582 | 601 |
| *Industrial Injuries Disablement Scheme* | | 80 | 79 | 78 | 78 | 77 |
| *Severe Disablement Allowance* | | 7 | 7 | 6 | 6 | 5 |
| Scottish Government social security portfolio – total spending | 437 | 3,387 | 3,492 | 3,597 | 3,692 | 3,789 |
| Scottish Child Payment | | 21 | 65 | 94 | 157 | 162 |
| Best Start Foods [3] | 6 | 9 | 8 | 8 | 8 | 8 |
| Employability Services | 15 | 18 | 13 | 5 | 0 | |
| Total spending | 458 | 3,435 | 3,578 | 3,704 | 3,857 | 3,959 |

Source: Scottish Fiscal Commission

Figures may not sum because of rounding.

[1] Includes spending for benefits devolved before 2020-21: Carer's Allowance, Carer's Allowance Supplement, Best Start Grant, Discretionary Housing Payments, Funeral Support Payment and Scottish Welfare Fund.

[2] We use the term 'Child Disability Assistance' to refer to the combined spending on Disability Living Allowance for Children and Disability Assistance for Children and Young People.

[3] Best Start Foods includes some spending on the UK Government Healthy Start Scheme while people are transferred to the new benefit.

48 For the new social security portfolio benefits for 2020-21, shown in Table 8, most of our forecasts are based on current UK Government policy. As responsibility for delivery of the benefits transfers to Social Security Scotland, the benefits will be reformed and delivery of those benefits changed from the

current system administered by the DWP. As there is not yet sufficient policy or operational detail available, our forecasts do not include the effect of these changes and are therefore likely to underestimate expenditure.

49 The exception is the spending for Child Disability Assistance which includes the Scottish Government's new Disability Assistance for Children and Young People. We estimate that the introduction of Disability Assistance for Children and Young People leads to an additional £6 million of spending in 2020-21, rising to an additional £23 million by 2024-25.

# Chapter 1 Introduction

## What is in this report?

1.1 This report presents the official and independent economic and fiscal forecasts created by the Scottish Fiscal Commission to inform the Scottish Budget 2020-21, published on 6 February 2020.

1.2 Alongside our forecasts, the report provides an overview of the main assumptions and judgements made as part of the forecasting process. We also set out what has changed since the last Scottish Budget in December 2018.

1.3 The report contains the following chapters:

| | |
|---|---|
| **Summary** | Our forecasts, the fiscal overview and the main stories from this round of forecasts. |
| **Fiscal Overview** | Explains how the Scottish Budget 2020-21 has been set. This includes the role of our forecasts, block grant adjustments and reconciliations. We also assess the Scottish Government's planned borrowing and use of the Scotland Reserve. |
| **Economy** | Our five-year forecasts for the Scottish economy, including the underlying judgements. |
| **Tax** | Our forecasts of income from devolved taxes. |
| **Social Security** | Our forecasts of devolved social security spending. |
| **Annex A: Policy Costings** | Our estimates of how much any individual policy will cost or raise, and how the Commission has arrived at that estimate. |

| | |
|---|---|
| **Annex B: Policy Recostings** | Our revised estimates of policies previously costed. Recostings may be required because of new outturn data or revisions to assumptions and judgements. |
| **Annex C: Materiality and Policy Costings** | Our approach to handling policies which have a very small fiscal effect. |

1.4 Our report focuses on the most important issues of interest to our stakeholders. Some additional information we previously provided in the main report, for example comparisons to our previous forecasts, comparisons to OBR forecasts and sensitivity analysis has now been moved to supplementary tables, available for download from our website. If there is any additional information you are looking for that is not in this report or the supplementary tables, please get in touch with us at info@fiscalcommission.scot.

1.5 We usually publish two forecasts a year – one in May to accompany the Scottish Government's Medium Term Financial Strategy (MTFS) and one in December to accompany the Scottish Budget. In previous publications to accompany the Scottish Budget we compared our latest Budget forecasts to our previous MTFS forecasts. Feedback from users suggests that comparing Budget to Budget forecasts is more helpful. Throughout this report, we compare our latest February 2020 forecasts published alongside the Scottish Budget 2020-21 to those we published in December 2018 alongside the Scottish Budget 2019-20. Tables comparing our latest forecasts to May 2019 are provided as supplementary tables on our website.

## The process behind creating our forecasts this year

1.6 On 2 October 2019, we received ten weeks' notice from the Cabinet Secretary for Finance, Economy and Fair Work of a Scottish Budget on 12 December, and we started to prepare our forecasts for this date. On 6 November, the Cabinet Secretary wrote confirming the Scottish Budget would not be on 12 December because of the UK general election being held on that date. On 14 November, we received notification that there would not be a Scottish Budget in December and we paused our forecast preparation. In discussion with the Scottish Government, we resumed preparation of our forecasts in early January 2020, with formal notification of a Scottish Budget on 6 February received on 13 January, notification of three and a half weeks.

1.7 Throughout this period, our interaction with the Scottish Government has been guided by our Protocol for engagement.[12] While three and a half weeks' notice of the February Scottish Budget is unusually short, this was manageable

[12] Protocol for engagement between the Scottish Fiscal Commission and the Scottish Government Version 3.0 published September 2019 (link)

because of the time spent preparing our forecasts in late 2019, and the positive engagement between the Scottish Government, Scottish Parliament and the Commission. Our view is that in future, it is essential that the standard ten week notice period is maintained to ensure high quality, independent forecasts to support the Scottish Budget.

1.8 Since the initial formal notification of the date of the Scottish Government's Budget on 2 October, the Commission has had several rounds of meetings to discuss our forecasts. Attendees included the Scottish Government, Revenue Scotland and the Office for Budget Responsibility. In accordance with the Protocol, more detail of timings and attendees is published on our website.[13]

1.9 To finalise our forecasts ready for publication, we need a cut-off date for incorporating new data and information in the forecasts. Our data cut-off, including information on Brexit, was 15 January. We made three exceptions to this data cut off point to incorporate data on LBTT and social security. We were provided with pre-release access on 17 January to the LBTT statistics with data up to the end of December by Revenue Scotland. We were given data on LBTT non-residential leases on 22 January to inform our policy costing. Our social security forecasts were informed by management information for the new Best Start Foods and Funeral Support Payments which was received on 16 January. No other new data or information available after 15 January was included in our forecasts.

1.10 Headline dates of interest are:

| | |
|---|---|
| 2 October | Cabinet Secretary for Finance, Economy and Fair Work wrote to advise that the Scottish Government intended to publish its Budget 2020-21 on 12 December. |
| 6 November | Cabinet Secretary for Finance, Economy and Fair Work wrote to advise that the Scottish Government could not go ahead with its Budget on 12 December because of the UK election on that date. |
| 7 November | Dame Susan Rice replied to the Cabinet Secretary for Finance, Economy and Fair Work. The Commission continued to work on its forecasts to allow for a Budget in the week commencing 16 December. |
| 14 November | Cabinet Secretary for Finance, Economy and Fair Work wrote to confirm that there would not be a budget in the week commencing 16 December. |
| 9 January | Scottish Government officials confirmed that they would work with the Commission to produce budget forecasts in the first week of February. |

[13] Scottish Fiscal Commission (2020) Scottish Economic and Fiscal Forecasts – February 2020 (link)

| | |
|---|---|
| 13 January | Cabinet Secretary for Finance, Economy and Fair Work provided formal notification that the Budget 2020-21 would be published on 6 February. |
| 15 January | Deadline for inclusion of new data in the forecasts, Brexit assumptions finalised. |
| 17 January | Closure of the economy forecast. |
| 23 January | The Scottish Government provided the Commission with finalised policy measures. |
| 28 January | The Commission presented the Scottish Government with final forecasts to allow the finalisation of the Scottish Government's Budget. |
| 31 January | The Commission's near-final report was shared with the Scottish Government. |
| 5 February | Phone call between Dame Susan Rice, Chair of the Commission, and Cabinet Secretary for Finance, Economy and Fair Work.<br>A pre-release version of the Commission's report was shared with the Cabinet Secretary for Finance, Economy and Fair Work. |
| 6 February | Scotland's Economic and Fiscal Forecasts – February 2020 published. |

# Chapter 2
# Fiscal Overview

2.1 This chapter initially focuses on our latest fiscal forecasts before discussing the components of the Scottish Budget. We cover the particular risks and uncertainties caused by the increasing size and complexity of the Scottish Budget, some of which are amplified this year because the Scottish Budget is occurring before the UK Budget. In this chapter we discuss:

- our forecasts informing the Scottish Budget
- the Scottish Budget 2020-21, including funding and reconciliations
- the reasonableness of the Scottish Government's borrowing plans and use of the Scotland Reserve

2.2 Our next forecasts, published alongside the Scottish Government's Medium Term Financial Strategy currently anticipated in May, will be combined with the March UK Budget and OBR forecasts to provide an updated overview of the Scottish public finances a few months into the financial year. The Scottish Government and Parliament will need to consider how best to monitor and respond to these in-year budget revisions.

## Scottish Fiscal Commission Forecasts

2.3 Tax revenues will account for £16 billion of the Scottish Budget in 2020-21. This includes the effect of three policy changes announced by the Scottish Government. The income tax higher rate threshold has again been frozen and is forecast to raise an additional £51 million, the new LBTT higher rate on non-residential lease transactions is forecast to raise £10 million, and the creation of a new Intermediate Property Rate for Non-Domestic Rates (NDR) is expected to reduce NDR revenues by £7 million.

2.4 A number of benefits will be devolved to the Scottish Parliament in April 2020. This means social security spending has become a significant component of the Scottish Budget 2020-21, accounting for 10 per cent of all resource spending or £3.4 billion. Our forecasts determine how much of the Scottish Budget should be allocated to social security spending. This spending is variable and difficult to manage within the year because everyone who applies and qualifies for a benefit must be paid.

2.5 Spending on three large social security payments is a significant component of total social security spend (see Table 2.2). This means even modest forecast errors are unlikely to offset each other and may result in spending differing in-year from our forecasts. Any differences between our forecasts and the actual amount spent in 2020-21 will need to be managed within the Scottish Budget.

2.6 A number of devolved social security benefits will be administered by DWP on behalf of the Scottish Government. DWP will administer these payments in line with existing UK Government policy and our forecasts reflect this. The Scottish Government is planning to replace nearly all benefits with new Scottish equivalents, starting with Disability Living Allowance for Children and Young People (DACYP) which will open to applications in summer 2020. We expect the introduction of DACYP to cost an additional £6 million in 2020-21. The Scottish Government also plans to introduce a new Scottish Child Payment by Christmas 2020, which we expect to cost £21 million in 2020-21 increasing to £162 million by 2024-25. This does not replace any existing benefit, therefore must be fully funded from the Scottish Budget.

2.7 As the Scottish Government takes over DWP administered benefits, we will update our forecasts to reflect the new Scottish policies and approach. However, the Scottish Government has responsibility for all spending on devolved benefits, regardless of who administers them.

2.8 Our tax and social security forecasts used in the Scottish Budget 2020-21 are set out in Tables 2.1 and 2.2.

**Table 2.1: Summary of tax forecasts informing the Scottish Budget 2020-21**

| £ million | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|
| Income tax | 11,677 | 12,365 | 12,897 | 13,447 | 14,059 | 14,722 |
| Non-Domestic Rates | 2,806 | 2,749 | 3,012 | 3,345 | 3,423 | 3,590 |
| Land & Buildings Transaction Tax | 613 | 641 | 666 | 692 | 720 | 749 |
| *of which, Residential* | 288 | 303 | 319 | 336 | 354 | 371 |
| *ADS* | 134 | 129 | 131 | 134 | 137 | 140 |
| *Non-Residential* | 191 | 209 | 216 | 222 | 230 | 238 |
| Scottish Landfill Tax | 124 | 116 | 110 | 94 | 79 | 66 |
| Total tax | 15,220 | 15,872 | 16,685 | 17,578 | 18,281 | 19,127 |

Source: Scottish Fiscal Commission
Figures may not sum because of rounding.

**Table 2.2: Summary of social security forecasts informing the Scottish Budget 2020-21**

| £ million | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|
| Social security portfolio benefits previously forecast [1] | 437 | 465 | 491 | 522 | 547 | 573 |
| New social security portfolio benefits for 2020-21, *of which* | | 2,921 | 3,001 | 3,075 | 3,145 | 3,216 |
| *Child Disability Assistance [2]* | | 217 | 250 | 275 | 295 | 312 |
| *Personal Independence Payment* | | 1,583 | 1,650 | 1,714 | 1,776 | 1,841 |
| *Disability Living Allowance Adult* | | 502 | 470 | 440 | 410 | 380 |
| *Attendance Allowance* | | 532 | 546 | 562 | 582 | 601 |
| *Industrial Injuries Disablement Scheme* | | 80 | 79 | 78 | 78 | 77 |
| *Severe Disablement Allowance* | | 7 | 7 | 6 | 6 | 5 |
| Scottish Government social security portfolio – total spending | 437 | 3,387 | 3,492 | 3,597 | 3,692 | 3,789 |
| Scottish Child Payment | | 21 | 65 | 94 | 157 | 162 |
| Best Start Foods [3] | 6 | 9 | 8 | 8 | 8 | 8 |
| Employability Services | 15 | 18 | 13 | 5 | 0 | |
| Total spending | 458 | 3,435 | 3,578 | 3,704 | 3,857 | 3,959 |

Source: Scottish Fiscal Commission
Figures may not sum because of rounding.
[1] Includes spending for Carer's Allowance, Carer's Allowance Supplement, Best Start Grant, Discretionary Housing Payments, Funeral Support Payment and Scottish Welfare Fund.
[2] We use the term 'Child Disability Assistance' to refer to the combined spending on Disability Living Allowance for children and Disability Assistance for Children and Young People (DACYP).
[3] Best Start Foods includes some spending on the UK Government Healthy Start Scheme while people are transferred to the new benefit.

2.9 Our tax and social security forecasts will be updated at the time of the Scottish Government's next Medium Term Financial Strategy, anticipated in May 2020. These updates will reflect the inclusion of new data, revised assumptions and any UK policy changes made, particularly those at the March 2020 UK Budget.

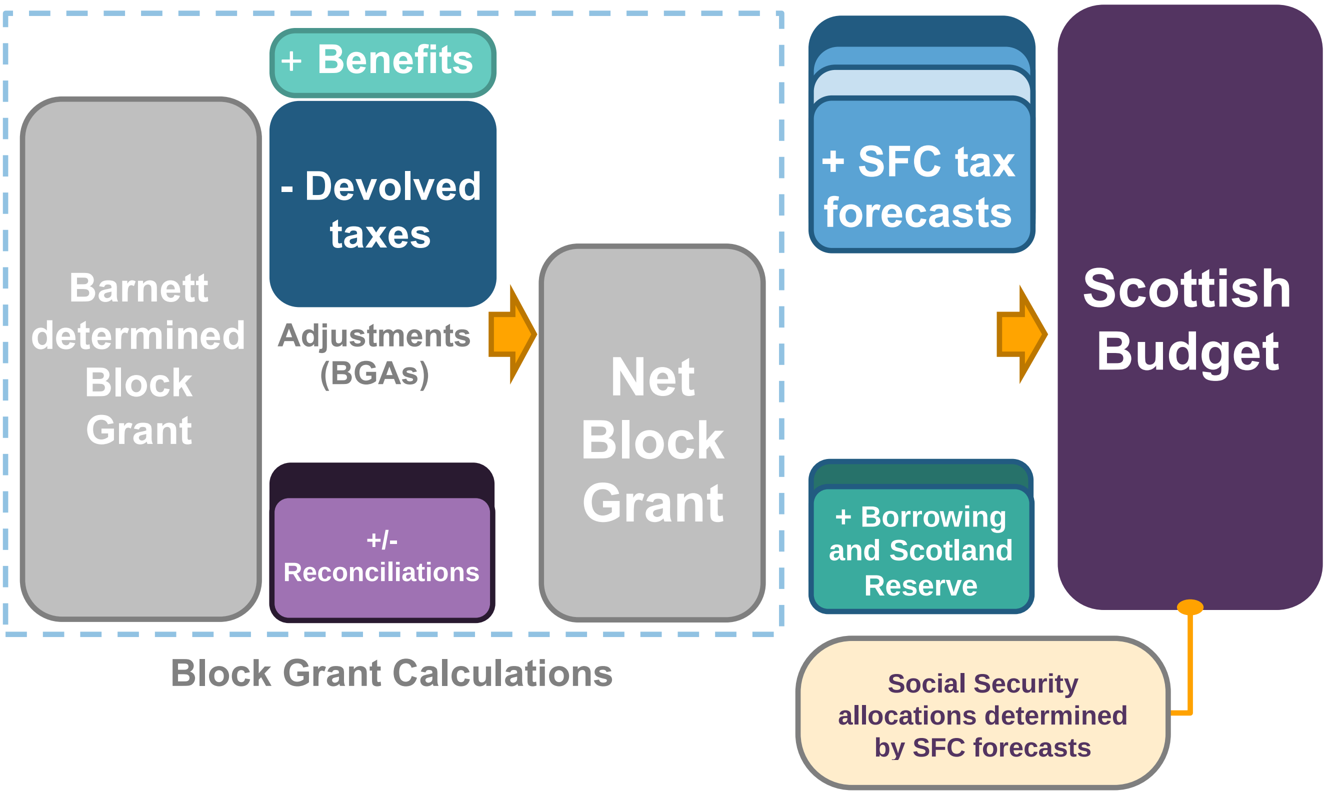
## How is the Scottish Budget 2020-21 set?

2.10 Our forecasts are just one component of the Scottish Budget which is based on a combination of funding from the UK Government, Scottish tax revenues, and Scottish Government borrowing and cash management decisions. All of these components can vary during the financial year as well as potential variations in social security spending, and the Scottish Government will need to manage the Budget throughout the year.

2.11 Funding from the UK Government is usually based on the UK Autumn Budget, and updated OBR forecasts. This year, however, the UK Budget will not take place until March 2020. The Scottish Government has agreed funding arrangements with HM Treasury and made a number of assumptions in order to set the Scottish Budget. These arrangements and assumptions may be revised following the March 2020 UK Budget.

2.12 Figure 2.1 presents a stylised illustration of how the Scottish Budget is determined and Table 2.3 summarises the Scottish Government's funding included in Budget 2020-21. We discuss each component in turn.

**Figure 2.1: How is the Scottish Budget set?**




Source: Scottish Fiscal Commission

**Table 2.3: Funding and spending plans for the Scottish Budget 2020-21**

| £ million | | 2020-21 |
|---|---|---|
| Resource | Barnett-determined Block Grant – resource [1] | 29,569 |
| | SFC tax revenue forecasts [2] | 13,123 |
| | Tax and non-tax BGAs | -12,991 |
| | Social Security BGAs | 3,203 |
| | Reconciliations [3] | -207 |
| | Other [4] | 639 |
| | Total resource funding | 33,335 |
| | Resource borrowing | 207 |
| | Drawdown from Scotland Reserve | 106 |
| | Other [5] | 269 |
| | Total resource spending | 33,917 |
| Capital | Barnett-determined Block Grant – capital [1] | 4,408 |
| | Financial Transactions (FTs) [1] | 606 |
| | Other [6] | 326 |
| | Total capital funding | 5,340 |
| | Capital borrowing | 450 |
| | Drawdown from Scotland Reserve (capital and FTs) [7] | 37 |
| | Other [8] | -10 |
| | Total capital spending | 5,817 |

Source: Scottish Government, Scottish Fiscal Commission.
The table does not include non-cash budget. Figures may not sum because of rounding.
All components of the Budget will vary in 2020-21 reflecting changes to the Barnett-determined Block Grant following changes in UK Government spending, changes in our forecasts of tax revenues, changes to the BGAs, and changes in the Scottish Government's plans for borrowing and the use of the Scotland Reserve.
[1] Agreed with HM Treasury based on September 2019 Spending Round.
[2] Scottish Fiscal Commission tax revenue forecasts cover income tax, Land and Building Transaction Tax, and Scottish Landfill Tax. Non-Domestic Rates are not included in the revenue forecasts as these are used separately to set the distributable amount for Non-Domestic Rates.
[3] Includes final reconciliations for: 2017-18 income tax revenue and BGA (-£204 million), 2018-19 Land and Building Transaction Tax BGA (-£3 million), 2018-19 Scottish Landfill Tax BGA (-£2 million), 2018-19 fines, forfeitures and penalties (FFFPs) BGA (£2 million), 2018-19 Carer's Allowance BGA (£0 million).
[4] Includes Pillar 1 Farm payments (£472 million), anticipated Barnett RDEL consequentials (£142 million), and Scottish Government's forecast of revenues from FFFPs (£25 million).
[5] Includes Rail Resource Grant (£80 million), fiscal framework administration costs (£66 million), Migrant Surcharge (£22 million), In-Year Reconciliations deferred from 2019-20 (£30 million), deferred consequentials from 2019-20 Supplementary Estimates (£58 million), Queen's and Lord Treasurer's Remembrancer (£5 million), and Machinery of Government Transfers (£8 million).
[6] Anticipated Barnett CDEL consequentials (£326 million).
[7] Includes planned drawdowns of £5 million for general capital spending and £32.2 million for FTs.
[8] Includes Glasgow City funding (£15 million) and repayment of Financial Transactions to HMT (-£25 million).

### Barnett-determined Block Grant

2.13 The Scottish Government receives funding from the UK Government based on the UK Government's spending announcements. This funding is calculated using the Barnett formula and the funding is labelled the Barnett-determined Block Grant in Figure 2.1. This is effectively the funding the Scottish Government would have received had there been no tax or social security devolution.

2.14 In the absence of the UK spending decisions announced alongside the March 2020 UK Budget, the Scottish and UK Governments have agreed to base the 2020-21 Barnett-determined Block Grant on the UK Government's September 2019 spending round.[14]

2.15 The 2020-21 Barnett-determined Block Grant will be adjusted throughout the year to reflect any new UK Government spending announcements, including those made at the March 2020 UK Budget. The Scottish Government receives a Barnett-determined share of any spending announcements, called consequentials.

2.16 Every year the Scottish Government receives consequentials which alter the funding position. In most years these consequentials result in additional funding which the Scottish Government can allocate during the course of the year.

2.17 The Scottish Government has included anticipated consequentials in its Budget (see notes [4] and [6] in Table 2.3). These anticipated consequentials are based on policies announced and costed in the Conservative Party Manifesto for the 2019 General Election.[15]

2.18 In our view it is reasonable to expect there will be increases in UK Government spending announced at the March Budget, and for the Scottish Government to include some provision in estimating the total size of its Budget. The exact size of the consequentials will only be known following the UK Budget.

**Table 2.4: The Scottish Government's anticipated consequentials for 2020-21**

| £ million | 2020-21 |
|---|---|
| Resource | 142 |
| Capital | 326 |

Source: Scottish Government

### Block Grant Adjustments

2.19 The Barnett-determined Block Grant is adjusted by removing funding where the Scottish Government is now raising its own tax revenue and adding

[14] HM Treasury (2019) Spending Round 2019 (link)

[15] Conservative and Unionist Party (2019) Costings Document – Manifesto 2019 (link)

funding where the Scottish Government has become responsible for social security payments. These are called Block Grant Adjustments (BGAs).

2.20 BGAs are applied to the Barnett-determined Block Grant to calculate the funding transferred to the Scottish Government for the next financial year, the Net Block Grant.

2.21 BGAs represent the hypothetical amounts that would have been raised or spent in Scotland if the taxes or benefits had not been devolved. They are based on revenues or spending in Scotland the year before devolution, adjusted in line with forecasts of changes in revenue or spending per head in the rest of the UK. The BGAs are calculated by the UK and Scottish Governments based on OBR forecasts of the corresponding UK Government tax or benefit and projected population growth in each country.

### 2020-21 Budget-setting Block Grant Adjustments

2.22 In the absence of updated OBR forecasts, the Scottish and UK Governments have agreed provisional BGAs in line with guidance in the fiscal framework to set the Scottish Budget.[16,17] These provisional BGAs use the OBR's latest available forecasts, which are based on the economic forecasts produced in March 2019.[18]

2.23 Comparing BGAs with Scottish Fiscal Commission (SFC) revenue or spend forecasts can illustrate how much more or less the Scottish Government has to spend, now the tax or benefit is devolved. In current circumstances, any comparison should be made with caution as the BGAs are based on the OBR's March 2019 economy assumptions while our forecasts consider up to date information. The BGAs may change following the UK Budget in March.

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[16] Scottish Parliament (2020) Letter from the Cabinet Secretary for Finance, Economy and Fair Work to the Finance and Constitution Committee (link)

[17] The agreement between the Scottish Government and the United Kingdom government on the Scottish Government's fiscal framework (link)

[18] The provisional social security BGAs are based on the OBR's March 2019 forecasts. The provisional tax BGAs are based on OBR forecasts which were published in December 2019. These December 2019 forecasts incorporate tax data to October 2019 inclusive but use economic assumptions from March 2019.

**Table 2.5: SFC forecasts for some taxes and provisional Budget-setting BGAs, for 2020-21**

| £ million | SFC revenue forecast | Provisional BGA | Difference |
|---|---|---|---|
| Income Tax | 12,365 | 12,319 | 46 |
| Land & Buildings Transaction Tax | 641 | 557 | 85 |
| Scottish Landfill Tax | 116 | 87 | 29 |
| Total | 13,123 | 12,963 | 160 |

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding. Differences are calculated as revenue subtract BGA to show the effect on the Scottish Government's funding. The remaining devolved taxes are not covered by BGA arrangements. The SFC revenue forecasts and provisional BGAs are calculated on different bases, so comparisons should be interpreted with caution.

**Table 2.6: SFC forecasts for some social security spending and provisional Budget-setting BGAs, for 2020-21**

| £ million | SFC spend forecast | Provisional BGA | Difference |
|---|---|---|---|
| Attendance Allowance | 532 | 535 | 3 |
| Disability Living Allowance [1] | 718 | 669 | -49 |
| Personal Independence Payment | 1,583 | 1,601 | 19 |
| Carer's Allowance | 292 | 303 | 12 |
| Industrial Injuries Benefits | 80 | 85 | 5 |
| Severe Disablement Allowance | 7 | 9 | 1 |
| Total | 3,213 | 3,203 | -10 |

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding. Differences are calculated as BGA subtract spend to show the effect on the Scottish Government's funding. The other benefits being devolved to the Scottish Parliament in April 2020 are not covered by BGA arrangements and instead are funded through the Barnett formula. The SFC spending forecasts and provisional BGAs are calculated on different bases, so comparisons should be interpreted with caution.
[1] SFC spend forecast for DLA includes DLA working age, DLA child & DACYP and DLA pensioners.

2.24 Almost all social security forecasts in Table 2.6 reflect current UK Government policy because the benefits will continue to be administered by DWP during 2020-21.[19] This is important because once the forecasts are based on Scottish policy, we expect the forecasts of Scottish spending to increase given Ministerial announcements and the passage of the Social Security (Scotland) 2018 Act. Any differences between spending and the BGAs will have to be managed within the Scottish Budget. In contrast, the SFC revenue forecasts include Scottish Government tax policy changes since devolution.

2.25 The BGAs for all benefits and taxes (except income tax) are typically recalculated throughout the year, called in-year BGAs. This generally occurs

[19] Our Disability Living Allowance forecast includes the introduction of the new Disability Assistance for Children and Young People but does not include any future changes made to the working-age adult or pensioner benefits.

at the UK Autumn Budget, and the difference between each updated in-year BGA and its original Budget-setting BGA is known as an in-year reconciliation. As part of managing the Budget during the year the Scottish Government will need to manage any variations in the BGAs. For income tax, typically the BGA and revenue figures are fixed based on the forecast until outturn data are known and a reconciliation is applied the subsequent year.

2.26 The Scottish Government and HM Treasury have agreed flexibility for the Scottish Government to update the 2020-21 provisional Budget-setting BGAs after the OBR publish revised forecasts in March 2020. The OBR's forecasts in March 2020 will reflect updated data, UK Government policy and revised economic assumptions.

2.27 For fully devolved taxes and social security, updating the provisional Budget-setting BGAs would result in an early in-year adjustment in 2020-21 and likely reduce the scale of in-year reconciliations expected later in 2020-21.

2.28 For income tax, updating the Budget-setting BGA could reduce the size of the final reconciliation, however without updating the corresponding forecast of Scottish income tax revenue this may not be the case.

## Reconciliations

2.29 Reconciliations will have a significant effect on the Scottish Budget this year. The Scottish Budget is set in advance of each financial year, based on forecasts. Over time, information on actual revenues and spending becomes available and the forecasts are updated or aligned with outturn. The Scottish Government's funding is then altered in response to the outturn data and revised forecasts. These changes in funding are called reconciliations. Reconciliations can be applied in-year or as adjustments to future Budgets. The Scottish Budget 2020-21 is the first with significant reconciliations applied. In future years we can expect reconciliations to become an increasingly important part of the level of funding for the Scottish Budget.

2.30 Reconciliations can be either positive or negative. Negative reconciliations indicate that the Scottish Government previously received more funding in the Net Block Grant than the data now show it should have. Positive reconciliations indicate the Scottish Government previously received less funding than the data now shows it should have.

2.31 These reconciliations must be managed within the Scottish Budget. Below, we discuss the tools to do so along with an assessment of the Scottish Government's resource borrowing plans.

### In-year reconciliations for 2019-20

2.32 Devolved taxes and benefits with BGAs (with the exception of income tax) are subject to both in-year and final reconciliations.

2.33 The Scottish Government must manage any difference between forecast and outturn Scottish spending or revenue throughout the financial year (with the exception of income tax revenue, which is fixed). The BGAs are revised during the financial year, when the OBR publish in-year forecasts to accompany the UK Budget. These in-year forecasts result in an in-year BGA. The difference between the in-year and Budget-setting BGAs results in a change of funding called an in-year reconciliation.

2.34 The OBR will publish in-year forecasts for 2019-20 alongside the UK Budget in March 2020, which will enable the calculation of in-year reconciliations. Table 2.7 shows our estimate of the in-year reconciliations, using the provisional BGAs agreed between the Scottish Government and HM Treasury.

**Table 2.7: 2019-20 indicative in-year reconciliations (based on provisional BGAs)**

| £ million | Indicative in-year reconciliations applied in 2019-20 |
|---|---|
| 2019-20 Carer's Allowance | -4 |
| 2019-20 Scottish Landfill Tax | -6 |
| 2019-20 Land and Buildings Transaction Tax | 39 |
| Total | 30 |

Source: Scottish Government
Figures may not sum because of rounding.

2.35 The Scottish Government has decided to delay this in-year reconciliation to 2020-21. It has included £30 million of funding in the Scottish Budget 2020-21 to account for this. This indicative estimate is subject to change when the OBR provided updated forecasts in March 2020.

2.36 This delay results in an extra reconciliation applied in 2020-21. The Scottish Government will also have 2020-21 in-year reconciliations applied later in the financial year.

## Final reconciliations applied in 2020-21

2.37 The Scottish Budget 2020-21 will be adjusted for final reconciliations relating to previous years. Table 2.8 sets out the final reconciliations applied in 2020-21. These are based on outturn information and not subject to change.

**Table 2.8: Final reconciliations applied in 2020-21**

| £ million | Final reconciliations applied in 2020-21 |
|---|---|
| 2017-18 Income tax | -204 |
| 2018-19 Scottish Landfill Tax | -2 |
| 2018-19 Land and Buildings Transaction Tax | -3 |
| 2018-19 Carer's Allowance | 0 |
| 2018-19 Fines, forfeitures and fixed penalties | 2 |
| Total | -207 |

Source: Scottish Government

Figures may not sum because of rounding. The negative reconciliations sum to -£209 million. These negative reconciliations allow the Scottish Government to access £209 million resource borrowing in 2020-21.

2.38 The -£207 million final reconciliation applied in 2020-21 is largely based on the income tax reconciliation. Other fully devolved tax and social security reconciliations are smaller, but with the devolution of £3.4 billion of social security spending, these may become more significant in future years. A description of the reconciliation process for fully devolved taxes and social security can be found on our website.[20]

2.39 The Scottish Budget 2020-21 is the first to have an income tax reconciliation applied, relating to income tax revenue from 2017-18. This reconciliation reduces the Scottish Budget by £204 million in 2020-21.

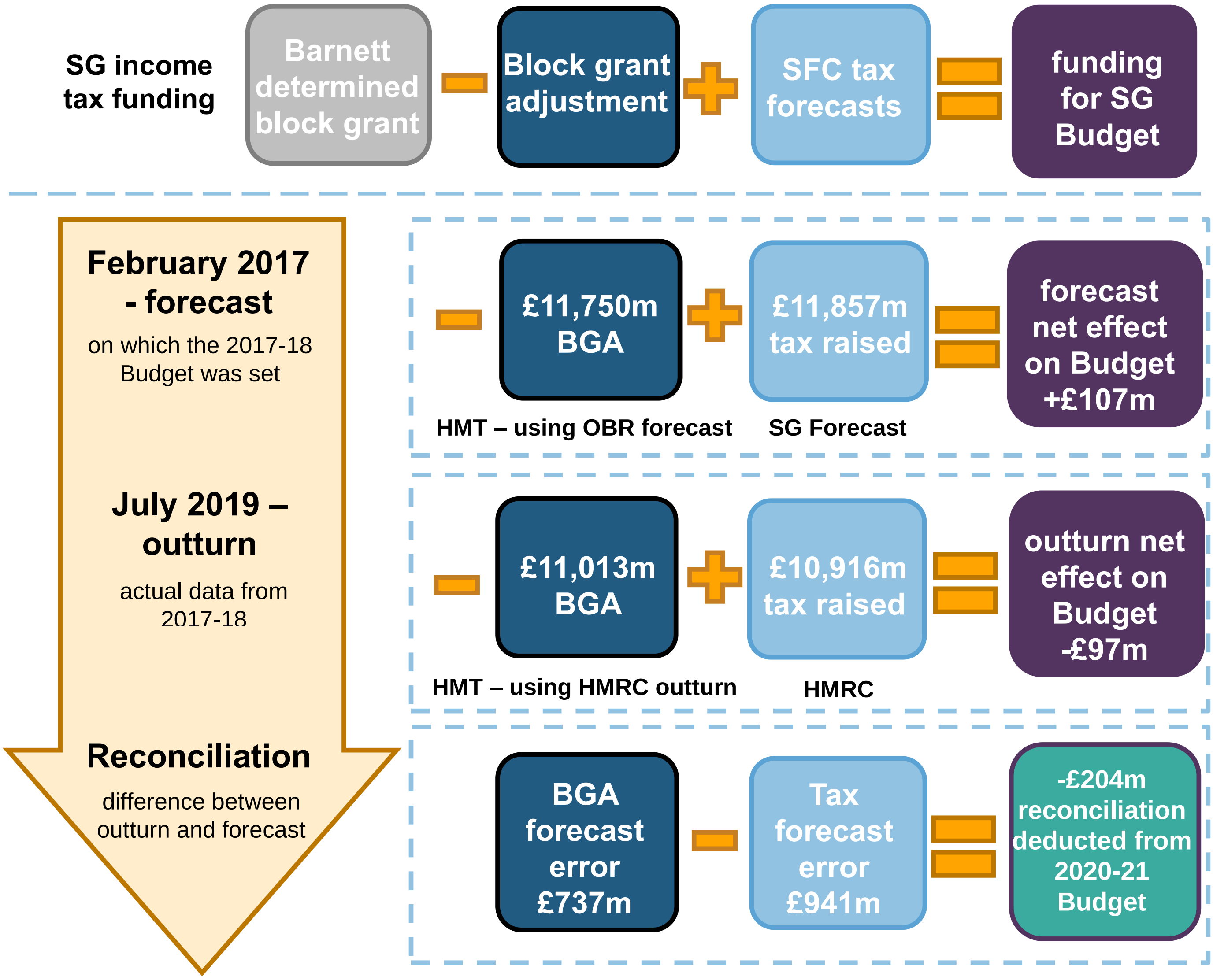
2.40 The size of the income tax reconciliation depends on the differences between how much revenue was forecast and how much was collected in both Scotland and the rest of the UK. Reconciliations do not directly relate to the relative performance of revenues in the two countries. Figure 2.2 sets out how the income tax reconciliation was calculated.[21,22]

[20] Scottish Fiscal Commission (2020) Explainers – Fully Devolved Tax and Social Security Reconciliations (link)

[21] We discussed the forecast errors which led to this reconciliation in our September 2019 Forecast Evaluation Report: Scottish Fiscal Commission (2019) Forecast Evaluation Report – September 2019 (link).

[22] 2017-18 income tax and BGA forecast errors were largely because both forecasting organisations did not have access to 2016-17 outturn income tax information. In terms of funding, the portion of the errors arising because of the 2016-17 outturn information cancelled one another out and had no effect on the reconciliation.

**Figure 2.2: 2017-18 income tax reconciliation**




Source: Scottish Fiscal Commission

### Indicative income tax reconciliations

2.41 How the Scottish Government chooses to respond to the reconciliations above should be considered alongside possible future reconciliations. Scottish income tax information becomes available each summer. Each release will result in an income tax reconciliation being calculated. This creates an ongoing reconciliation process.

2.42 We compare our February 2020 income tax forecasts with the provisional 2020-21 Budget-setting BGAs to estimate future reconciliations (indicative reconciliations). These provisional BGAs are based on OBR December 2019 forecasts which do not account for changes in the underlying economic outlook since March 2019. Our February 2020 and the OBR's December 2019 forecasts consider different data and are based on assumptions made at different times, so the indicative reconciliations should be considered with caution. The indicative reconciliations shown in Table 2.9 are highly likely to change once updated OBR forecasts are published in March 2020.

**Table 2.9: Final and indicative income tax reconciliations, based on 2020-21 provisional Budget-setting BGAs**

| £ million | Reconciliations | Applied in |
|---|---|---|
| 2017-18 income tax | -204 | 2020-21 |
| 2018-19 income tax | -555 | 2021-22 |
| 2019-20 income tax | -211 | 2022-23 |

Source: Scottish Fiscal Commission, Scottish Government.
Shaded cells indicate final reconciliations while unshaded cells are indicative reconciliations, based on 2020-21 provisional Budget-setting BGAs and February 2020 SFC forecasts. These indicative estimates will change following the publication of updated OBR forecasts alongside the March 2020 UK Budget.

2.43 Indicative reconciliations can be calculated each time the SFC or OBR provide updated forecasts. The final reconciliations will be calculated each summer once a new year of Scottish income tax information becomes available.

## Resource Management

2.44 In setting the Scottish Budget, the Scottish Government considers its Net Block Grant, including the size of the reconciliations and our forecasts of tax revenues. The Scottish Government can then decide if it wants to use its resource borrowing powers or draw down from the resource reserve.[23] These tools can be used to manage variation in funding and spending. Any resource borrowing or drawdowns from the Scotland Reserve are added to the funding position to calculate the total funds available to be spent in the Scottish Budget.

2.45 With the devolution of more powers to the Scottish Parliament, these tools are becoming increasingly important as the Scottish Budget becomes more complex.

### Resource Borrowing

2.46 The Scottish Government has the power to borrow for forecast errors up to an annual limit of £300 million and an overall limit of £1.75 billion.[24] This resource borrowing can be used to address the effects of forecast errors in both our forecasts, and forecasts of the Block Grant Adjustments (based on OBR forecasts).

2.47 The Scottish Government plans to use its resource borrowing powers for the first time in 2020-21, announcing plans to borrow £207 million. This borrowing

[23] The resource reserve is one part of a larger Scotland Reserve.

[24] In the case of a Scotland-specific economic shock, the annual resource borrowing limit is increased to £600 million.

will be repaid over the next five years. Box 2.1 sets out the current understanding of how resource borrowing will operate.

| **Box 2.1: Resource borrowing in practice** |
|---|
| The Scottish Government and HM Treasury have agreed that the Scottish Government can 'unlock' the borrowing powers in the fiscal framework based on any negative differences between forecast and outturn Budget positions. This includes:<br>• negative in-year reconciliations<br>• negative final reconciliations<br>• higher spend than forecast on devolved social security benefits<br>• lower tax revenue than forecast for fully devolved taxes<br><br>The Scottish Government can borrow for the total negative effects of forecast errors, subject to the overall limits. Forecast errors which result in increased funding for the Scottish Budget do not reduce the Government's ability to borrow. Currently the Scottish Government could borrow a maximum of £209 million to account for the negative reconciliations applied to 2020-21. Should any forecast errors next year further reduce funding, this borrowing limit for 2020-21 will increase up to the maximum annual limit of £300 million.<br><br>Resource borrowing can be drawn down at any point in the financial year. The Scottish Government can change its plans at any point and draw down more or less than planned, subject to the overall limits and the existence of reductions in funding caused by forecast error. |

### Resource Reserve

2.48 The Scottish Government has a cash reserve, the Scotland Reserve, which can be used to build up funds and draw them down in later years. The Scotland Reserve is split into resource and capital reserves with an overall limit of £700 million. The Scottish Government has no annual limit on the amount which can be paid into the Scotland Reserve, however a maximum of £250 million of resource funding can be drawn down annually.[25]

2.49 Table 2.10 shows how the resource reserve has been used so far and future plans.

[25] In the case of a Scotland-specific economic shock, the annual drawdown limit is waived.

**Table 2.10: Historic and planned use of the resource reserve**

| £ million | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
|---|---|---|---|---|
| Opening balance | 74 | 440 | 381 | 206 |
| Drawdowns | 0 | -250 | -250 | -106 |
| Additions | 366 | 191 | 75 | 0 |
| Closing balance | 440 | 381 | 206 | 100 |

Source: Scottish Government

Shaded cells reflect outturn and unshaded reflect Scottish Government plans. Figures may not sum because of rounding.

2.50 The Scottish Government currently forecast £206 million will remain in the resource reserve at the end of 2019-20. The Government are planning on drawing down £106 million in 2020-21 which would leave £100 million in the reserve for future years.

## Resource Assessment

2.51 In 2020-21 the Scottish Government is planning to draw down £106 million from the resource reserve, along with borrowing £207 million. These plans are within the limits of the fiscal framework and therefore we assess this borrowing to be reasonable.

2.52 This assessment should be considered within the context of an evolving Budget process which, for the first time, begins to fully incorporate the effects of devolution.

2.53 Budget management between years will also become more important. Reconciliations which adjust the budget to account for forecast errors in previous years, may become larger. Although our current estimates of the indicative income tax reconciliations in the next two years must be considered with caution, these predict much larger negative effects on future budgets than we have seen this year. The Scottish Government will need to consider how to manage these in future years.

2.54 Based on the information we have to date, and the evidence that the balance of the reserve has been falling in recent years, it would seem from these plans that the Scottish Government is not building up large reserves to mitigate the large expected income tax reconciliations in 2020-21 and 2021-22 shown in Table 2.9.[26] We will continue to report on the use of the Scotland Reserve in future publications.

2.55 The exact position of the reserve will remain uncertain as the Government may make further additions to the resource reserve in 2019-20 if there are any

[26] Subject to annual drawdown limits.

further underspends towards the end of the financial year.[27] It's likely that the 2019-20 reserve position and therefore total funding for 2020-21 will change.

2.56 By the time of the MTFS, anticipated in May 2020, the Scottish Government will have updated information on the size of the indicative reconciliations and of any additional funding provided by the UK Government following the March Budget. Based on this information the Scottish Government should consider how best to prepare for the future reconciliations.

## Capital Management

2.57 The Scottish Government's capital budget is determined by a similar process to the one set out above for resource, although with no BGAs or reconciliations. The Barnett-determined Block Grant is the funding provided by the UK Government. In the same approach as resource funding, the Scottish Government had made an additional allowance to account for anticipated consequentials based on the Conservative Party manifesto. The Scottish Government can then top-up this funding through its capital borrowing powers and use of a capital reserve to manage its spending on capital projects. Table 2.11 sets out the funding for capital spending included in the Scottish Budget.

**Table 2.11: Capital funding plans for the Scottish Budget 2020-21**

| £ million | 2020-21 |
|---|---|
| Barnett-determined Block Grant – capital [1] | 4,408 |
| Financial Transactions (FTs) [1] | 606 |
| Other [2] | 326 |
| Total capital funding | 5,340 |
| Capital borrowing | 450 |
| Drawdown from Scotland Reserve (capital and FTs) [3] | 37 |
| Other [4] | -10 |
| Total capital spending | 5,817 |

Source: Scottish Government
The table does not include non-cash budget. Figures may not sum because of rounding.
All components of the Budget will vary in 2020-21 reflecting changes to the Barnett-determined Block Grant following changes in UK Government spending and changes in the Scottish Government's plans for borrowing and the use of the Scotland Reserve.
[1] Agreed with HM Treasury (HMT) based on September 2019 Spending Round.
[2] The £326 million figure refers to anticipated Barnett CDEL consequentials.
[3] Includes planned drawdowns of £5 million for general capital spending and £32.2 million for FTs.
[4] Includes Glasgow City funding (£15 million) and repayment of Financial Transactions to HMT (-£25 million).

[27] As the Scottish Government cannot overspend on their Budget, it's reasonable to expect underspends, which may be paid into the resource reserve. Additionally, Barnett consequentials may be given to the Scottish Government late in the financial year. The resource reserve can be used to carry these over into future financial years.

2.58 The Scottish Government drew down less capital funding than planned from both the capital reserve and borrowing in 2018-19.

2.59 In 2019-20 the Scottish Government has had large negative consequentials for capital spending, including financial transactions, which reduce the expected size of the Scottish capital budget in 2019-20. In order to maintain the level of capital spending planned in 2019-20 the Scottish Government agreed an increase in the capital drawdown limits with HM Treasury. The Scottish Government plan to draw down a total of £181 million in 2019-20.

## Capital Borrowing

2.60 The Scottish Government can borrow for capital spending up to a maximum of £450 million each year up to a total limit of £3 billion. The Scottish Government published self-imposed principles for capital borrowing in its 2019 Medium Term Financial Strategy.[28] These include:

- introducing a contingency reserve of £300 million to be left unused
- borrowing between £250 million and £450 million each year until 2025-26 inclusive

2.61 Table 2.12 shows the Government's historic and planned capital borrowing.

**Table 2.12: Scottish Government historic and planned capital borrowing**

| £ million | 2017-18 | 2018-19 | 2019-20 Tranche 1 | 2019-20 Tranche 2 | 2020-21 |
|---|---|---|---|---|---|
| Borrowing | 450 | 250 | 200 | 250 | 450 |
| Agreed repayment period (years) | 25 | 10 | 20 | 25 | 25 |
| Interest rates (per cent) [1] | 1.9 | 1.0 | 0.6 | 1.0 | 1.0 |
| Principal repayments | 21 | 28 | | 47 | 73 |
| Debt stock - end of year | 1,036 | 1,258 | | 1,662 | 2,039 |
| Percentage of debt cap reached (end of year) | 35 | 42 | | 55 | 68 |

Source: Scottish Fiscal Commission, Scottish Government.
Shaded cells reflect historic capital borrowing while unshaded cells reflect planned borrowing. The Scottish Government split its 2019-20 borrowing into two tranches, with the first in October 2019 and the second planned for March 2020.
[1] Interest rates in years of planned borrowing are set by SFC assumptions.

2.62 We assess this historic and planned capital borrowing as reasonable, as it complies with the terms set out in the fiscal framework.

[28] Scottish Government (2019) Scottish Government's Medium Term Financial Strategy: May 2019 (link)

2.63 In December 2018 the Scottish Government planned to borrow the maximum £450 million in both 2018-29 and 2019-20.[29] Table 2.12 shows it borrowed less than planned in 2018-19 but still expects to borrow the maximum amount in 2019-20. Capital funding in 2020-21 may be more uncertain than previous years, as the Scottish Government has included £326 million in anticipated consequentials in its Budget. The Scottish Government may receive more or less capital funding than included in the Scottish Budget 2020-21 and changes in funding may be reflected in the actual level of borrowing in 2020-21.

2.64 Beyond 2020-21, the Scottish Government may choose to borrow in a number of ways. We illustrate potential future borrowing based on two scenarios. The first projects a low borrowing scenario, where the Scottish Government borrow £250 million each year with 10 year repayment terms. The second a high borrowing scenario where the Scottish Government borrows £450 million each year until the £2.7 billion self-imposed cap is reached in 2022-23, then borrows the maximum available in future years. In 2022-23 the Government can only borrow £400 million to keep the debt stock at £2.7 billion. Both scenarios are in line with the rules in the fiscal framework.

**Table 2.13: Percentage of the debt cap reached under high and low borrowing scenarios**

| Per cent | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|
| High borrowing scenario | 55 | 68 | 80 | 90 | 90 | 90 |
| Low borrowing scenario | 55 | 68 | 73 | 78 | 82 | 85 |

Source: Scottish Fiscal Commission, Scottish Government.
Shaded cells indicate the Scottish Government's planned borrowing. Unshaded cells reflect the high and low projected borrowing scenarios. We include the Scottish Government's self-imposed £2.7 billion borrowing cap in our scenario analysis, so borrowing will not exceed 90 per cent of the total £3 billion cap.

2.65 In our assessment we note that the debt stock has been increasing each year and continues to do so in each scenario, reaching at least 85 per cent of the debt cap by 2024-25.

## Capital Reserve

2.66 The Scotland Reserve capital reserve covers both capital funds and financial transactions. The annual drawdown limit of £100 million applies to the combined value of capital and financial transaction drawdowns.[30] In 2019-20 large negative consequentials reduced the expected size of the Scottish

[29] Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link)

[30] In the case of a Scotland-specific economic shock, the annual drawdown limit is waived. The £100 drawdown limit covers both capital and financial transaction drawdowns combined.

capital budget in 2019-20. The Scottish Government and HM Treasury have agreed to waive the drawdown limit with £181 million.

2.67 Tables 2.14 and 2.15 below shows historic and planned use of the capital and reserve, split by capital funding and financial transactions respectively.

**Table 2.14: Historic and planned use of the capital reserve**

| £ million | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
|---|---|---|---|---|
| Opening balance | 0 | 87 | 65 | 5 |
| Drawdowns | 0 | -22 | -60 | -5 |
| Additions | 87 | 1 | 0 | 0 |
| Closing balance | 87 | 65 | 5 | 0 |

Source: Scottish Government

Shaded cells reflect outturn while unshaded are Scottish Government plans. Figures may not sum because of rounding.

**Table 2.15: Historic and planned use of financial transaction reserve**

| £ million | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
|---|---|---|---|---|
| Opening balance | 0 | 11 | 159 | 38 |
| Drawdowns | 0 | 0 | -121 | -32 |
| Additions | 11 | 147 | 0 | 0 |
| Closing balance | 11 | 159 | 38 | 6 |

Source: Scottish Government

Shaded cells reflect outturn while unshaded are Scottish Government plans. Figures may not sum because of rounding.

2.68 The Scottish Government is planning to draw down almost the full capital and financial transaction reserves by the end of 2020-21, with a closing balance of £6 million.

2.69 In our December 2018 report, we noted the Scottish Government planned to draw down £85 million of the capital reserve in 2018-19 and £46 million in 2019-20.[31] Table 2.15 above shows that while the Scottish Government drew down less than planned in 2018-19, the planned drawdown for 2019-20 is now significantly higher than originally planned.

[31] Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link)

# Chapter 3
# Economy

## Introduction

3.1 We forecast the Scottish economy for two main reasons: to provide the necessary economic forecasts to feed into our fiscal forecasts; and to fulfil the Commission's remit of providing five-year forecasts of onshore Gross Domestic Product (GDP) growth. This chapter also provides our forecasts of economic factors such as productivity, wages, employment and investment.

3.2 The Scottish Budget occurring before the UK Budget has an effect on the way we prepare our forecasts. We use forecasts of the UK economy – usually from the OBR – as part of our process of building forecasts of the Scottish economy. In the absence of an updated UK economic outlook from the OBR, we have used forecasts of the UK economy published by the National Institute of Economic and Social Research (NIESR) in November 2019.

3.3 Our economy forecasts were finalised on 17 January 2020, so no new data or information received after this date were incorporated into the forecasts.

## Forecast summary

3.4 Over the course of 2018 and 2019, Brexit negotiations have played a dominant role in the economic narrative of Scotland and the UK. Uncertainty about both the nature and timing of Brexit has resulted in subdued growth over the last year and greater volatility between quarters. Looking ahead in 2020, the UK has now left the EU, and the unwinding of some Brexit-related uncertainty may support some additional growth. However, Brexit remains a risk to continued economic growth. Concerns about slowing global growth remain, particularly for the Euro Area, and this is expected to affect Scotland's trade prospects. The outlook for trade has been exacerbated by the potential for global trade wars.

3.5 As shown in Table 3.1, our estimate of productivity growth in Scotland has remained low and below our previous forecasts. As a result, we have revised down our forecast of trend productivity growth at the beginning of the forecast period. Offsetting slower productivity growth and weaker global conditions, higher UK and Scottish Government spending is expected to continue to support growth in the Scottish economy.

**Table 3.1: Headline economy forecasts, December 2018 and February 2020, per cent growth rates unless otherwise stated**

| GDP | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 |
|---|---|---|---|---|---|---|---|
| December 2018 | 1.4 | 1.2 | 1.0 | 1.0 | 1.1 | 1.2 | |
| February 2020 | 1.5 | 0.9 | 1.0 | 1.1 | 1.2 | 1.2 | 1.2 |
| **Trend productivity** | | | | | | | |
| December 2018 | 0.3 | 0.7 | 0.9 | 1.0 | 1.1 | 1.2 | |
| February 2020 | 0.2 | 0.3 | 0.6 | 0.9 | 1.1 | 1.2 | 1.3 |
| **Average nominal earnings** | | | | | | | |
| December 2018 | 2.0 | 2.3 | 2.5 | 2.8 | 3.0 | 3.1 | |
| February 2020 | 2.6 | 2.8 | 3.0 | 3.1 | 3.2 | 3.3 | 3.3 |
| **Average real earnings** | | | | | | | |
| December 2018 | -0.3 | 0.3 | 0.5 | 0.6 | 0.9 | 1.1 | |
| February 2020 | 0.6 | 1.0 | 1.1 | 1.0 | 1.2 | 1.2 | 1.2 |
| **Employment (millions)** | | | | | | | |
| December 2018 | 2.64 | 2.65 | 2.65 | 2.66 | 2.66 | 2.66 | |
| February 2020 | 2.67 | 2.68 | 2.67 | 2.67 | 2.68 | 2.68 | 2.69 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link).
Shaded cells refer to outturn available at time of publication.

3.6 In Scotland, earnings growth has continued to exceed our earlier expectations. After a period of subdued growth, earnings finally appear to be responding to tight conditions in the labour market. Earnings are also being supported by public sector pay policy and faster growth in the minimum wage and national living wage. As a result, we have revised up our forecast of earnings growth and this will support greater household consumption. However it should be noted that earnings growth, both nominal and real, remains below historical values over the forecast period.

3.7 Balancing all these factors, our forecast of headline GDP is similar to December 2018, with small upwards revisions from 2021 onwards. The fiscal framework provides additional borrowing powers for Scotland in the event of a Scotland-specific economic shock.[32] Our assessment is that a Scotland-specific economic shock, as defined by the fiscal framework, is not expected to occur. Supplementary Table S3.9 provides the details of our assessment.

[32] The agreement between the Scottish Government and the United Kingdom government on the Scottish Government's fiscal framework (link)

## Main Judgements

**Table 3.2: Economy forecast main judgements**

| Issue | February 2020 | Change since December 2018 |
|---|---|---|
| **1. Spare capacity** | 0.1 per cent in 2018 and 0.8 per cent in 2019 | Downward revisions from 0.8 per cent in 2018 and from 1.1 per cent in 2019, mainly reflecting new outturn data |
| **2. Trend productivity** | From growth of 0.3 per cent in 2019 to growth of 1.3 per cent in 2024 | Downward revisions in 2019 and 2020, as our estimates of trend productivity growth are still near zero and below expectations |
| **3. Long-run unemployment rate** | 4.0 per cent in all years | A downward revision from 4.25 per cent |
| **4. Nominal average annual earnings** | Growth increasing from 2.8 per cent in 2019 to 3.3 per cent in 2024, broadly aligning with productivity | Upward revisions to overall earnings profile, reflecting wage growth finally starting to respond to the tight labour market |
| **5. Population projections** | ONS 2018-based 50 per cent net EU migration | ONS 2016-based 50 per cent net EU migration |
| **6. Forecasts of the UK** | Short-term based on forecasts published by the National Institute of Economic and Social Research (NIESR) in November 2019, long-run view maintained in line with the OBR UK March 2019 forecasts | OBR UK October 2018 forecasts used in December 2018 |
| **7. Brexit** | Our Brexit assumptions are that:<br>• the UK leaves the EU on 31 January 2020<br>• this is followed by a transition period until December 2020<br>• new trading arrangements with the EU and others slow the pace of import and export growth<br>• the UK adopts a tighter migration regime than that currently in place | Difference in the date of exit but no substantial change in the effect of Brexit on our forecast, as the future trade relationship is still to be negotiated during the transition period |
| **8. Oil & gas** | Neutral impact of UK Continental Shelf activity on onshore economy | No change |
| **9. Savings ratio** | Broadly flat, picking up slightly in the later years of the forecast | No change |
| **10. Second round effects** | The Commission is not including second round economy effects from any policies | No change |

Source: Scottish Fiscal Commission

## Developments in the Scottish economy

### Brexit

3.8 The political context has developed since our last forecast in May 2019. At the time, with little prospect of the UK parliament voting to approve the Withdrawal Agreement (WA) and the deadline for Brexit being pushed back to October 2019, there was significant uncertainty about the nature and timing of Brexit. A no-deal or an indefinite delay to Brexit were both real possibilities, with a large number of scenarios between these two extremes.

3.9 Since our previous forecast and following a UK general election in December 2019, there is now certainty about a Brexit date and the ability of the UK Parliament to pass Brexit-related legislation. At the time of writing, the Withdrawal Agreement Bill is expected to have become law by the end of January 2020. This eliminates the possibility of a no-deal on 31 January or lengthy delays to Brexit.

3.10 The immediate uncertainty around Brexit is now lower than it was in 2019 and, as a consequence, we expect moderately higher household consumption and business investment in early 2020 than would otherwise have been the case. Although the short-term Brexit uncertainty has diminished, there remains significant long-term uncertainty around negotiations during the transition period and what might happen after the transition period.

3.11 Overall, we do not yet have sufficient evidence to suggest that there has been a significant and material change in the distribution of possible Brexit outcomes over the longer term. While we now have certainty that Brexit will happen, we have limited new information about what form it will take. We have therefore largely retained our previous Brexit assumptions and judgements.

3.12 Our current assumptions are that:

- the UK leaves the EU on 31 January 2020
- this is followed by a transition period lasting until December 2020
- after the end of the transition period, new trading arrangements slow the pace of import and export growth
- the UK adopts a tighter migration regime than that currently in place

3.13 These are similar to the Brexit assumptions in our December 2018 and May 2019 forecast except for the date of departure from the EU. They are also similar to the Brexit assumptions that NIESR used in its main-case November 2019 forecasts for the UK.

3.14 However, significant uncertainty remains about negotiations during the transition period and what the UK's relationship with the EU and other countries will be after the end of the transition period. In any scenario, we expect trade between the UK and the EU to be less free compared to when the UK was in the EU.

3.15 In one scenario, the UK may fail to negotiate a free trade agreement (FTA) with the EU before the end of 2020, and so would move on to World Trade Organisation (WTO) terms with the EU for a period of time. This outcome would be similar to a no-deal scenario as having no FTA with the EU would have many, though not all, of the negative economic effects of leaving the EU without a withdrawal agreement. Therefore, we are basing our forecast on an orderly Brexit and, as in December 2018 and May 2019 when we treated a no-deal scenario as a downside risk, we are now treating no-FTA as a downside risk to our forecast.

3.16 Overall, therefore, with some minor adjustments, our previous broad-brush Brexit assumptions remain appropriate. We will update our Brexit judgements once we have greater certainty about the UK's future trading relationship with the EU.

## Productivity

3.17 The growth rate of productivity has slowed since 2004, with the financial crisis exacerbating this trend. We estimate that trend productivity growth has averaged 0.4 per cent per year since 2008, compared to an average annual growth rate of 1.5 per cent over the 10 years before 2008.

3.18 As in our previous forecasts, we assume that productivity growth gradually increases from the low rates observed in recent years but remains well below its pre-crisis average over the forecast period.

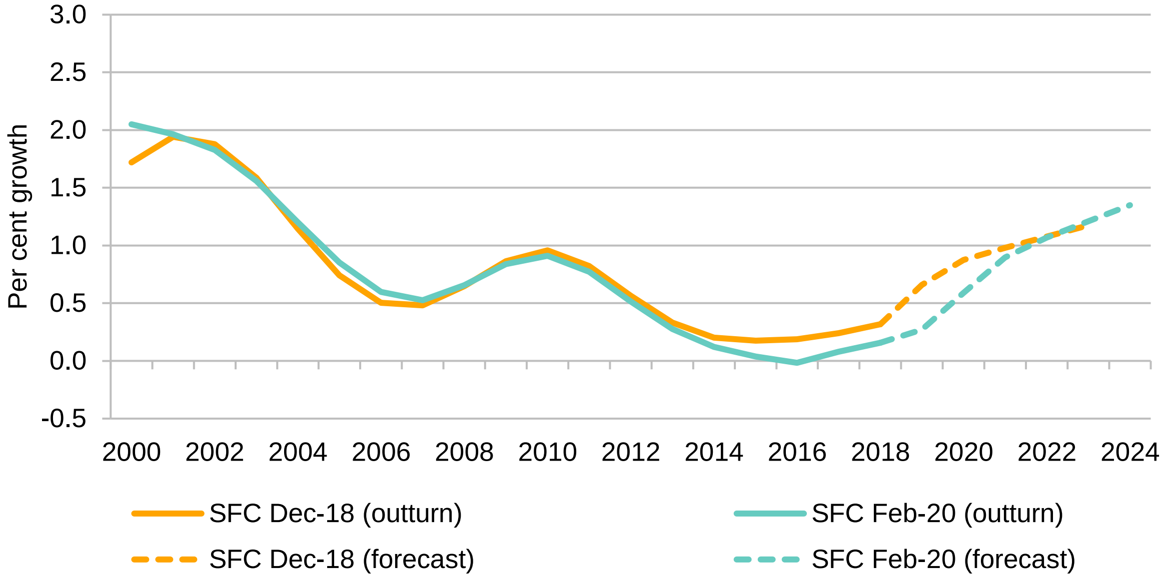
3.19 As shown in Figure 3.1, compared to our last report, we have revised down our productivity judgements by around 0.3 percentage points in 2019 and 2020. In our December 2018 and May 2019 reports, we expected productivity growth to be 0.7 per cent in 2019. Our estimate of productivity shows continuing near-zero trend growth, so we think that an immediate pick-up in productivity now looks implausible and that it will take longer for growth in output per hour to recover.

3.20 In May 2019, while we adjusted our GDP and business investment forecast in line with Brexit developments and their effect on uncertainty, we did not change our view on productivity.[33] Since May, we have had more outturn data showing slow productivity growth and that business investment continued to

[33] In May 2019 there were also downward revisions to trend estimates of productivity growth between 2015 and 2018. These are evident from Figure 3.1 and were driven by upward revisions to outturn data on employment, as shown in Figure 3.4, and thus total hours worked.

fall, and this has been compounded by the context of the global slowdown in 2019. For these reasons we now expect a reduced pace of productivity growth in the near term.

**Figure 3.1: Trend productivity growth, outturn and forecast**




Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link).

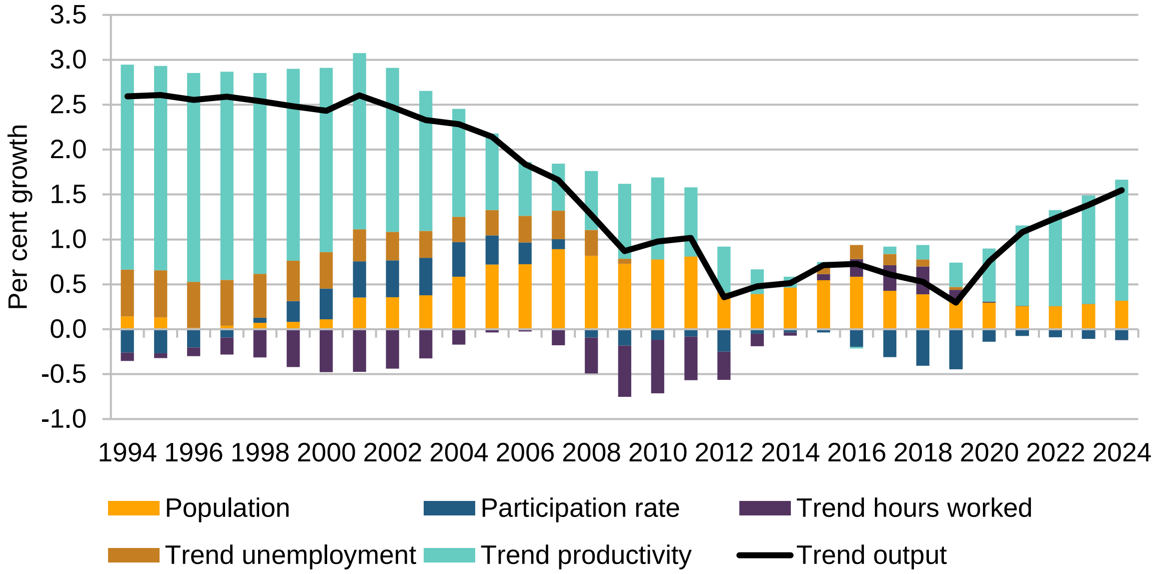
## Trend GDP

3.21 Our forecast of trend GDP growth is shown in Figure 3.2 and Table 3.3, which include the contribution of each component.

3.22 Since May 2019, there have been two main changes to our forecast of trend GDP growth. The downward revisions to our productivity assumptions have reduced the rates of trend GDP growth, especially in 2019 and 2020.

3.23 We have also updated the population projections in our forecast to the latest, 2018-based 50 per cent EU migration variant. The ONS has revised up its migration projections, so the incorporation of the new population data has increased trend GDP growth in 2023 and 2024.

**Figure 3.2: Trend GDP growth and contribution of components**




Source: Scottish Fiscal Commission

**Table 3.3: Growth of trend GDP and contribution of components**

| Per cent | Trend GDP growth | 16+ population | 16+ participation rate | Long-run unemployment rate | Trend average hours worked | Trend productivity |
|---|---|---|---|---|---|---|
| 2018 | 0.5 | 0.4 | -0.4 | 0.1 | 0.3 | 0.2 |
| 2019 | 0.3 | 0.3 | -0.4 | 0.0 | 0.1 | 0.3 |
| 2020 | 0.8 | 0.3 | -0.1 | 0.0 | 0.0 | 0.6 |
| 2021 | 1.1 | 0.3 | -0.1 | 0.0 | 0.0 | 0.9 |
| 2022 | 1.2 | 0.3 | -0.1 | 0.0 | 0.0 | 1.1 |
| 2023 | 1.4 | 0.3 | -0.1 | 0.0 | 0.0 | 1.2 |
| 2024 | 1.5 | 0.3 | -0.1 | 0.0 | 0.0 | 1.3 |

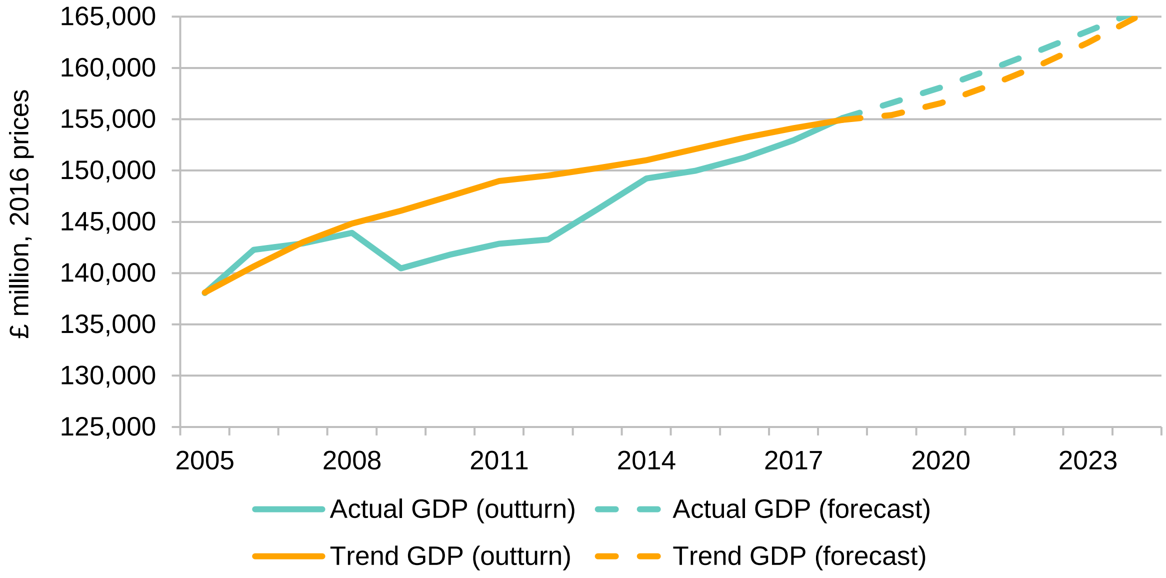
Source: Scottish Fiscal Commission
Figures may not sum because of rounding.

## Spare capacity in the economy

3.24 Spare capacity shows the economy's position relative to its estimated trend. Figure 3.3 shows that, after a period below trend, the level of GDP in 2018 was close to its potential. In 2019, GDP grew by more than its estimated trend and this resulted in a small positive deviation of output from potential.

3.25 The economy already being slightly above its estimated trend position will act to limit growth in the coming years. We expect the small positive output gap of 1.0 per cent in 2020 to gradually close over the forecast horizon.

**Figure 3.3: Trend and actual GDP, outturn and forecast, annual**




Source: Scottish Fiscal Commission

## Employment

3.26 The December 2019 outturn data suggest the labour market appears to be reaching a turning point, with employment no longer rising in 2019 Q2 and Q3 as shown in Figure 3.4. The unemployment rate has also stabilised. This can be explained by weakening labour demand. Survey indicators of hiring intentions, such as the IHS Markit and Royal Bank of Scotland PMI composite employment index, have decreased during 2019, despite recovering in the most recent period. The latest Royal Bank of Scotland Report on Jobs also indicates softer vacancies growth during 2019, especially for permanent jobs.[34]

3.27 The labour market however remains tight. Business surveys such as the Scottish Chambers of Commerce Quarterly Economic Indicator and the Bank Agents' Summary of Business Conditions continue to report limited spare capacity in the labour market, as recruitment difficulties remain elevated in both Scotland and the UK.[35]

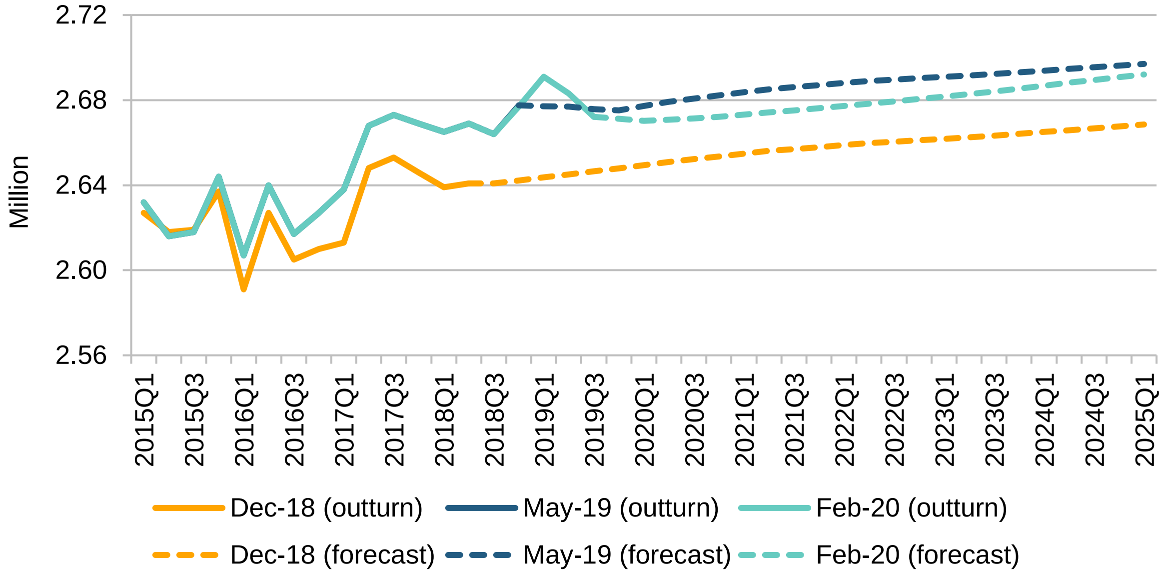
3.28 The unemployment rate, moreover, is still at historically low levels. Therefore we have maintained our long-term unemployment assumption at 4.0 per cent compared to May 2019. Employment is expected to continue to grow, although at a slower rate than over the last few years. As shown in Figure 3.4, in level terms, employment forecasts are revised up from December 2018,

[34] Royal Bank of Scotland (2020) Royal Bank of Scotland (RBS) Report on Jobs – 10 January 2020 (link)

[35] Scottish Chamber of Commerce (2019) Quarterly Economic Indicator results for Q3 of 2019 (link), Bank of England (2019) Agents' summary of business conditions – 2019 Q4 (link)

because of upward revisions to outturn data, while there are smaller changes from May 2019.

**Figure 3.4: Employment level, outturn and forecast, quarterly**




Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2019) Scotland's Economic and Fiscal Forecasts – May 2019 (link), Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link).

## Earnings and household incomes

3.29 Since our December 2018 forecast, we finally started to see evidence of employers responding to the exceptionally low unemployment rate, and we reflected this in our subsequent forecasts. In May 2019, we noted that earnings growth in 2018 had generally been above expectations and we revised up our overall earnings profile. Earnings in 2019 have continued to grow in response to the tight labour market, and are also being supported by public sector pay policy and faster growth in the minimum wage and national living wage. Therefore, we have now made further upward revisions to earnings growth over the period 2019 to 2021.

3.30 Table 3.4 presents the latest figures for average earnings growth from the available data sources, alongside our current and previous earnings forecasts for the last three years.

**Table 3.4: Data on nominal average earnings growth in Scotland**

| Per cent | Average 2010 to 2016 | 2017 | 2018 | 2019 |
|---|---|---|---|---|
| ASHE (workplace based) | 1.4 | 0.9 | 3.3 | 1.6 |
| RTI (mean) [1] | | 2.1 | 2.5 | *3.3* |
| LFS | 2.1 | -1.5 | 3.8 | *3.5* |
| QNAS COE-based measure [2] | 1.9 | 1.7 | 2.0 | *4.1* |
| Average | 1.8 | 0.8 | 2.9 | *3.1* |
| SFC December 2018 | | 1.5 | 2.0 | 2.3 |
| SFC May 2019 | | 1.0 | 2.6 | 2.6 |
| SFC February 2020 | | 1.4 | 2.6 | 2.8 |

Source: Scottish Fiscal Commission, ONS (2019) Annual Survey of Hours and Earnings (ASHE) access via nomisweb (link), HMRC (2019) UK Real Time Information (link), ONS (2019) Labour Force Survey Gross weekly earnings of full-time employees by region (link).

Italics for 2019 are part-year data expressed as annualised growth rates for comparison to previous years. LFS is average Gross Weekly Earnings. ASHE data are up to April 2019.

[1] The mean RTI rate for 2019 is annual growth for the four quarters to 2019 Q1. Median RTI data, available up to October 2019, also suggest an increase in average earnings growth between 2018 and 2019.

[2] QNAS only contains compensation of employees (COE) data for the whole economy. It does not report average annual earnings figures. The data we present in this table are based on SFC calculations applied to QNAS COE data.

3.31 As in previous reports we note mixed signals from the available earnings data. While RTI, LFS and QNAS all indicate increasing earnings growth in 2018 and 2019, ASHE data indicates slower earnings growth in 2019. Looking across all of these measures and thinking about broader economic conditions, we believe earnings growth has risen in 2018 and 2019.

3.32 The Real Time Information (RTI) Pay As You Earn (PAYE) publication is a data source on which we place increasing weight in forming our overall earnings judgement. However the RTI publication was recently changed making it less useful for our purposes. In particular, the latest publication included only median pay at regional level, not mean pay. Mean pay is a more appropriate measure of average earnings growth to inform our forecast. In discussion with HMRC and the ONS we expect mean RTI earnings for the UK regions to be reinstated in future releases.

3.33 Regional pay data were last released on a mean basis in July 2019 with data up to 2019 Q1. Using these data we estimate annual growth for the four quarters to 2019 Q1 of 3.3 per cent, compared to calendar-year growth of 2.5 per cent for 2018. As with other sources, RTI suggests rising earnings growth compared to the last few years.

3.34 As presented in Table 3.4, on balance across all sources, average earnings growth is up from 2.9 per cent in 2018 to 3.1 per cent in 2019. While we do not directly align our earnings forecast to this average rate, we revised up our estimate of 2019 earnings growth from 2.6 per cent in May 2019 to 2.8

per cent, consistent with the broader evidence of rising pay growth in the last year.

3.35 In addition to the tight labour market, there are other factors which have contributed to stronger earnings growth in 2018 and 2019. These include higher economic growth in 2018 feeding through to higher wages, public sector pay growth, and increases in the national minimum wage and national living wage.

3.36 Countering this, we believe pay growth will remain moderate in the longer term, because of factors such as continued low productivity growth and recent evidence that the labour market is no longer tightening. In addition, ongoing uncertainty around the new UK-EU trade relationship after Brexit is likely to weigh on economic activity, at least in the near term. There has already been evidence that pay pressures started to ease at the end of 2019.[36]

3.37 On balance, we have revised up our outlook for earnings from December 2018, but our forecast of nominal average earnings growth remains weak compared to historical values of around 4.5 per cent. With inflation around 2 per cent over the forecast, real earnings growth is also still low.

**Table 3.5: Nominal and real average earnings growth**

| Per cent | Forecast | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 |
|---|---|---|---|---|---|---|---|---|
| Nominal | December 2018 | 2.0 | 2.3 | 2.5 | 2.8 | 3.0 | 3.1 | |
| | February 2020 | 2.6 | 2.8 | 3.0 | 3.1 | 3.2 | 3.3 | 3.3 |
| Real | December 2018 | -0.3 | 0.3 | 0.5 | 0.6 | 0.9 | 1.1 | |
| | February 2020 | 0.6 | 1.0 | 1.1 | 1.0 | 1.2 | 1.2 | 1.2 |

Source: Scottish Fiscal Commission
Shaded cells refer to outturn available at time of publication.

## GDP and expenditure components

3.38 The Commission forecasts consumption, investment, net trade and government spending separately. These sum to create a pathway for GDP.

3.39 Household consumption growth slowed to 0.1 per cent during 2018.[37] Consumer confidence in Scotland remains low, related in part to ongoing Brexit uncertainty. The Scottish Government Consumer Sentiment Indicator has been negative since the EU Referendum and reached record lows at the start of 2019.[38] We expect household consumption to gradually increase in

[36] Royal Bank of Scotland (2020) Royal Bank of Scotland (RBS) Report on Jobs – 10 January 2020 (link)

[37] Scottish Government (2019) Quarterly National Accounts Scotland 2019 Quarter 2 (link)

[38] Scottish Government (2019) Scottish Consumer Sentiment Indicator Quarter 3 2019 (link)

line with earnings and as consumer sentiment recovers, at least in part, with diminishing Brexit uncertainty.

3.40 Similarly to our previous reports, we predict consumption growth to remain low in coming years because of limited growth in real average earnings and employment, combined with flattening consumer credit and weak consumer sentiment.

3.41 The outlook for business investment in 2020 is slightly more positive than in our previous forecast. With some of the Brexit-related uncertainty now removed, we expect some confidence to return among businesses, which should help to unlock delayed investment. However a period of uncertainty is likely to remain as the UK negotiates its new future trade relationships with the EU and other countries. We expect business investment will be positive but will not contribute significantly to GDP growth over the forecast horizon.

3.42 Net trade growth contributed positively to economic growth in 2018 thanks to strong export growth, especially for manufactured goods, driven by sterling's depreciation. Over the first half of 2019, exports growth has been negative and the net trade balance has deteriorated, reflecting the slowdown in global trade mainly caused by trade disputes.

3.43 As in our last forecast, we expect net trade to have a negative effect on GDP growth in 2019. Thereafter, the outlook will largely depend on the outcome of the UK's trade negotiations with EU and non-EU countries. Overall, we still assume net trade will play a minor role over the forecast period.

### Government

3.44 The public sector, including consumption and investment spending, accounts for around a quarter of GDP. General Government expenditure in Scotland includes spending by all levels of government: Scottish Government expenditure, expenditure by other UK Government departments in Scotland, and spending by local authorities in Scotland.

3.45 For Scottish Government expenditure in 2020-21, our figures are consistent with the Scottish Government's plans set out in the Scottish Budget 2020-21. Thereafter, we assume this new baseline will grow in line with the OBR March 2019 forecast of UK RDEL and CDEL expenditure.[39] For UK Government and local authority spending in Scotland, we also use OBR forecasts from March 2019.

3.46 Compared to December 2018 and May 2019, the main change is an upward revision to our forecast of Government consumption and investment growth in 2020-21, driven by the Scottish Government expenditure component. This is

[39] Resource Departmental Expenditure Limits and Capital Departmental Expenditure Limits

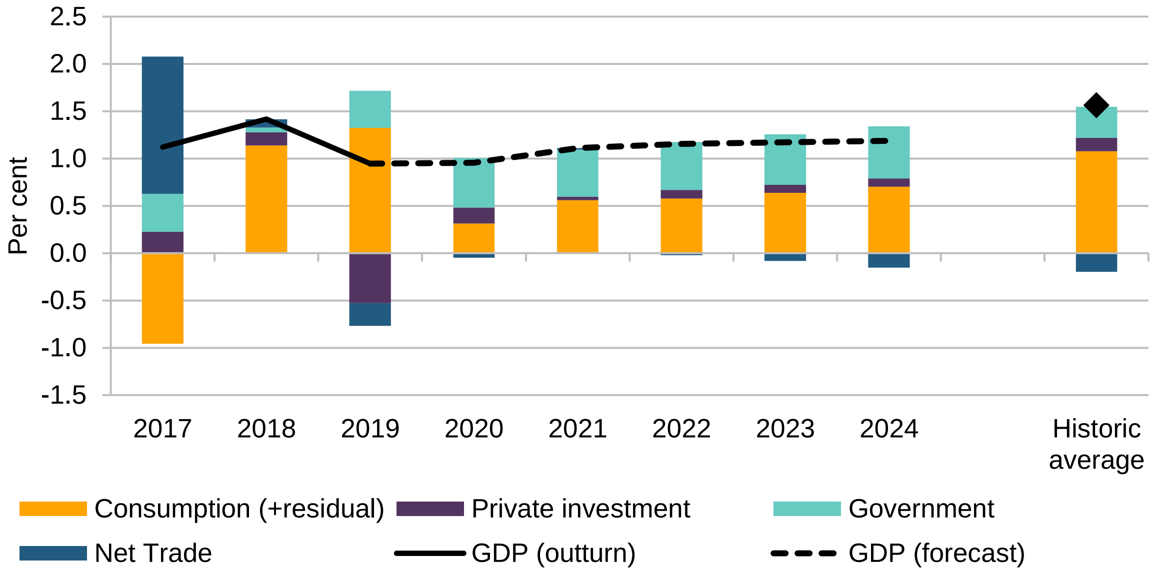
primarily explained by a higher Block Grant following the UK spending increases set out in the September 2019 Spending Round and the inclusion of anticipated consequentials from policies announced during the UK General Election. Further details on these funding elements are provided in Chapter 2.

3.47 Overall, this upward revision does not have a material effect on our GDP forecast. We expect General Government expenditure to account for around half of GDP growth over the next five years, as in our previous forecasts.

## GDP growth

3.48 The contribution of each of the components to growth in GDP are shown in Figure 3.5.[40]

**Figure 3.5: Contributions by component of expenditure to growth in GDP**




Source: Scottish Fiscal Commission
Historical average is based on growth from 1998 to 2008.

[40] The 2018 net trade contribution in Figure 3.5, which is flat, is not consistent with the October 2019 Quarterly National Accounts Scotland (QNAS) data, which show strong positive growth in net trade in 2018. This is because of revisions to QNAS trade data between the August 2019 release underlying our forecast and the latest publication in October 2019. This is counteracted by revisions to household consumption growth in the opposite direction.

# Chapter 4
# Tax

## Income Tax

### Forecast

**Table 4.1: Forecast revenue for non-savings non-dividend income tax**

| £ million | 2017-18 | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|---|
| | 10,916 | 11,378 | 11,677 | 12,365 | 12,897 | 13,447 | 14,059 | 14,722 |

Source: Scottish Fiscal Commission, HMRC (2019) Scottish Income Tax Outturn Statistics (link).
Shaded cells refer to outturn available at time of publication.

### Background

4.1. The Scottish Parliament has control of non-savings and non-dividend (NSND) income tax rates and bands. NSND income tax is paid on all income other than from savings or dividends. NSND income tax falls mainly on employment income, income from property, pension income, and profits for the self-employed.

4.2. Income tax is partially devolved. The UK Government is responsible for defining the income tax base, including setting or changing income tax reliefs and the personal allowance. The Scottish Government is responsible for all income tax rates and bands applied to taxpayers resident in Scotland. Her Majesty's Revenue and Customs (HMRC) remains responsible for the collection and management of Scottish income tax.

### Scottish Government policy

4.3. In the 2020-21 Scottish Budget the Scottish Government announced that it would freeze the higher rate threshold at £43,430 in 2020-21. This policy raises NSND income tax revenue by £51 million in 2020-21. Table 4.2 shows Scottish income tax rates and bands for 2020-21. From 2020-21 onwards, we assume that all bands will be uprated in line with the Consumer Price Index, other than the Top Rate Threshold, which we assume is frozen in cash terms at £150,000 throughout the forecast period. The rates and bands we have used to produce our forecast can be found in Supplementary Table S4.3.

**Table 4.2: NSND income tax rates and bands for 2020-21**

| Tax band range | Band name | Tax rate (per cent) |
|---|---|---|
| Above £12,500 to £14,585 [1] | Starter | 19 |
| Above £14,585 to £25,158 | Basic | 20 |
| Above £25,158 to £43,430 | Intermediate | 21 |
| Above £43,430 to £150,000 [2] | Higher | 41 |
| Above £150,000 | Top | 46 |

Source: Scottish Fiscal Commission

[1] Assuming individuals are in receipt of the standard UK Personal Allowance. We assume that the Personal Allowance will remain frozen at £12,500 in 2020-21, as announced in the UK Budget 2018.[41]

[2] Individuals earning more than £100,000 have their Personal Allowance reduced by £1 for every £2 earned above £100,000.

4.4. Table 4.3 shows our costing of the 2020-21 policy. More details can be found in Annex A.

**Table 4.3: Income tax 2020-21 policy costing**

| £ million | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|
| Static costing | 59 | 62 | 66 | 71 | 75 |
| Behavioural change | -7 | -8 | -10 | -11 | -12 |
| Post-behavioural costing | 51 | 54 | 56 | 59 | 63 |

Source: Scottish Fiscal Commission

Figures may not sum because of rounding.

## Change since December 2018

4.5. Changes to our forecast since December 2018 are shown in Table 4.4.

4.6. In December 2018 we had assumed all thresholds for 2020-21 would be uprated with inflation and the fact that SG has frozen higher rate threshold for this year, plus new outturn data and revised economy forecasts, in particular earnings growth, has led to revisions in our income tax forecast from 2020-21 onwards. We discussed updates in how we account for UK policy measures in our May 2019 report.[42]

[41] HM Treasury (2018) Budget 2018 (link)

[42] Scottish Fiscal Commission (2019) Scotland's Economic and Fiscal Forecasts – May 2019 (link)

Table 4.4: Change in NSND income tax revenue since December 2018

| £ million | 2017-18 | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|---|
| December 2018 | 11,008 | 11,452 | 11,684 | 12,285 | 12,746 | 13,242 | 13,805 |
| Economy earnings | | 129 | 237 | 321 | 411 | 485 | 544 |
| Economy employment | | -18 | -12 | -48 | -55 | -57 | -55 |
| PUT 2016-17 data | | -20 | -32 | -47 | -61 | -77 | -93 |
| UK policy measures | | -79 | -117 | -120 | -130 | -135 | -140 |
| 2017-18 outturn | -92 | -90 | -98 | -110 | -119 | -129 | -140 |
| Other | | 11 | 26 | 47 | 69 | 87 | 111 |
| Policy recostings | | -6 | -11 | -15 | -19 | -25 | -32 |
| February 2020 pre-measures | 10,916 | 11,378 | 11,677 | 12,314 | 12,843 | 13,390 | 14,000 |
| 2020-21 policy costing | | | | 51 | 54 | 56 | 59 |
| February 2020 post-measures | 10,916 | 11,378 | 11,677 | 12,365 | 12,897 | 13,447 | 14,059 |
| Change since December 2018 | -92 | -74 | -7 | 80 | 151 | 205 | 254 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link), HMRC (2019) Scottish Income Tax Outturn Statistics (link).
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

## 2017-18 Outturn Data

4.7. In July 2019 HMRC published outturn income tax data for the 2017-18 tax year.[43] This figure, at £10,916 million, was £92 million below our December 2018 forecast of that year. Our September 2019 Forecast Evaluation Report sets out our analysis of the 2017-18 outturn data.[44]

4.8. In May 2019 we committed to considering how best to use the HMRC Real-Time Information (RTI) data published alongside the 2017-18 outturn.[45] In our September 2019 Statement of Data Needs, we noted that RTI data are not directly comparable to outturn.[46] While we are continuing to analyse and monitor the relationship between RTI and outturn, we do not currently adjust our forecasts using the RTI data.

## Model developments

4.9. We have reviewed how we model taxpayer migration behavioural responses to differences in Scottish and UK income tax policy. We think the available literature suggests a slightly higher migration response than we included in our December 2018 forecast. As a result, we have revised our migration response estimate from £6 million to £8 million in 2019-20, with gradually increasing adjustments in later years. This results in a small downwards revision to our forecast. These adjustments are small in the context of total

[43] HMRC (2019) Scottish Income Tax Outturn Statistics (link)
[44] Scottish Fiscal Commission (2019) Forecast Evaluation Report (link)
[45] Scottish Fiscal Commission (2019) Scotland's Economic and Fiscal Forecasts – May 2019 (link)
[46] Scottish Fiscal Commission (2019) Statement of Data Needs – September 2019 (link)

income tax revenues. We will continue to keep our taxpayer behaviour estimates under review and will publish occasional papers discussing our methodology as necessary.

### Updates to previous policy costings

4.10. Updated costings of policies from previous Scottish Budgets can be found in Annex B. As we now have 2017-18 outturn data the effect of the 2017-18 income tax policy is in our forecast baseline and we no longer provide a separate costing of this policy.

### HMRC Forecasts

4.11. We use HMRC's forecasts of Gift Aid and Tax-Motivated Incorporations (TMI) to create our forecasts. The Scottish Budget 2020-21 has come before the UK Budget, and so HMRC have not produced updated Gift Aid or TMI estimates. We have used the numbers shared with us in May 2019 to produce this forecast.

## Assumptions about the distribution of income

4.12. A given increase in total NSND incomes can lead to different increases in income tax revenues depending on where in the income distribution the increase occurs. For example, if a higher rate taxpayer with a marginal tax rate of 41 per cent sees their income grow by £100, they would pay £41 more in income tax. If a basic rate taxpayer receives £100 more income, then income tax revenues would increase by only £20. In previous forecasts, we have assumed that growth in income occurs evenly across the income distribution.

4.13. In its Pre-budget Scrutiny 2020-21 report the Finance and Constitution Committee recommended that the SFC reflects on distributional issues and writes to the Committee with findings once 2018-19 SPI data are available.[47] In our letter responding to this report we made a number of commitments.[48] These were:

- For this report, to reflect on the latest available distributional information, consider whether our judgement on distributional effects needs updating, set our judgment out clearly, and provide sensitivity analysis.
- To write to the Committee with more detailed and specific findings on distributional issues in summer 2020 once further data are available. In

[47] Finance and Constitution Committee (2019) Pre-budget scrutiny 2020-21 (link)
[48] Scottish Fiscal Commission (2019) Letter from SFC to Finance and Constitution Committee in response to Pre-budget scrutiny 2020-21 report (link)

particular, we'll compare Scotland to the UK and show how distributional issues could affect the Scottish budget over the longer term.

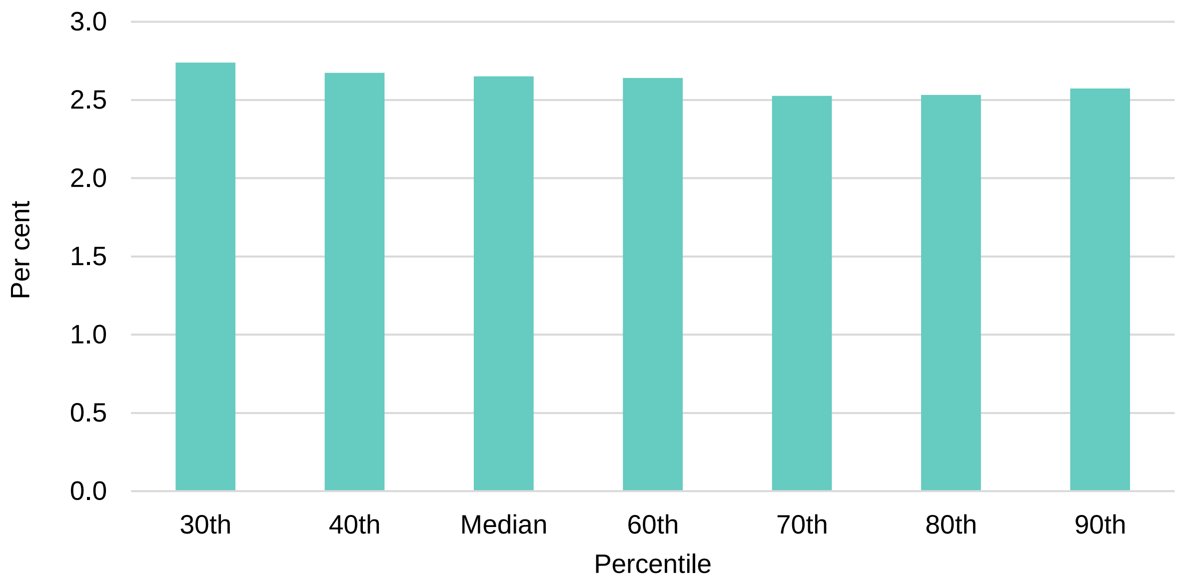
- To consider distributional issues as part of our ongoing analysis of fiscal risks.

4.14. This section fulfils the first of these commitments. We acknowledge the significant concerns about distributional issues and in particular the effect that any divergence between Scotland and the UK could have in the longer term via the fiscal framework. We will cover this aspect of distributional issues in a report in summer 2020.

4.15. For this forecast we have retained our judgement, that over the next five years, growth in incomes will be evenly spread across the income distribution. While growth can be quite variable across the income distribution from one year to the next, we do not see evidence of a persistent pattern over the longer term that we could build in to our forecast.

4.16. Figure 4.1 shows average growth in earnings at different points in the income distribution. We have considered the average growth over the period from 2003 to 2019. We focus on the 30th percentile and upwards as those in the lower percentiles earn below the personal allowance and therefore do not pay income tax. While there is some small variation, over this period of time growth in earnings has been roughly even across the income distribution – around 2.5 to 2.6 per cent for most individuals.

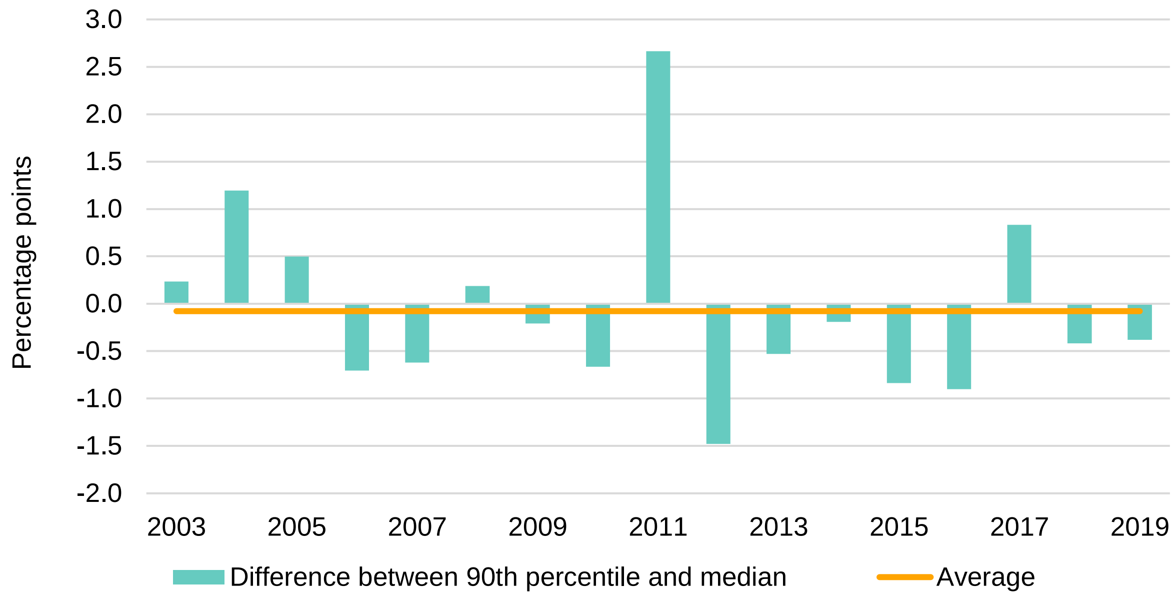
**Figure 4.1: Average annual growth in gross annual earnings by percentile, Scotland, 2003 to 2019**




Source: Scottish Fiscal Commission, ONS (2019) Annual Survey of Hours and Earnings (residence basis) access via nomisweb (link).

4.17. Of particular interest are individuals with the highest earnings, as they have the greatest effect on total income tax revenues. Figure 4.2 shows how growth in earnings at the 90th percentile has compared to growth in earnings of the median earner since 2003. While the difference between growth at the 90th percentile and the median can vary substantially between years, there does not appear to be a persistent pattern over time, with the average difference close to zero.

**Figure 4.2: Difference in earnings growth between 90th percentile and median, 2003 to 2019**




Source: Scottish Fiscal Commission, ONS (2019) Annual Survey of Hours and Earnings (residence basis) access via nomisweb (link).

4.18. At present we do not believe that the annual variation demonstrated in Figure 4.2 is predictable, and over the longer term we expect such variation to average to zero. As the sensitivity analysis in Box 4.1 shows, while a different assumption would have some effect on our forecast, this effect is still relatively small.

**Box 4.1: The distribution of income and growth in income tax revenues – sensitivity testing**

In this box, we present sensitivity analysis that illustrates the effect of making different assumptions about growth across the income distribution. This sensitivity analysis is highly illustrative focussing only on employment earnings. In the scenarios we ran, total earnings growth is fixed at 3 per cent, but we vary the way this earnings growth is distributed between taxpayers.

We looked at two simple scenarios, one where higher earners receive relatively faster earnings growth, and one where higher earnings receive relatively slower earnings growth. Over the last five years growth at the 90th percentile has on average deviated from the median by 0.3 percentage points. While we don't consider this to be a persistent trend, we have considered the following two sensitivities:

- The median taxpayer has earnings growth of 2.9 per cent, while a taxpayer at the 90th percentile has earnings growth of 3.2 per cent.
- The median taxpayer has earnings growth of 3.1 per cent, while the taxpayer at the 90th percentile has earnings growth of 2.9 per cent.

In the first scenario where higher earners see faster earnings growth, income tax revenues are around £50 million higher in 2020-21 than they would have been if the earnings growth had been spread evenly among all taxpayers. In the second scenario, income tax revenues are around £41 million lower than would otherwise have been the case.

These numbers are relatively small in the context of total income tax revenues; £50 million is around 0.4 per cent of total income tax revenues. In comparison, increasing total earnings growth by just 0.1 percentage points each year adds £50 million to the forecast. While the distribution of earnings growth does affect revenues, the effects of any changes in the distribution could be outweighed by even small changes to total earnings growth.

## Forecast uncertainty

4.19. We assess the sensitivity of our income tax forecast to the alternative economy scenarios considered in Chapter 3. This analysis can be found in Figure S4.3 in our Supplementary Tables.

4.20. We also assess how taxpayers' behavioural responses to income tax policy would change if we made different assumptions about their behaviour. This analysis can be found in Supplementary Table S4.10.

4.21. Another source of uncertainty is the response to UK Government policy decisions. Because this Scottish Budget has taken place before the UK Budget, we do not yet know what income tax policy will be in the rest of the UK. Under our current assumptions, there will not be an increase in the gap between the income tax systems in Scotland and the rest of the UK. If the gap between the tax system in Scotland and the rest of the UK does increase, the behavioural response to this is a risk to Scottish income tax revenues.

## Comparison to OBR

4.22. The Scottish Parliament has asked us to compare the growth rates in our income tax forecast to those in the OBR's forecast of Scottish NSND income tax revenues. Table 4.5 compares our income tax forecast, and the growth rates in our forecast, to the OBR's December 2019 restated forecast of

Scottish NSND income tax, published alongside the Welsh Government's 2020-21 Draft Budget.

**Table 4.5: SFC and OBR Scottish NSND income tax forecast comparison**

| | 2017-18 | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|---|
| Headline forecasts (£ million) | | | | | | | |
| SFC February 2020 | 10,916 | 11,378 | 11,677 | 12,365 | 12,897 | 13,447 | 14,059 |
| OBR December 2019 | 10,916 | 11,571 | 12,017 | 12,629 | 13,096 | 13,576 | 14,105 |
| Difference | 0 | -193 | -340 | -264 | -199 | -130 | -46 |
| Year-on-year growth rate (per cent) | | | | | | | |
| SFC February 2020 | | 4.2 | 2.6 | 5.9 | 4.3 | 4.3 | 4.6 |
| OBR December 2019 | | 6.0 | 3.9 | 5.1 | 3.7 | 3.7 | 3.9 |
| Difference | | -1.8 | -1.2 | 0.8 | 0.6 | 0.6 | 0.7 |

Source: Scottish Fiscal Commission, HMRC (2019) Scottish Income Tax Outturn Statistics (link), OBR (2019) Welsh Taxes Outlook - December 2019 (link).
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

# Non-Domestic Rates

## Forecast

**Table 4.6: Forecast revenue for Non-Domestic Rates**

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| | 2,847 | 2,806 | 2,749 | 3,012 | 3,345 | 3,423 | 3,590 |

Source: Scottish Fiscal Commission, Scottish Government NDR returns.
Shaded cells refer to outturn available at time of publication.

4.23. Revenues from Non-Domestic Rates are forecast to increase by £841 million from 2020-21 to 2024-25. The forecast reflects new data and revised judgements, as well as a number of policies introduced in the Non-Domestic Rates (Scotland) Bill,[49] and an additional policy introduced in the Scottish Budget 2020-21.

## Background

4.24. NDR (also known as business rates) are paid by the owners, tenants or occupiers of non-domestic properties. The amount of tax paid is dependent on the rateable value (RV) of the property, the tax rate and any reliefs or exemptions for which the property is eligible.[50] While NDR is collected and ultimately spent by local authorities, the Scottish Government is responsible for the tax. This includes decisions such as the tax rate, the system of reliefs available and the date at which a revaluation of properties will take effect.[51]

## Change since December 2018

**Table 4.7: Change in Non-Domestic Rates revenue since December 2018**

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|
| December 2018 | 2,827 | 2,785 | 2,887 | 3,087 | 3,295 | 3,332 |
| Data updates | 18 | -50 | -132 | -85 | -88 | -91 |
| Methodology changes | 2 | 71 | -15 | -9 | -5 | 36 |
| NDR Bill costings | | | 17 | 27 | 151 | 153 |
| February 2020 Pre-measures | 2,847 | 2,806 | 2,757 | 3,020 | 3,353 | 3,431 |
| Budget policy costing | | | -7 | -7 | -8 | -8 |
| February 2020 Post-measures | 2,847 | 2,806 | 2,749 | 3,012 | 3,345 | 3,423 |
| Change since December 2018 | 20 | 21 | -137 | -74 | 50 | 90 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link), Scottish Government NDR returns.
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

[49] Non-Domestic Rates (Scotland) Bill (link)

[50] Rateable value is defined in the Valuation and Rating (Scotland) Act 1956 (link)

[51] Local authorities do have the power to introduce their own locally funded reliefs under the Community Empowerment (Scotland) Act 2015 (link)

4.25. There are three main changes to our pre-measures forecast since December 2018. The first is our forecast for appeals losses. Previously, we forecast RV lost to appeal over the cycle based on the historical pattern of RV of appeals resolved relative to the RV of appeals lodged. We now base our forecast on the historical pattern of RV actually lost to appeal, relative to the RV that has ultimately been lost to appeal over a whole revaluation cycle. This aligns our methodology more with what we are forecasting, namely RV lost to appeal. Our new approach lowers the NDR income forecast by £15 million in 2020-21.

4.26. Our forecasts have also changed as a result of various data updates since December 2018. These include the audited local authority returns for 2018-19, the 2019-20 mid-year estimates from local authorities and updated data on appeals losses. The combined effect of all data updates has been to reduce the forecast from 2019-20 onwards. In 2020-21 the reduction is £132 million, the majority of which comes from incorporating the 2018-19 audited returns (£41 million reduction) and the appeals loss data (£62 million reduction).

4.27. The final important change to the pre-measures forecast relates to the various policy changes included in the Non-Domestic Rates (Scotland) Bill as at Stage 2.[52] These include:

- bringing large-scale private student accommodation onto the valuation roll
- properties not in active occupation no longer being eligible to claim certain reliefs
- ending the eligibility for mainstream independent schools to claim charity relief
- changing the empty property relief reset period
- bringing commercial activity in currently exempt parks onto the valuation roll
- repealing Section 153 of the Local Government Finance Act under which the Higher Property Rate (formerly Large Business Supplement) and a number of reliefs are set

4.28. The effect of these policies is to increase NDR income by £17 million in 2020-21.

[52] For full details of our Non-Domestic Rates (Scotland) Bill costings see Scottish Fiscal Commission (2019) Non Domestic Rates (Scotland) Bill – Supplementary Costings December 2019 (link). Changing the empty property relief reset period will be enacted via secondary legislation rather than via the Bill, but we included this policy change in our supplementary costing publication.

## Scottish Government policy

4.29. The Scottish Government will introduce an Intermediate Property Rate (IPR) as of 1 April 2020. While properties with an RV above £95,000 will continue to be charged the Higher Property Rate (HPR) of 2.6p on top of the Basic Property Rate (also known as poundage), properties with an RV between £51,000 and £95,000 will instead be charged 1.3p on top of the standard poundage.[53] The effect of this policy is to reduce NDR income by £7 million in 2020-21. It is assumed that from 2024-25 there will be no effect from this policy as a result of section 8C of the Bill which repeals the legislation under which the IPR will be set. Further details of the IPR costing can be found in Annex A.

**Box 4.2: Calculation of the Distributable Amount in 2020-21**

The Commission forecasts what is known as the ‘contributable amount’ for NDR, which can be thought of as being the amount collected by local authorities that subsequently notionally flows to the Scottish Government. The contributable amount collected by local authorities is pooled at a national level, before being redistributed by the Scottish Government as part of the local government finance settlement. The amount of NDR income redistributed to local authorities as part of this settlement is known as the ‘distributable amount’.

In our previous reports we have outlined how our forecast is used by the Scottish Government to inform what amount can be distributed to local authorities for the year ahead.[54] Government can distribute more or less than the forecast contributable amount in any given year, as long as the total amount collected is subsequently distributed back to local government. Notwithstanding this flexibility, the calculation of the distributable amount by Government also takes account of three factors:

1. the estimated closing balance on the account from the previous financial year
2. estimated prior year adjustments to be carried over to the account from the year before
3. the amount forecast to be raised in the year ahead

[53] The Higher Property Rate replaces the Large Business Supplement, whereby properties with a rateable value above £51,000 were charged 2.6p on top of the Basic Property Rate (also known as the poundage).

[54] Scottish Fiscal Commission (2018) Forecast Evaluation Report (link)

At the last Budget, the Scottish Government chose to set the distributable amount at a level so the account was projected to be balanced at the end of 2021-22.[55] This year, the distributable amount set by Government leads to a projected negative balance of £100 million on the account at the end of 2020-21, as shown in Table 4.8. The Scottish Government plans to bring the account back into balance by 2022-23.

**Table 4.8: Illustrative projected balance of the Non-Domestic Rating Account**

| £ million | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
|---|---|---|---|---|
| Provisional contributable amount **(A)** [56] | 2,844 | 2,883 | 2,890 | 2,749 |
| Net effect of prior year adjustments **(B)** [57] | -23 | -82 | -36 | -84 |
| Distributable amount **(C)** | 2,666 | 2,636 | 2,853 | 2,790 |
| Annual balance **(D)** **(A + B - C)** | 155 | 165 | 1 | -125 |
| Cumulative balance **(E)** **(E from year before + D)** | -141 | 24 | 25 | -100 |

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding. Shaded cells refer to outturn at the time of publication. The projected balance is illustrative because at time of publication, we do not have the audited NDR income figures for 2019-20 or the Provisional Contributable Amount for 2020-21. The presentation differs slightly to that in the published audit of the NDR rating account, mainly because of the presentation of line B – 'net effect of prior year adjustments'.

As outlined in our previous reports, the audited balance of the pool will be determined by several factors in practice. These include not only our forecast accuracy, but also the difference between the start of year estimates provided by local authorities to the Government after the start of the financial year in April (the provisional contributable amount in Table 4.8) and the final audited NDR income returns for the financial year. The difference is termed the prior year adjustment. Contributions to the pool are determined by local authorities own estimates of collections for the year, submitted to the Scottish Government after the start of the financial year. This means that the balance of the pool could be positive despite our projection of a negative balance if local authorities report a high level of collections on their start-of-year estimates.

[55] The calculation of the 2019-20 distributable amount, showing how our forecasts were used is shown in Scottish Government (2018) Scottish Budget: Budget 2019-20, Table 6.13 (link). Page 84 of the same publication contains the Scottish Government's statement of its intention to bring the cumulative balance back to zero at the end of 2021-22.

[56] Provisional contributable amount is reported by local authorities to the Scottish Government after the start of the financial year and determines level of contributions to the pool.

[57] Differences between the provisional contributable amount and final audited figures from the previous year are reflected in this line.

Should the projected negative balance in 2020-21 materialise this will have to be addressed by the Government at future Budgets. This does not necessarily affect the local government settlement directly, but would need to be managed as part of the overall Scottish Government Budget.

## Forecast uncertainty

4.30. Our forecast for NDR is subject to several uncertainties. The most significant of these concerns Stage 3 of the Non-Domestic Rates (Scotland) Bill, which took place on 4 February 2020 and is not included in our forecast. Any policy changes included at this stage are therefore not included in our forecast. We will revisit our costings, if necessary, as part of our publication to accompany the Medium Term Financial Strategy.

4.31. Our assumption about the amount of RV expected to be lost to appeal is also a source of uncertainty. The effect this has on NDR income is determined by both the size and timing of appeals losses. As revaluation appeals are backdated to the date of revaluation, the later an appeal is resolved in the cycle the greater the effect it has on NDR income.

# Land & Buildings Transaction Tax (LBTT)

## Forecast

**Table 4.9: Forecast revenue for LBTT**

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| Total LBTT revenue | 554 | 613 | 641 | 666 | 692 | 720 | 749 |
| *of which* | | | | | | | |
| *Residential (excluding ADS)* | 262 | 288 | 303 | 319 | 336 | 354 | 371 |
| *Additional Dwelling Supplement* | 99 | 134 | 129 | 131 | 134 | 137 | 140 |
| *Non-residential* | 193 | 191 | 209 | 216 | 222 | 230 | 238 |

Source: Scottish Fiscal Commission, Revenue Scotland (2019) Annual Report and Accounts for the year ended 31 March 2019 (link).
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

4.32. LBTT is payable on purchases or leases of residential or non-residential properties. We forecast LBTT revenues of £641 million in 2020-21. Two thirds will be raised from residential transactions, including those liable for the Additional Dwelling Supplement (ADS), with the remaining one third coming from non-residential LBTT.

## Residential LBTT

### Forecast

**Table 4.10: Forecast revenue for Residential LBTT (excluding ADS)**

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| | 262 | 288 | 303 | 319 | 336 | 354 | 371 |

Source: Scottish Fiscal Commission, Revenue Scotland (2019) Annual Report and Accounts for the year ended 31 March 2019 (link).
Shaded cells refer to outturn available at time of publication.

## Change since December 2018

**Table 4.11: Change in residential LBTT revenue (excluding ADS) since December 2018**

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|
| December 2018 | 267 | 296 | 324 | 349 | 373 | 398 |
| Prices | -7 | -26 | -25 | -26 | -29 | -32 |
| Transactions | 4 | 11 | 12 | 13 | 14 | 15 |
| Modelling | | -11 | -27 | -37 | -44 | -51 |
| Data updates | | 18 | 19 | 20 | 21 | 22 |
| Other | -1 | 0 | 0 | 0 | 1 | 1 |
| February 2020 | 262 | 288 | 303 | 319 | 336 | 354 |
| Change since December 2018 | -5 | -8 | -21 | -30 | -37 | -45 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link), Revenue Scotland (2019) Annual Report and Accounts for the year ended 31 March 2019 (link).

Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

4.33. We have changed our residential LBTT forecast model since December 2018. Previously we used a model that estimated the distribution of house purchases using forecasts for the mean price, the median price and transactions.[58] Our new approach projects forward the distribution of transactions in 2018-19 using forecasts for two determinants rather than three: mean house prices and transactions growth. The change reduces the share of transactions falling into the top two tax bands in future years and lowers forecast revenue by £27 million in 2020-21.[59]

4.34. House price growth up to the end of the second quarter of 2019-20 was lower than we expected in December 2018. We have revised our house price forecast down leading to a £25 million reduction in our LBTT forecast for 2020-21. More recent monthly data and forward looking indicators suggest continued house price growth, with signs of a modest acceleration in the near term.

4.35. There has been renewed growth in transactions during 2019-20. In the financial year to November, transactions grew by 0.8 per cent, having fallen over the same period in 2018-19.[60] We have revised our forecast upwards accordingly, increasing the LBTT forecast by £12 million in 2020-21.

[58] Scottish Fiscal Commission (2017) Current Approach to Forecasting (link)

[59] A discussion of the forecast share of purchases in the top two tax bands on our December 2017 forecast and forecast error can be found in Scottish Fiscal Commission (2019) Forecast Evaluation Report (link).

[60] Registers of Scotland (2019) Quarterly House Price Statistics (link)

4.36. Our final change comes from the inclusion of LBTT revenue data up to December 2019.[61] This increases the forecast by £18 million in 2019-20 and by £19 million in 2020-21.

## Forecast uncertainty

4.37. Our revenue forecast is driven by two determinants: average house prices and total transactions. Forecast errors in either of these will produce errors in our revenue forecast. Around 75 per cent of residential LBTT revenue comes from the top two tax brackets, which accounts for less than 10 per cent of transactions. This can lead to significant forecast uncertainty from year to year because small unanticipated changes in the number of these transactions can have a significant effect on LBTT revenue.

4.38. The Scottish Government has introduced the First Home Fund to help First Time Buyers (FTBs) purchase a property. It is a shared equity scheme and runs from 18 December 2019 to March 2021. It offers FTBs an interest-free equity loan up to £25,000 toward the purchase of their first home. The loan is repayable in full when the property is sold or can be repaid in part or in full at any time. Our judgement is that the effect on LBTT revenue will be minimal, as additional FTB transactions displace home mover and additional dwelling transactions.

4.39. A final source of uncertainty comes from any potential UK Government policy changes, for example the introduction of a Stamp Duty Land Tax surcharge for non-UK resident buyers.[62] We will continue to monitor developments and update our forecasts should further relevant information become available.

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[61] Revenue Scotland (2020) Land and Buildings Transaction Tax Statistics (link)

[62] Conservative Party (2019), Conservative Manifesto 2019 (link)

# Additional Dwelling Supplement

## Forecast

### Table 4.12: Forecast revenue for ADS

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| | 99 | 134 | 129 | 131 | 134 | 137 | 140 |

Source: Scottish Fiscal Commission, Revenue Scotland (2019) Annual Report and Accounts for the year ended 31 March 2019 (link).
Shaded cells refer to outturn available at time of publication.

## Change since December 2018

### Table 4.13: Change in ADS revenue since December 2018

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|
| December 2018 | 94 | 122 | 123 | 127 | 130 | 134 |
| Prices | 0 | -1 | -1 | -2 | -2 | -2 |
| Transactions | 2 | 5 | 5 | 5 | 5 | 5 |
| Modelling | | 7 | 1 | -1 | -1 | -1 |
| Other | 4 | 1 | 2 | 2 | 1 | 1 |
| February 2020 | 99 | 134 | 129 | 131 | 134 | 137 |
| Change since December 2018 | 5 | 12 | 6 | 4 | 3 | 3 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts December 2018 (link), Revenue Scotland (2019) Annual Report and Accounts for the year ended 31 March 2019 (link).
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

4.40. The main change to our ADS forecast comes from our updated forecasts for house prices and transactions. The former decreases our forecast by £1 million in 2020-21, while the latter increases our forecast by £5 million in 2020-21.

4.41. We have also changed our ADS forecast model since December 2018. Gross ADS is now estimated using distributional data for 2018-19 as a base while repayments are calculated by financial year rather than by quarter. This increases the forecast by £1 million in 2020-21 and decreases it by £1 million in later years. The modelling change combined with our updated forecast for transactions also increases our estimate of the additional ADS raised from the introduction of the 4 per cent rate (see Annex B).

4.42. We note that forecast ADS falls in 2020-21 compared to 2019-20. This is because net ADS in 2019-20 is temporarily boosted by the fact that some of the ADS reclaimed over the year will be for tax paid under the 3 per cent system in place before 25 January 2019, whereas ADS revenue for new transactions (subject to ADS) taking place in 2019-20 will be due at the 4 per cent rate.

# Non-Residential LBTT

## Forecast

**Table 4.14: Forecast revenue for Non-Residential LBTT**

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| | 193 | 191 | 209 | 216 | 222 | 230 | 238 |

Source: Scottish Fiscal Commission, Revenue Scotland (2019) Annual Report and Accounts for the year ended 31 March 2019 (link).
Shaded cells refer to outturn available at time of publication.

## Change since December 2018

**Table 4.15: Change in non-residential LBTT revenue since December 2018**

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|
| December 2018 | 208 | 226 | 233 | 240 | 247 | 255 |
| Prices | | 2 | 0 | 0 | 0 | 1 |
| Transactions | | -1 | -1 | -1 | -1 | -1 |
| Data | -15 | -37 | -31 | -31 | -32 | -33 |
| Other | 0 | 1 | -3 | -3 | -3 | -3 |
| February 2020 pre-measures | 193 | 190 | 199 | 205 | 211 | 219 |
| Policy costing | | 2 | 10 | 11 | 11 | 11 |
| February 2020 post-measures | 193 | 191 | 209 | 216 | 222 | 230 |
| Change since December 2018 | -15 | -34 | -24 | -24 | -25 | -25 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts December 2018 (link), Revenue Scotland (2019) Annual Report and Accounts for the year ended 31 March 2019 (link).
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

4.43. The main change to our non-residential forecast comes from data updates, including outturn data from Revenue Scotland for 2018-19.[63] This lowers our forecast by £37 million in 2019-20 and £31 million in 2020-21.

4.44. We have also made a modelling change to our non-residential leases forecasting model. The new approach is based on the distribution of lease transactions by rental net present value (NPV), and the determinants used are the same as those in the main non-residential model for conveyances. This change, combined with our recosting of the December 2018 change to non-residential LBTT rates and bands for conveyances, leads to the £3 million downward adjustment from 2020-21 onwards shown in Table 4.15.

[63] Revenue Scotland (2019) Annual Report and Accounts for the year ended 31 March 2019 (link)

## Scottish Government policy

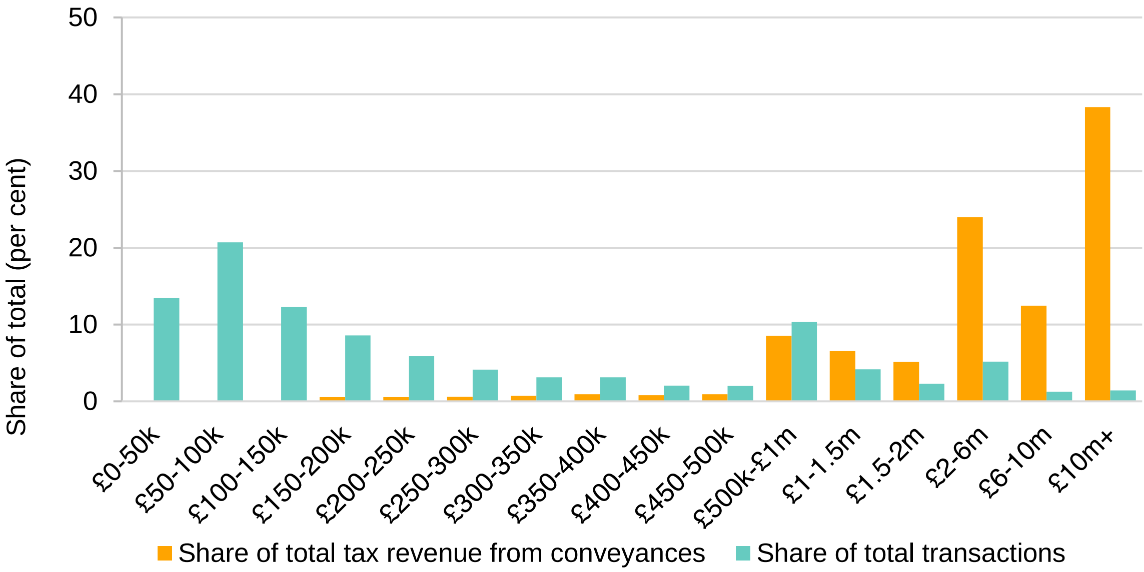
4.45. The Scottish Government has announced the introduction of a new tax band for non-residential leases. Leases where the net present value of the rent is above £2 million will be charged at a 2 per cent rate, instead of 1 per cent, for the portion of the value of the lease that is above the threshold. The policy takes effect as of midnight on 7 February 2020. The policy change is expected to increase non-residential LBTT by £10 million in 2020-21. Annex A contains full details of how we have produced the costing.

## Forecast uncertainty

4.46. Non-residential LBTT is dependent on a small number of high value transactions. In 2018-19, transactions valued over £10 million accounted for 38 per cent of non-residential LBTT revenue from conveyances but 1 per cent of the total purchases. This introduces significant volatility as small changes in the number of high value transactions can disproportionately affect revenues.

4.47. Changes in average non-residential property prices and total non-residential transactions are volatile from year-to-year. Depending on the scale of the change, these may deviate considerably from our forecasts, which are tied to our forecasts for growth in the Scottish economy.

**Figure 4.3: Non-residential conveyances and LBTT distribution 2018-19**




Source: Revenue Scotland (link)

4.48. The UK's changing relationship with the EU is another source of uncertainty to the forecast. Approximately one quarter of non-residential LBTT revenue is from buyers who gave a non-UK address on their LBTT return.[64] We will continue to monitor developments in future forecasts.

[64] Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts December 2018 (link)

# Scottish Landfill Tax

## Forecast

### Table 4.16: Forecast revenue for Scottish Landfill Tax

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| | 149 | 124 | 116 | 110 | 94 | 79 | 66 |

Source: Scottish Fiscal Commission, Revenue Scotland (2019) Annual Report and Accounts for the year ended 31 March 2019 (link).
Shaded cells refer to outturn available at the time of publication. SLfT revenue is net of repayments, excludes penalties & interest and also excludes revenue losses.

4.49. Scottish Landfill Tax (SLfT) revenues are forecast to fall to £116 million in 2020-21. Revenues fall over our forecast horizon as incineration capacity and recycling rates in Scotland increase.

## Scottish Government policy

4.50. The Scottish Government announced that full enforcement of the ban on biodegradable municipal waste (BMW) will be delayed until 2025.[65] The BMW ban was previously planned to be introduced in January 2021. The delay to the introduction of the ban significantly increases SLfT revenues because BMW continues to be landfilled.

## Change since December 2018

### Table 4.17: Change in Scottish Landfill Tax revenue since December 2018

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|
| December 2018 | 136 | 104 | 83 | 13 | 13 | 14 |
| BMW ban | | | 25 | 103 | 84 | 78 |
| Incineration capacity | | 11 | -2 | -9 | -4 | -12 |
| Methodology changes | | 5 | 6 | 3 | 0 | -3 |
| Outturn data | 5 | 5 | 4 | 1 | 2 | 3 |
| Other | 7 | -1 | -1 | -1 | -1 | -1 |
| February 2020 | 149 | 124 | 116 | 110 | 94 | 79 |
| Change since December 2018 | 13 | 20 | 33 | 97 | 81 | 66 |

Source: Scottish Fiscal Commission, Revenue Scotland (2019) Annual Report and Accounts for the year ended 31 March 2019 (link).
Figures may not sum because of rounding. Shaded cells refer to outturn available at the time of publication.
SLfT revenue is net of repayments, excludes penalties & interest and also excludes revenue losses.

[65] Scottish Parliament (2019) Parliamentary Question S5W-25409: Economy (link)

4.51. The change to the start date of the BMW ban is the main reason for the change in our forecast since December 2018. This change contributed £25 million to the £33 million total increase in our forecast for 2020-21.

4.52. Aside from the effect of the BMW ban, the timing of new incineration capacity becoming operational has the largest effect on our forecast as more waste in general is diverted away from landfill sites. Our 2019-20 forecast includes some delays to facilities becoming fully operational, meaning more waste continues to be landfilled and a higher SLfT revenue forecast. We have also updated our incineration capacity assumptions from 2020-21, including the addition of a new facility, which has decreased our forecast by £2 million in 2020-21.

4.53. We have incorporated an adjustment to our forecast to account for SLfT revenue arising from any Revenue Scotland compliance activities relating to previous financial years. This is the main reason for the difference between the 2018-19 outturn figure and our December 2018 forecast.[66]

## Forecast uncertainty

4.54. Our forecast is highly sensitive to the timing and nature of the BMW ban. Changes to the introduction of the ban have led to large revisions in our SLfT forecast. We will continue to monitor progress and will factor any interventions by the Scottish Government into our future forecasts as appropriate.

4.55. Changes to the timing and scale of new incineration capacity becoming operational are the second major source of forecast uncertainty. We will continue to monitor new information on development of waste infrastructure in Scotland.

[66] For further detail see Appendix B (ii) of Revenue Scotland (2020), Annual Summary of Trends in the Devolved Taxes 2018/19 (link)

# Illustrative Forecast – VAT Assignment

**Table 4.18: Forecast of Scottish VAT Assignment**

| £ million | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|---|---|
| | 5,012 | 5,243 | 5,379 | 5,554 | 5,727 | 5,886 | 6,045 | 6,206 | 6,404 |

Source: Scottish Fiscal Commission, HM Treasury, HMRC and Scottish Government.
Shaded cells refer to outturn available at time of publication. Outturn in this context refers to a provisional estimate of the Scottish share of VAT, applied to outturn UK VAT receipts.

4.56. The Scotland Act 2016 states that half of VAT raised in Scotland will be assigned to the Scottish Government.[67] On 31 October 2019 the then Chief Secretary to the Treasury wrote to the Convenor to the Finance and Constitution Committee stating that the full implementation of VAT assignment will be delayed by a year to April 2021.[68] On 2 November 2019, the Cabinet Secretary for Finance, Economy and Fair Work also wrote a letter to the Convenor confirming the delay to implementation.[69]

4.57. We will continue to produce illustrative forecasts of VAT assignment to help users understand the potential change. We await further information from the VAT Assignment Working Group on how our future VAT Assignment forecasts may be utilised. We published a paper on our approach to creating forecasts of assigned VAT in September 2018.[70] Our broad approach remains consistent with this paper.

**Table 4.19: Change in VAT Assignment since December 2018**

| £ million | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|---|---|
| December 2018 | 5,033 | 5,383 | 5,631 | 5,801 | 5,966 | 6,122 | 6,279 | 6,434 |
| Data updates | -21 | -51 | -147 | -135 | -129 | -126 | -125 | -125 |
| Economic determinants | 0 | -90 | -106 | -112 | -110 | -110 | -108 | -103 |
| February 2020 | 5,012 | 5,243 | 5,379 | 5,554 | 5,727 | 5,886 | 6,045 | 6,206 |
| Change since December 2018 | -21 | -141 | -252 | -247 | -239 | -236 | -233 | -228 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link).
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication. Outturn in this context refers to a provisional estimate of the Scottish share of VAT, applied to outturn UK VAT receipts.

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[67] Scotland Act 2016 Part 2 Section 16 (link). The Scotland Act 2016 legislated to assign 10 pence of the standard rate and 2.5 pence of the reduced rate to the Scottish Budget. This is represents half of the current VAT rates.

[68] Letter from the Chief Secretary to the Treasury to the Convener of the Finance and Constitution Committee 31 October 2019 (link).

[69] Letter from the Cabinet Secretary for Finance, Economy and Fair Work to the Convener of the Finance and Constitution Committee 2 November 2019 (link).

[70] Scottish Fiscal Commission (2018) Approach to forecasting VAT assignment (link)

# Illustrative Forecast – Air Passenger Duty

## Background

**Table 4.20: Forecast revenue for the Scottish share of Air Passenger Duty**

| £ million | 2018-19[1] | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| | 286 | 286 | 297 | 310 | 323 | 339 | 355 |

Source: Scottish Fiscal Commission.
[1] Figure not classed as outturn data. It is an estimate of the Scottish share of APD revenues.

4.58. Air Passenger Duty (APD) is a tax paid on eligible passengers on flights departing from UK airports. The tax paid depends on the passenger's class of travel, for example business or economy, and their final destination.

4.59. Air Departure Tax (ADT) was due to replace UK APD in Scotland from April 2018. The introduction of ADT has been deferred until the state-aid issue raised in relation to the Highlands and Islands exemption has been resolved.[71]

4.60. We produce an illustrative forecast of the Scottish share of UK APD based on a combination of administrative and survey data. The accuracy of the estimates will only be known once ADT is introduced and separately collected for Scotland. There remains significant uncertainty around both the outturn revenue data and the forecast. Detail on our approach to forecasting the Scottish share of APD can be found in our December 2018 publication.[72]

## Forecast

4.61. OBR UK GDP and inflation forecasts from March 2019 and updated Civil Aviation Authority (CAA) survey figures have been included. These reduce the forecast by £25 million in 2020-21.

**Table 4.21: Change in Scottish share of Air Passenger Duty revenue since December 2018**

| £ million | 2018-19[1] | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|
| December 2018 | 302 | 312 | 322 | 336 | 349 | 364 |
| Data updates | -16 | -26 | -25 | -26 | -26 | -25 |
| February 2020 | 286 | 286 | 297 | 310 | 323 | 339 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link).
[1] Figure is not classed as outturn data. It is an estimate of the Scottish share of APD revenues.

[71] Scottish Parliament (2019) Parliamentary Question S5W-22720 (link), Letter from the Minister for Public Finance and Digital Economy to the Convener of the Finance and Constitution Committee 23 April 2019 (link)

[72] Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link)

# Chapter 5
# Social Security

## Introduction

5.1 From 1 April 2020 the Scottish Parliament will have executive competence for nearly all of the benefits that are to be devolved to the Scottish Parliament. This transfer of executive competence gives Scottish Ministers the power to make regulations and payments, and underpins delivery responsibilities. This means that the Scottish Government will have financial responsibility for these benefits and money will need to be allocated to cover the expected payments in the Scottish Budget 2020-21, and in future budgets.

5.2 Some of these payments will continue to be delivered by the Department for Work and Pensions (DWP) on the Scottish Government's behalf for the next few years. While these agreements are in place, Scottish recipients will see very little change because of devolution as their payments will continue to be paid by DWP under UK Government policy.

5.3 Over the next five years, the Scottish Government will launch their own versions of these payments to be delivered by Social Security Scotland.[73] Existing recipients will be transferred from DWP to Social Security Scotland and Social Security Scotland will also be accepting new applications directly. When these new payments 'launch' is important to our forecasts as this determines whether we produce our forecasts based on Scottish Government policy, rather than UK Government policy.

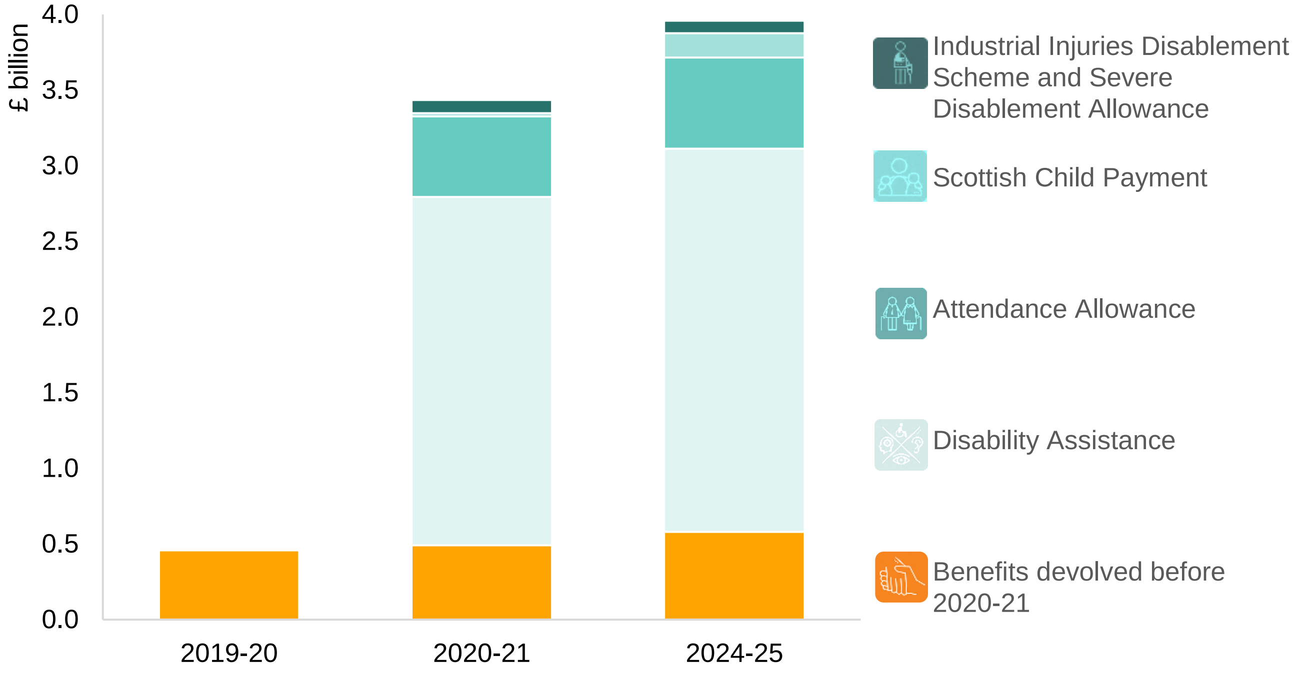
5.4 In this chapter, we provide our forecasts of devolved social security spending to inform the Scottish Budget 2020-21. Social security portfolio spending increases from £437 million in 2019-20 to £3.4 billion in 2020-21.[74] We

[73] The Scottish Government does not plan to introduce a replacement for the UK Government's Severe Disablement Allowance benefit, this will continue to be delivered by DWP (link)

[74] A summary table of our social security forecasts can be found in Chapter 2 Fiscal Overview

estimate that it will continue to increase over the forecast period, reaching £3.8 billion in 2024-25.

**Figure 5.1 Total social security spending forecast**




Source: Scottish Fiscal Commission
Disability Assistance includes spending for Child Disability Assistance, Disability Living Allowance Adult and Personal Independence Payment. Total social security spending includes all social security portfolio spending as well as spending on Best Start Foods, Employability Services and Scottish Child Payment.

5.5 Cold Weather Payments and Winter Fuel Payments will be devolved at a later date so we provide indicative forecasts of spending on these benefits.[75] There will be no spending allocations for these benefits in the Scottish Budget 2020-21.

## Payments launched before 2020-21

5.6 A number of social security payments have already been launched by the Scottish Government. At the time of publication:

- Social Security Scotland is making payments for Best Start Grant, Best Start Foods, Carer's Allowance Supplement and Funeral Support Payment

- Scottish Welfare Fund and Discretionary Housing Payments are managed by local authorities

[75] Correspondence (2019) Cabinet Secretary for Social Security and Older People to Social Security Committee (link)

- Fair Start Scotland, also referred to as Employability Services, is delivered by the external providers that have been contracted by the Scottish Government

5.7 We provided forecasts of spending for these payments for the Scottish Budget 2019-20. Figure 5.2 compares our February 2020 forecasts of the spending in 2019-20 and 2020-21, total spending has increased by £19 million. £6 million of this change is because of Scottish Government policy changes. Funding for the Scottish Welfare Fund and Discretionary Housing Payments has increased, along with an increase in the payment rate for Funeral Support Payment. Since these payments have already been launched by the Scottish Government, our forecasts are based on existing Scottish Government policy.

**Figure 5.2 Social security payments launched before 2020-21**

| | Forecast based on Scottish Government policy | | |
|---|---|---|---|
| £ million | 2019-20 | 2020-21 | Change |
| Best Start Foods | 6 | 9 | 3 |
| Best Start Grant | 20 | 18 | -2 |
| Carer's Allowance Supplement | 37 | 39 | 2 |
| Funeral Support Payment | 4 | 9 | 5 |
| Discretionary Housing Payments | 67 | 73 | 5 |
| Scottish Welfare Fund | 33 | 36 | 3 |
| Employability Services | 15 | 18 | 3 |

Source: Scottish Fiscal Commission
The Scottish Government has also launched Young Carer Grant and Job Start Payment is expected to launch in 2020-21. We do not provide a forecast for Young Carer Grant as the expected spend is less than £1 million each year which is below our materiality threshold. Job Start Payment is not included in our legislative scope.
Best Start Foods includes some spending on the UK Government Healthy Start Scheme while people are transferred to the new benefit.

## Payments launching in 2020-21

5.8 Our forecasts include two new forms of assistance opening to applications in 2020-21 and included in the Scottish Budget 2020-21. Our forecasts for Scottish Child Payment and Child Disability Assistance, which includes the

Scottish Government's new Disability Assistance for Children and Young People, are shown in Figure 5.3.

**Figure 5.3 Social security payments launching in 2020-21**

| £ million | Forecast based on Scottish Government policy | |
|---|---|---|
| | 2020-21 | 2024-25 |
| Scottish Child Payment | 21 | 162 |
| Child Disability Assistance | 217 | 312 |

Source: Scottish Fiscal Commission

5.9 We provide forecasts for Scottish Child Payment and Disability Assistance for Children and Young People based on existing Scottish Government policy. Disability Assistance for Children and Young People replaces the UK Government benefit, Disability Living Allowance for Children. The Scottish Government has proposed changes to this form of disability assistance when it launches in Scotland and in Annex A we estimate the cost of these policy changes. There is no equivalent UK benefit for Scottish Child Payment.

5.10 The Scottish Government has set out the ambition for Disability Assistance for Working Age People and it is expected to launch in early 2021.[76] The Scottish Government is still developing the details of Disability Assistance for Working Age People and there is further work to be done including draft secondary legislation and associated guidance. Although the high level policies have been set out, the details will be developed over the next year. In this particular case, we have made a judgement to produce a forecast for Disability Assistance for Working Age People once policy and administrative details are clearer. Instead we forecast spending for working age disability assistance based on current UK Government policy as embodied in the two benefits; Personal Independence Payment and Disability Living Allowance.

5.11 The Scottish Government plans to start delivery of additional financial support to carers of more than one disabled child in spring 2021.[77] For the same reasons as noted above for Disability Assistance for Working Age People, we do not provide a costing for this additional payment and will look to provide a forecast when more details become available.

[76] Scottish Government (2019) Delivery of disability and carer benefits: policy position paper (link).

[77] Scottish Government (2019) Support for carers: policy position paper (link)

### Payments launching after 2020-21

5.12 The Scottish Government plans to launch a number of new payments after 2020-21.[78] These payments will replace existing UK Government benefits such as Attendance Allowance and Carer's Allowance. We have not forecast these using Scottish Government policy as we do not have sufficient detail of the policy and operational changes that the Scottish Government wants to introduce. For the purposes of the Scottish Budget 2020-21, we provide forecast spending under existing UK Government policy. As the Scottish Government announces their policy intent, we will incorporate these changes into future published forecasts.

**Figure 5.4 Social security forecasts based on UK Government policy**

| | Forecast based on UK Government policy | |
|---|---|---|
| £ million | 2020-21 | 2024-25 |
| Personal Independence Payment | 1,583 | 1,841 |
| Disability Living Allowance Adult | 502 | 380 |
| Attendance Allowance | 532 | 601 |
| Carer's Allowance | 292 | 375 |
| Industrial Injuries Disablement Scheme | 80 | 77 |
| Severe Disablement Allowance | 7 | 5 |

Source: Scottish Fiscal Commission
Cold Weather Payments and Winter Fuel Payments will not be devolved in April 2020 and are excluded from the table above.

[78] Scottish Government (2020) Social security: policy position papers (link). Severe Disablement Allowance will continue to be administered by DWP.

# Payments launched before 2020-21

5.13 We now report on the forecasts of the various benefits, grouped into the three categories discussed in the introduction. In this first section we present the spending forecasts for the social security payments that have already been launched by the Scottish Government.

## Carer's Allowance and Carer's Allowance Supplement

### Forecast

**Table 5.1: Forecast spending for Carer's Allowance and Carer's Allowance Supplement**

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| Total spend | 187 | 313 | 330 | 352 | 381 | 403 | 425 |
| Forecast on UK Government policy | | | | | | | |
| Carer's Allowance | 152 | 276 | 292 | 311 | 336 | 355 | 375 |
| Forecast on Scottish Government policy | | | | | | | |
| Carer's Allowance Supplement | 35 | 37 | 39 | 41 | 45 | 47 | 50 |

Source: Scottish Fiscal Commission, Social Security Scotland (2019) Annual Report and Accounts (link). Figures may not sum because of rounding. Shaded cells refer to outturn at time of publication.

5.14 Carer's Allowance (CA) was devolved to the Scottish Parliament on 3 September 2018. The spending figure for 2018-19 shows the spending for the devolved portion of the year, September 2018 to March 2019. Combined spending on CA and Carer's Allowance Supplement (CAS) is forecast to increase by £95 million between 2020-21 and 2024-25.

### Background

5.15 DWP will continue to administer Carer's Allowance payments on behalf of the Scottish Government until Social Security Scotland takes over delivery. The Scottish Government plans to start taking applications in early 2022. Our forecast is based on UK Government policy.

5.16 Carer's Allowance Supplement was introduced by the Scottish Government in 2018 to increase the amount paid to carers in Scotland. It does not have a UK Government equivalent benefit and we produce our forecasts based on Scottish Government policy.

## Change since December 2018

**Table 5.2: Change in CA and CAS spending since December 2018**

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|
| December 2018 | 191 | 320 | 345 | 367 | 389 | 412 |
| Population and caseload update | 0 | -1 | -2 | -1 | 0 | 0 |
| Expenditure outturn | -4 | -5 | -6 | -6 | -6 | -7 |
| UC adjustment | 0 | 0 | -6 | -6 | 0 | 0 |
| Other data and modelling | 0 | 0 | -1 | -2 | -2 | -3 |
| February 2020 | 187 | 313 | 330 | 352 | 381 | 403 |
| Change since December 2018 | -5 | -7 | -14 | -15 | -8 | -9 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link), Social Security Scotland (2019) Annual Report and Accounts (link).
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

5.17 The number of people receiving Carer's Allowance, the caseload, continues to grow. Recent outturn data indicate that the trend is slower than assumed in December 2018 and we have revised down our caseload forecast accordingly. Our caseload forecast can be found in Supplementary Table S5.1. We also updated our forecast with 2018-based population estimates and projections, which slightly offsets some of this decrease in the caseload forecast.

5.18 2018-19 outturn expenditure for both Carer's Allowance and Carer's Allowance Supplement was lower than we forecast in December 2018, leading to a decline in our forecast.

5.19 We have reduced the extent to which we expect the rollout of Universal Credit to increase the Carer's Allowance caseload in the next two years.

5.20 Other data and modelling updates, including a lower outturn inflation for September 2019, slightly reduce the forecast.

## Forecast uncertainty

5.21 In addition to the overall uncertainties noted in Box 5.1, eligibility for Carer's Allowance is linked to receipt of disability benefits and will also be affected by the rollout of Universal Credit. It is also possible that the availability of the Carer's Allowance Supplement will encourage more people to claim. We will continue to monitor eligibility, and will consider incorporating a more direct link to disability benefit caseloads into our forecast models.

**Box 5.1: Forecast uncertainties for social security**

**Take-up rates:** The proportion of the eligible population which applies for and receives social security support is known as the take-up rate. Take-up rates are challenging to measure as there is limited information available about the proportion of the population who could receive support but are not doing so. As noted in our Forecast Evaluation Report, it is difficult to predict take up for new social security assistance as there is uncertainty about how benefits will be launched and how people will react.[79] This means our forecasts for new social security assistance such as Scottish Child Payment are particularly uncertain.

**Accounting treatment:** Outturn expenditure for each benefit will include accounting adjustments. Where devolved benefits are administered by DWP under agency agreements, accounting adjustments will be attributed to Scotland and presented in Social Security Scotland's annual accounts. This may result in differences in outturn expenditure, compared to the estimates DWP has published historically for Scottish benefit spend. As we are using DWP data to inform our forecasts, any differences in accounting treatment may result in forecast errors.

**Launch of Scottish social security payments:** Although the majority of benefits will be devolved in April 2020, new Scottish social security payments such as the replacement for PIP will not be launched until later. The pace at which Social Security Scotland opens to new applications, and accepts transfers of those currently in receipt of equivalent UK Government benefits, will have an effect on the spending we expect in each financial year. For 2020-21, we are only considering launch dates and transition periods for Scottish Child Payment and Disability Assistance for Children and Young People.

**Timing of fiscal events:** The Scottish Budget 2020-21 will take place before the UK Government fiscal event. If there are changes to any UK Government policy as part of the March 2020 UK Budget these will not be reflected in our forecasts. We use OBR forecasts of inflation to uprate the payment rates for the majority of the benefits. The OBR has not published an inflation forecast since March 2019 and as a result, the payment rates we assume in our forecasts may be subject to greater uncertainty than usual.

**Demographics:** The working age population can be expected to be stable, but spending on pensioners and benefits for young children will be sensitive to the number of births and deaths. In particular, if the recent downward trend in fertility continues, then our forecasts for social security assistance for young children may prove to be too high.

[79] Scottish Fiscal Commission (2019) Forecast Evaluation Report (link)

# Best Start Grant

## Forecast

**Table 5.3: Forecast spending for Best Start Grant**

| | | Forecast on Scottish Government policy | | | | | |
|---|---|---|---|---|---|---|---|
| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Pregnancy and Baby Payment | 4 | 7 | 7 | 7 | 7 | 7 | 7 |
| Early Learning Payment | | 8 | 5 | 5 | 5 | 5 | 5 |
| School Age Payment | | 5 | 5 | 5 | 5 | 5 | 5 |
| Total Best Start Grant | 4 | 20 | 18 | 17 | 17 | 17 | 18 |

Source: Scottish Fiscal Commission, Social Security Scotland (2019) Annual Report and Accounts (link).
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

5.22 Spending is highest in 2019-20 at the launch of Early Learning Payment as a large cohort of children aged from two to three and a half became eligible. In future years, only children turning two will be newly eligible each year. From 2021-22 onwards we forecast an annual increase of around one per cent, with rising take-up partly offset by a fall in the population of young children.

## Background

5.23 Best Start Grant is a series of one-off payments to help low income households with the costs associated with having a young child. This includes the Pregnancy and Baby Payment, launched in December 2018; the Early Learning Payment for two and three year olds, launched at the end of April 2019; and the School Age Payment for four and five year olds, launched in June 2019.

5.24 Eligibility is usually based on having a new baby or a child within a particular age range while receiving a qualifying benefit.

## Change since December 2018

**Table 5.4: Change in Best Start Grant spending since December 2018**

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|
| December 2018 | 2 | 12 | 13 | 13 | 14 | 15 |
| Take-up assumptions | 3 | 3 | 5 | 4 | 4 | 3 |
| Population update | 0 | -1 | -1 | -1 | -1 | -1 |
| Other data and modelling | 0 | 1 | 1 | 1 | 1 | 1 |
| First year eligibility | 0 | 4 | 0 | 0 | 0 | 0 |
| February 2020 | 4 | 20 | 18 | 17 | 17 | 17 |
| Change since December 2018 | 3 | 7 | 5 | 4 | 3 | 2 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link), Social Security Scotland (2019) Annual Report and Accounts (link).
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

5.25 Estimated take up has been higher than we had assumed in our December 2018 forecast, and we anticipate that the launch of Scottish Child Payment later this year will lead to further increases.

5.26 Updates to population data and projections reduce the forecast. The number of children under five in 2023-24 is around nine per cent lower than in our December 2018 forecast, with a proportionate effect on spending.

5.27 Our estimate of the proportion of the population who are eligible is slightly higher, increasing the forecast by £1 million in 2020-21 and beyond. There is a further increase of around £4 million for 2019-20 as our original forecast did not fully account for all the children aged between two and three and a half who became eligible at the launch of the Early Learning Payment.

## Forecast uncertainty

5.28 Setting take-up rate assumptions continues to be challenging. If the launch of Scottish Child Payment does not encourage higher take-up, then our forecast could be too high. Our forecast could also be too low if take-up for Best Start Grant aligns with the Scottish Government’s assumption that 83 per cent of eligible families will receive Scottish Child Payment.

5.29 We currently assume that 45 per cent of first births and around half of other births and young children are eligible for Best Start Grant. These assumptions could be a source of uncertainty for a number of reasons. For example, unemployment rates or take-up of qualifying benefits could change.

5.30 Our forecasts are based on a population projection in which the number of births remains fairly flat, but if fertility rates continue to fall as they have done in recent years then our forecast could be too high.

# Best Start Foods

## Forecast

**Table 5.5: Forecast spending for Best Start Foods and Healthy Start Vouchers**

| | | | Forecast on Scottish Government policy | | | | |
|---|---|---|---|---|---|---|---|
| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Healthy Start Vouchers [1] | 4 | 3 | 0 | | | | |
| Best Start Foods | | 3 | 9 | 8 | 8 | 8 | 8 |
| Total | 4 | 6 | 9 | 8 | 8 | 8 | 8 |

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding. Shaded cells refer to outturn available at the time of publication.
[1] Healthy Start Vouchers are run by the Department of Health and Social Care under UK Government policy, on behalf of the Scottish Government.

5.31 We forecast spending on Best Start Foods and Healthy Start Vouchers to peak at £9 million in 2020-21. Spending will initially include transitional protection for claimants of Healthy Start Vouchers, and then remain at around £8 million from 2021-22 onwards.

## Background

5.32 Best Start Foods launched in August 2019. The payments are made every four weeks and equate to £4.25 per week for each eligible family member. Those entitled are pregnant mothers, and children under three, with a double payment for babies up to their first birthday. It has the same application form and a similar set of qualifying benefits as Best Start Grant, but fewer families are eligible as the conditions also include an income limit.

5.33 Best Start Foods replaces Healthy Start Vouchers, which gives vouchers worth £3.10 a week to a similar set of families, but for children aged under four. During 2020-21 and 2021-22 Best Start Foods will also pay transitional protection to families of children aged three who had been receiving Healthy Start Vouchers prior to qualifying for Best Start Foods payments.

## Change since December 2018

**Table 5.6: Change in Best Start Foods and Healthy Start Vouchers spending since December 2018**

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|
| December 2018 | 4 | 4 | 5 | 4 | 4 | 4 |
| Transitional protection | | 1 | 1 | 0 | | |
| Launch date and rundown | | 0 | 1 | 0 | 0 | 0 |
| Population updates | 0 | 0 | 0 | 0 | 0 | 0 |
| Eligibility | 0 | 1 | 2 | 2 | 2 | 2 |
| Take-up | 0 | 1 | 1 | 2 | 2 | 2 |
| February 2020 | 4 | 6 | 9 | 8 | 8 | 8 |
| Change from December 2018 | 0 | 2 | 5 | 3 | 4 | 4 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link), Scottish Government.
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

5.34 Our December 2018 forecast did not include spending on transitional protection for families who were receiving Healthy Start Vouchers before the launch of Best Start Foods.

5.35 In our December 2018 forecast we assumed that Best Start Foods would launch in June 2019. The actual launch date was 12 August 2019. This reduces the spend on Best Start Foods in the first year, but other updates to our modelling of how Healthy Start Vouchers will run down have increased the forecast for 2020-21, as the Scottish Government will not be charged until next year for some of the vouchers issued in late 2019-20.

5.36 The projected number of children under three in 2023-24 is 10 per cent lower than in our December 2018 forecast, with a proportionate effect on spending.

5.37 In our previous forecasts we had assumed that the proportion of families who are eligible would fall through the early 2020s, primarily because of the income limits being fixed while earnings rise. Informed by Healthy Start Voucher management information up to late 2019 we now assume that the proportion of families who are eligible will rise a little in the short-term.

5.38 While the estimated eligible population is bigger than we had previously assumed, the estimated take-up rate for Healthy Start Vouchers has been lower. This reduces spend on Healthy Start Vouchers in 2019-20. We assume higher take-up rates for Best Start Foods, in light of early management information, the joined up application process with Best Start Grant, and the announcement of the new Scottish Child Payment.

## Forecast uncertainty

5.39 We currently assume that around 19 per cent of families with children under three will be eligible. This assumption could prove wrong for a number of reasons, with a proportionate effect on spending. For example, unemployment rates or take-up of qualifying benefits could change, or rising incomes could take more families above the income threshold.

5.40 If the launch of Scottish Child Payment does not encourage higher take-up of Best Start Foods, then our forecast of Best Start Foods could be too high. If take-up proves to be as high as the Scottish Government assumption that 83 per cent of eligible families will receive Scottish Child Payment then our Best Start Foods forecast will be too low.

5.41 Our forecasts are based on a population projection in which the number of births remains fairly flat, but if fertility rates continue to fall as they have done in recent years then our forecast could be too high.

# Discretionary Housing Payments

## Forecast

**Table 5.7: Forecast spending for Discretionary Housing Payments**

| | | Forecast on Scottish Government policy | | | | | |
|---|---|---|---|---|---|---|---|
| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Bedroom tax mitigation [1] | 52.5 | 56.3 | 59.7 | 62.9 | 65.3 | 67.8 | 70.4 |
| Other DHPs [2] | 9.1 | 10.9 | 12.9 | 12.9 | 12.9 | 12.9 | 12.9 |
| Total | 61.7 | 67.2 | 72.6 | 75.8 | 78.2 | 80.7 | 83.3 |

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.
[1] Also known as the 'removal of the spare room subsidy', the bedroom tax is the reduction in housing support for people living in social housing who are deemed to have a spare bedroom.
[2] This represents the Scottish Government's announced funding plans, not a forecast of need or demand.

5.42 We forecast spending on Discretionary Housing Payments (DHPs) will be £73 million in 2020-21, rising to £83 million in 2024-25. This includes an additional £2 million every year from 2020-21 to support care-experienced young people, as announced in the Programme for Government 2019-20.[80]

5.43 Spending to mitigate the bedroom tax is forecast to rise. This is driven by our forecast increase in social rents.

## Background

5.44 DHPs are awarded by local authorities to provide additional assistance with housing costs for people in receipt of Housing Benefit or Universal Credit.

5.45 The budget is split into two parts. The first part allocates a fixed pot of funding to each local authority to help pay for DHPs paid for any other reason. From 2020-21 this includes an element to provide financial support to care-experienced young people. We simply assume that this funding will be fixed over the forecast period. We do not forecast whether local authorities will spend all of their allocation, or assess whether the funding set by Scottish Government is reasonable. The second part fully reimburses local authorities for the costs of bedroom tax mitigation.

[80] Scottish Government (2019) Protecting Scotland's Future: the Government's Programme for Scotland 2019-2020 (link)

## Change since December 2018

**Table 5.8: Change in Discretionary Housing Payments spending since December 2018**

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|
| December 2018 | 61 | 63 | 65 | 66 | 68 | 69 |
| Rent and housing stock | 0 | 1 | 1 | 2 | 3 | 3 |
| Modelling of pension age | 1 | 2 | 3 | 4 | 4 | 4 |
| Other data and modelling | 1 | 1 | 1 | 2 | 2 | 2 |
| Recovered funding | -2 | 0 | 0 | 0 | 0 | 0 |
| Care-experienced people | | | 2 | 2 | 2 | 2 |
| February 2020 | 62 | 67 | 73 | 76 | 78 | 81 |
| Change since December 2018 | 0 | 4 | 8 | 10 | 11 | 12 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link), Scottish Government.
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

5.46 Social rents have grown faster than we had assumed, leading to higher spending in 2018-19 and a faster growth assumption for future years.[81] This effect was partly offset by a slower increase in the social housing stock.[82]

5.47 Our forecast now takes into account the increase in the State Pension age to 66 and the restrictions on access to Pension Credit and pensioner Housing Benefit for 'Mixed Age Couples'.[83]

5.48 The outturn spending reported for 2018-19 by local authorities was around one per cent higher than predicted by our updated model. As we have only partial data on the number and size of bedroom tax deductions in Universal Credit, it is difficult to determine what may be driving this, but we have assumed that around half of this unexplained growth will continue over the forecast period.

5.49 In 2018-19 the Scottish Government recovered around £2 million that local authorities did not use from the £10.9 million allocated for 'other DHPs'. The additional funding for care-experienced young people adds £2 million from 2020-21.

## Forecast uncertainty

5.50 The Scottish Government plans to mitigate the bedroom tax at source through higher Universal Credit awards. Given the uncertainty around the date when

[81] Scottish Housing Regulator (2019) Charter Indicators and Data by Outcomes and Standards (link)

[82] Scottish Government (2019) Stock by tenure 2018 (link)

[83] Department for Work and Pensions (2019) Changes to benefits for mixed age couples (link)

this will be possible we assume that DHPs will continue to be used to mitigate the bedroom tax for the entire forecast period.

5.51 Annual social rent increases and housebuilding levels could differ from our current assumptions.

5.52 The number of working-age social tenants receiving Housing Benefit or Universal Credit could change for reasons other than the pension age and housebuilding assumptions described above. For example, unemployment among social tenants could rise, or the rollout of UC could affect levels of eligibility and take-up.

5.53 In both 2017-18 and 2018-19, councils used around £9 million out of the £10.9 million funding that was available from the Scottish Government for purposes other than bedroom tax mitigation. If this pattern continues then our forecast will be around £2 million too high.

# Employability Services

## Forecast

**Table 5.9: Forecast spending for Employability Services**

| | | Forecast on Scottish Government policy | | | | |
|---|---|---|---|---|---|---|
| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
| Fair Start Scotland | 15 | 15 | 18 | 13 | 5 | 0 |
| Work Able Scotland | 0 | | | | | |
| Work First Scotland | 4 | 0 | | | | |
| Total | 19 | 15 | 18 | 13 | 5 | 0 |

Source: Scottish Fiscal Commission, Scottish Government (2019) Fair Start Scotland Annual Report Year 1 (link). Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

5.54 We forecast spending will peak in 2020-21 as people referred to the Fair Start Scotland service find employment and remain in work for long enough that performance fees are paid to the service providers.

## Background

5.55 Fair Start Scotland is a service designed to help people with disabilities or at risk of long-term unemployment to find sustained work. People will be referred to the service over three years from 2018-19 to 2020-21 and participation is voluntary. Work Able Scotland and Work First Scotland were transitional services which took referrals during 2017-18 and do not form part of the forecast for 2020-21 onwards.

5.56 The Scottish Government has contracted external providers to deliver the service over five years, paying them a regular service fee for the first three years, plus performance fees when participants achieve periods of sustained employment.

5.57 The forecast is produced using the Scottish Government's model, but the Commission has specified its preferred assumptions on the number of participants and the proportion who achieve sustained employment.

## Change since December 2018

**Table 5.10: Change in Employability Services spending since December 2018**

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|
| December 2018 | 19 | 19 | 28 | 22 | 9 | 0 |
| Data and modelling updates | -1 | -3 | -4 | -1 | 0 | 0 |
| Assume fewer participants | 0 | -1 | -1 | -1 | -1 | 0 |
| Assume fewer job outcomes | 0 | 0 | -4 | -7 | -3 | 0 |
| February 2020 | 19 | 15 | 18 | 13 | 5 | 0 |
| Change since December 2018 | -1 | -4 | -10 | -9 | -4 | 0 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link), Scottish Government.
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

5.58 The model provided by the Scottish Government has been updated for management information up to December 2019. There have been fewer participants and fewer job outcomes than originally assumed, reducing spending on performance fees.

5.59 Previously we assumed that the service would have a total of 38,000 participants. By the half way point, at the end of September 2019, there had been 16,000 starts.[84] While the Scottish Government aims to reach 38,000 participants, in our new forecast we assume that there will be 35,000, reducing the forecast by around five per cent.

5.60 Our May forecast used performance assumptions based on providers' forecasts of the number of job outcomes they would achieve. Aggregated across the providers, 39 per cent of participants were assumed to achieve a '13 week job outcome'. For people who joined the service in the first quarter of 2018-19, this has been achieved for 22 per cent of participants. In this forecast we assume that job outcomes will be achieved for 25 per cent of participants, as there is still time for the early cohorts to find work, and there is evidence of job outcomes being achieved more often for more recent cohorts.

## Forecast uncertainty

5.61 Our assumptions on the conversion rates from 13 week job outcomes to the 26- and 52-week periods in work which attract the largest fees are still based on providers' assumptions, as although the service has now been in place for 21 months, most participants have started too recently to be able to achieve a long period in work. As the longer job outcomes attract large performance fees spending is sensitive to these assumptions, which we will continue to review.

[84] Scottish Government (2019) Scotland's Devolved Employment Services: Statistical Summary (link)

# Funeral Support Payment

## Forecast

**Table 5.11: Forecast spending for Funeral Support Payment**

| | | Forecast on Scottish Government policy | | | | |
|---|---|---|---|---|---|---|
| £ million | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| | 4 | 9 | 10 | 10 | 11 | 11 |

Source: Scottish Fiscal Commission

5.62 We forecast Funeral Support Payment spending to grow from £4 million in 2019-20 to £11 million by 2024-25. Spending is lower in 2019-20 as Funeral Support Payment opened to new applications on 16 September 2019.

## Background

5.63 Funeral Support Payment is comprised of two components to cover reasonable burial or cremation costs and 'other' funeral expenses such as venue hire and funeral director costs.

## Scottish Government policy

5.64 The Scottish Government has increased the amount paid to cover other funeral costs from £700 in 2019-20 to £1,000 in 2020-21.[85] For the rest of the forecast horizon, the new rate will continue to be uprated annually. There is more detail on our costing of the policy change in Annex A. This change adds around £2 million to our forecast from 2021-22 onwards.

## Change since December 2018

**Table 5.12: Change in Funeral Support Payment spending since December 2018**

| £ million | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|
| December 2018 | 6 | 6 | 7 | 6 | 7 |
| Change in payment amount | 0 | 1 | 2 | 2 | 2 |
| Take up rate update | 0 | 0 | 1 | 1 | 1 |
| Change in start date | -2 | 0 | 0 | 0 | 0 |
| Data and assumptions update | 0 | 1 | 1 | 1 | 1 |
| February 2020 | 4 | 9 | 10 | 10 | 11 |
| Difference | -2 | 3 | 3 | 4 | 4 |

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts – December 2018 (link).
Figures may not sum because of rounding.

[85] Scottish Government (2020) Funeral Support Payment to be increased (link)

5.65 As stated in our May 2019 publication, we have updated our take-up rate assumptions, increasing them over the forecast horizon.[86] This was based on observed higher take-up for the Best Start Grant payments launched in December 2018.

5.66 Our forecast in December 2018 was developed with the assumption that Funeral Support Payment would launch on 1 June 2019. The actual launch was on 16 September 2019, shortening the window for applications in 2019-20 and reducing our forecast by £2 million.

5.67 We have updated our forecast of the average value of a Funeral Support Payment, in light of 2018-19 outturn for Funeral Expense Payments, and the first set of FSP statistics.[87]

5.68 We have also updated the forecast number of deaths in line with the new '2018-based' population projections released by the Office for National Statistics. These new projections have higher mortality rates than the previous edition, increasing the forecast.

5.69 On 10 June 2019, the BBC announced that people aged 75 years and over, and not receiving Pension Credit must pay for their TV licence from June 2020. Analysis by the OBR suggests that this change will increase Pension Credit take up, and in turn raise eligibility for Funeral Support Payment for pensioners.[88] We have taken this into consideration.

## Forecast uncertainty

5.70 The take-up rate for Funeral Support Payment remains the major source of uncertainty. We have started to receive preliminary management information from Social Security Scotland and we will continue to monitor and analyse the data as it becomes available. There is a possibility that the increase in payment amount would encourage more people to take up the benefit, thus raising the take-up rate for the later years of the forecast period.

5.71 The growth in the average amount paid for the UK Government benefit, Funeral Expense Payments, changes year on year. We use the average growth observed over the last five outturn years (currently around 1.5 per cent) to forecast the average amount paid. If the average amount paid for Funeral Support Payment grows at a significantly different rate to this estimate, it will affect our forecast.

[86] Scottish Fiscal Commission (2019) Scotland's Economic and Fiscal Forecasts – May 2019 (link)

[87] Scottish Government (2019) Funeral Support Payment: high level statistics to 31 October 2019 (link)

[88] Office of Budget Responsibility (2019) Fiscal Risks Report – July 2019 (link)

## Scottish Welfare Fund

**Table 5.13: Funding plans for the Scottish Welfare Fund**

| | | Forecast on Scottish Government policy | | | | |
|---|---|---|---|---|---|---|
| £ million | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| | 33.0 | 35.5 | 35.5 | 35.5 | 35.5 | 35.5 |

Source: Scottish Government

5.72 The Scottish Welfare Fund helps people on a low income who are in crisis because of a disaster or emergency and helps vulnerable people set up home or continue to live independently in their community. The Scottish Government provides funding to local authorities who then award the discretionary payments.

5.73 The Scottish Government has set the 2020-21 budget for the Scottish Welfare Fund at £35.5 million. This is a £2.5 million increase from 2019-20. Funding had remained constant at £33.0 million since 2013-14.

5.74 The Scottish Government has not informed us of any plan to make further changes to the level of funding for the Scottish Welfare Fund over the forecast period. We present the Scottish Government's funding plans in Table 5.13. We do not assess the demand for the Scottish Welfare Fund or whether the funding provided to local authorities is reasonable.

# Payments launching in 2020-21

5.75 Our forecasts include two new forms of assistance opening to applications in 2020-21 and included in the Scottish Budget 2020-21. In this section we provide our forecasts for Scottish Child Payment and Child Disability Assistance, which includes the Scottish Government's new Disability Assistance for Children and Young People.

## Scottish Child Payment

### Forecast

**Table 5.14: Forecast spending for Scottish Child Payment**

| | | | Forecast on Scottish Government policy | | |
|---|---|---|---|---|---|
| £ million | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| | 21 | 65 | 94 | 157 | 162 |

Source: Scottish Fiscal Commission

5.76 We forecast expenditure of £65 million in the first full year of implementation for children under six in 2021-22, and £157 million in the first full year of implementation for all eligible children in 2023-24.

### Background

5.77 The Scottish Government announced the Scottish Child Payment in June 2019 as a new benefit to help tackle child poverty by providing additional support for low income families.[89]

5.78 Scottish Child Payment will be administered by Social Security Scotland and will be an income supplement of £10 per week for each eligible child. The payment will be made every four weeks and increased annually in line with inflation. Eligibility for the payment will be based on receipt of qualifying benefits including Universal Credit and legacy benefits.

### Main assumptions

5.79 For children under six years old, the Scottish Government plans to have Scottish Child Payment open for applications in autumn 2020, with first payments made by Christmas 2020. In the absence of information about the actual start date, we have developed our forecast assuming that the first year will cover around four months of spending (December 2020 through to March 2021).

[89] Scottish Government (2019) Scottish Child Payment: Position Paper (link) and Scottish Government (2020) Updated Policy Position Paper (link).

5.80 The Scottish Government plans to extend the child payment to all children under the age of 16 by the end of 2022 and at this stage no further details are available on the start date. We assume that the launch of this extension will follow the same pattern as that for children under 6, and consequently the benefit will be available to all eligible children for around four months of spending in 2022-23.

5.81 Published Scottish Government analysis of Scottish Child Payment assumes a flat 83 per cent take-up rate over the forecast period, informed by estimates of Child Tax Credit take-up rates at different income levels.[90] We assume a slightly lower rate in the initial years that rises over the forecast period. Our caseload forecast can be found in Supplementary Table S5.19.

5.82 We assume a lower take-up rate for children aged six and over as their parents may not be eligible for the other benefits available for young children such as Best Start Grant, and may be less engaged with the public and third sector bodies who can encourage take up. Table 5.15 shows our take-up rate assumptions.

**Table 5.15: Take-up rate assumptions for Scottish Child Payment**

| Per cent | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|
| All under 6 years | 76 | 77 | 78 | 79 | 80 |
| All aged 6-15 | | | 66 | 68 | 70 |
| Average under 16 years | | | 71 | 72 | 74 |

Source: Scottish Fiscal Commission

## Forecast uncertainty

5.83 Scottish Child Payment is a new benefit with limited data available on which to base much of our modelling assumptions. This creates significant uncertainty around our forecast.

5.84 We have assumed relatively high take-up rates for Scottish Child Payment, rising over the forecast horizon. This is directly affected by the Scottish Government's advertisement and communication plans as noted in its benefit take-up strategy.[91] There is significant uncertainty on the take-up rates for new benefits and how take-up may change over the forecast horizon.

5.85 Changes to the actual start date will result in the expenditure for 2020-21 being different for our forecast. The same risk applies if the start date differs from our assumption for children aged over six.

[90] Scottish Government (2019) Analysis of Options for the Income Supplement (link).

[91] Scottish Government (2019) Social Security: benefit take-up strategy (link)

# Child Disability Assistance

## Forecast

**Table 5.16: Forecast spending for Child Disability Assistance**

| £ million | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|
| Total spend | 217 | 250 | 275 | 295 | 312 |
| **Forecast on UK Government policy** | | | | | |
| Disability Living Allowance for Children | 189 | 25 | | | |
| **Forecast on Scottish Government policy** | | | | | |
| Disability Assistance for Children and Young People | 27 | 225 | 275 | 295 | 312 |

Source: Scottish Fiscal Commission
Figures may not sum because of rounding.

5.86 The combined spending on Disability Assistance for Children and Young People (DACYP) and Disability Living Allowance for Children is forecast to increase from £217 million to £312 million over the period 2020-21 to 2024-25. We use the phrase ‘Child Disability Assistance’ to refer to the combination of DACYP and Disability Living Allowance for Children.

## Background

5.87 Disability Living Allowance for Children will be devolved to the Scottish Parliament from April 2020 but will continue to be administered by DWP. DACYP will open to new applications in summer 2020. Existing Disability Living Allowance for Children cases will be transferred to DACYP between summer 2020 and summer 2021. After all cases have been transferred to DACYP, Disability Living Allowance for Children will cease in Scotland.

5.88 There are some policy differences between DACYP and the current Disability Living Allowance for Children, which we forecast will lead to an increase in spending. Further details on our policy costing can be found in Annex A.

5.89 Recipients who get the highest level of care on Disability Living Allowance for Children or DACYP will also be eligible for an annual Child Winter Heating Assistance payment, starting in 2020. We include this in the DACYP spending.

## Main Assumptions

### Caseload Forecast

5.90 We forecast the Child Disability Assistance caseload to increase over the next five years, as shown in Supplementary Table S5.21. The Disability Living

Allowance for Children caseload will run to zero by 2022-23 as all cases will have been transferred to DACYP.

5.91 In order to forecast the combined Child Disability Assistance caseload we first model a baseline Disability Living Allowance for Children caseload based on historical data from DWP. We analyse these by individual ages in order to fully capture the growth in the caseload.

5.92 We then factor in the transfer of cases from Disability Living Allowance for Children to DACYP and take account of the effects that the new policy changes may have on the caseload. Further details on our policy costing can be found in Annex A.

5.93 We expect the changes to the application process to increase the caseload as more application routes will become available, as well as support with the application process for prospective clients. Similarly the changes made to the award review and duration are expected to increase the number of people receiving DACYP, although by a lesser extent than the changes to the application process. These effects are all captured in our DACYP caseload forecast in Supplementary Table S5.21.

5.94 Additional spending will arise from the increase in the age limit that a young person can stay on DACYP, to their 18$^{th}$ birthday instead of their 16$^{th}$ birthday as has been the case in Disability Living Allowance.

## Payment amount forecast

5.95 Our spending forecast depends on the number of people receiving payment, as well as the amount they are paid, their award. The award can be made up of both a mobility and care component. The payment rates for each component are the same for Disability Living Allowance for Children and DACYP. We include the underlying payment rates in Supplementary Table S5.22.

5.96 We forecast the average award for both Disability Living Allowance for Children and DACYP using historical Disability Living Allowance for Children information from DWP. The average award is uprated by inflation annually.

5.97 The average award for Disability Living Allowance for Children, in real terms, has been decreasing for the last four years, as a result of a decreasing proportion of the caseload getting higher awards. We assume this trend continues in future years for Disability Living Allowance for Children and DACYP.

## Spending forecast

5.98 We combine our caseload and average award forecasts, as well as the additional policy costs that affect spending, in order to reach a spending forecast. The additional policy costs we consider at this stage are Child Winter Heating Assistance and Short-Term Assistance.

5.99 Our spending forecast also includes an adjustment factor that aligns historic caseload data to published expenditure from DWP, and is then projected forward for the forecast years.

**Table 5.17: Breakdown of forecast spending for Child Disability Assistance**

| £ million | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|
| Baseline cost [1] | 202 | 214 | 226 | 237 | 246 |
| Application process | 2 | 7 | 9 | 12 | 14 |
| Child Winter Heating Assistance | 3 | 3 | 4 | 4 | 4 |
| Extension to 16 and 17 year olds | 9 | 23 | 33 | 39 | 43 |
| Other costs | 0 | 2 | 3 | 4 | 5 |
| Child Disability Assistance | 217 | 250 | 275 | 295 | 312 |

Source: Scottish Fiscal Commission
Figures may not sum because of rounding.
[1] The cost if Disability Living Allowance for Children continued without policy change.

5.100 Other costs consist of: widening of the terminal illness eligibility, changes to award duration and reviews and the introduction of Short-Term Assistance.

5.101 The additional cost of increasing the age limit to the 18th birthday is cancelled out by the corresponding decrease in PIP spending, when disability support spending is looked at as a whole.

## Forecast uncertainty

5.102 As DACYP is a new policy there are no historical data that we can use to base our forecast on, so instead we rely on Disability Living Allowance for Children historical data to provide the baseline of our forecast. There are numerous policy and process changes, each carrying its own level of uncertainty and each modelled using a set of assumptions. This means there is significant uncertainty in our forecast. Further details on uncertainties around the DACYP costing can be found in Annex A.

5.103 The Scottish Government has published draft secondary regulations for DACYP and the entitlement rules are broadly unchanged from DWP's Disability Living Allowance for Children benefit.[92] There is a risk to our forecast that case advisors at Social Security Scotland may interpret these entitlement rules differently to their DWP counterparts, although they are legislatively similar. The guidance for case advisors at Social Security Scotland is currently being drafted so at this stage we do not know how it compares to the existing DWP guidance. We may also expect a behavioural

[92] Correspondence (2019) Cabinet Secretary for Social Security and Older People to Social Security Committee Draft DACYP regulations (link)

response from applicants but it is too early to be able to quantify this, given the guidance has yet to be published.

5.104 There are also uncertainties in our baseline Disability Living Allowance for Children forecast. We forecast the real average award to follow a downwards trend, as has been the case for Disability Living Allowance for Children for the last four years. We do not have any information on whether this trend is likely to continue or for how long. This is a significant risk to the forecast as this average award is used to calculate expenditure for both Disability Living Allowance for Children and DACYP.

# Payments launching after 2020-21

5.105 The Scottish Government plans to launch a number of new payments after 2020-21.[93] These payments will replace existing UK Government benefits such as Attendance Allowance and Carer's Allowance. For the purposes of the Scottish Budget 2020-21, we provide forecast spending under existing UK Government policy for the following payments. As the Scottish Government announces their policy intent, we will incorporate these changes into future published forecasts.

## Personal Independence Payment

### Forecast

**Table 5.18: Forecast spending for Personal Independence Payment**

| | Forecast on UK Government policy | | | | |
|---|---|---|---|---|---|
| £ million | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| | 1,583 | 1,650 | 1,714 | 1,776 | 1,841 |

Source: Scottish Fiscal Commission

5.106 Spending on Personal Independence Payment (PIP) is forecast to increase from £1,583 million in 2020-21 to £1,841 million in 2024-25.

### Background

5.107 PIP was introduced in April 2013 to replace the working age component of Disability Living Allowance (DLA). The migration of cases from DLA to PIP is not yet complete, and DWP is currently inviting people on DLA to apply for PIP. Executive Competence for PIP will transfer to the Scottish Government on 1 April 2020. DWP will continue to administer the payments on behalf of the Scottish Government until Social Security Scotland takes over delivery of Disability Assistance for Working Age People (DAWAP) in early 2021.

5.108 From April 2020, DLA recipients in Scotland will no longer be invited to move to PIP.[94] After this date, there will be a small number of new PIP claims from DLA recipients such as people reporting a change in circumstances.

5.109 The Scottish Government has set out its ambition for Disability Assistance.[95] DAWAP is expected to be introduced in early 2021. The Scottish Government

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[93] Disability Assistance for Working Age People will be launched in early 2020-21. We have made a judgement to produce a forecast for Disability Assistance for Working Age People once policy and administrative details are clearer. There will not be a replacement for Severe Disablement Allowance.

[94] Parliamentary Question S5W-24954 (link)

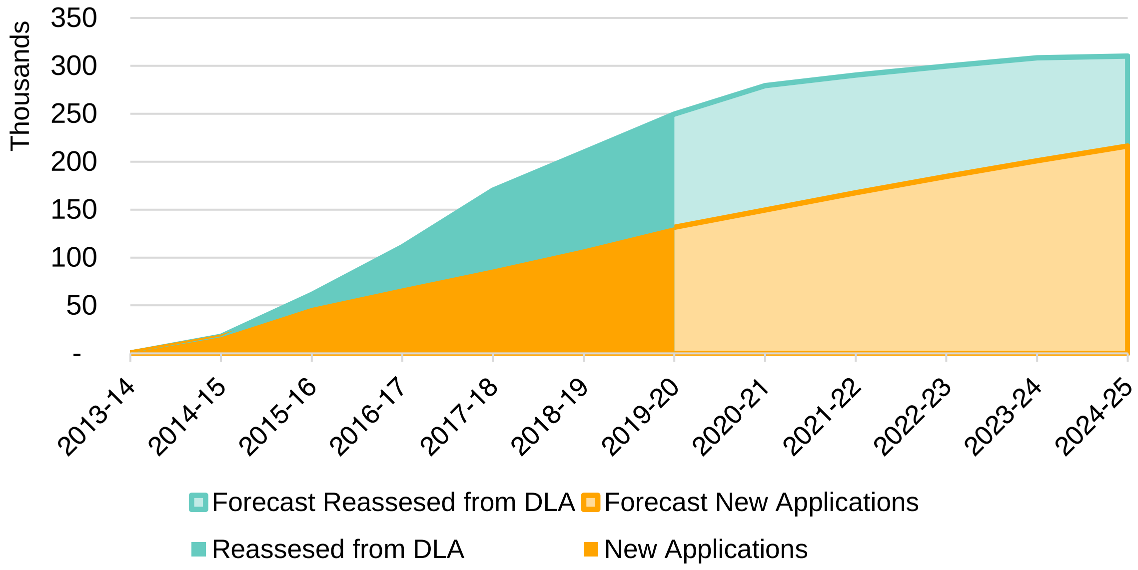
[95] Scottish Government (2019) Disability Assistance policy position papers (link)

is still developing the details of DAWAP and there is further work to be done including draft secondary legislation and associated guidance. Although the high level policies have been set out, the details will be developed over the next year before the policy is launched. In this particular case, we have made a judgement to produce a forecast for DAWAP once policy and administrative details are firmer. Therefore, the following forecast is based on current UK Government policy and does not account for any changes in spending associated with DAWAP.

## Main assumptions

5.110 The number of people receiving PIP support as a percentage of the population has been increasing in recent years.[96] We expect this trend to continue in future years as shown by our caseload forecast in Figure 5.5. We look at different groups of people who make applications to PIP, for example those who are terminally ill and make an application under special rules. Considering the past trends in how many people have made a successful application helps inform our judgment on future levels of awards.

**Figure 5.5: PIP caseload**




Source: Scottish Fiscal Commission

5.111 It is possible to apply for PIP up to State Pension age. A rise in the State Pension age increases the number of people eligible to apply for PIP. The male and female State Pension age increases to 66 over the period March 2019 to October 2020.

5.112 The introduction of DACYP in 2020-21 will extend the current DLA for Children upper age limit from 16 to 18 years. We expect that this policy change will decrease the number of people receiving PIP, as these people will

[96] OBR (2019) Welfare Trends Report (link)

continue to receive DACYP payments instead of applying to PIP (an individual cannot be in receipt of both payments). 16 and 17 year olds can still make a new application to PIP. Details can be found in Annex A.

5.113 Our forecast depends on the number of individuals receiving payments and how much they receive. We base our estimate of the average weekly payment on trends in the combinations of the mobility and daily living awards for different groups of people in recent years. Our estimate of the average weekly payment reflects trends in the mobility and daily living award combinations for different groups of people in recent years. PIP payments will be increased by inflation each year, also referred to as uprating.

5.114 Our spending forecast contains model adjustments that align our estimates to past spend. In addition, our forecast includes further adjustments to account for spending changes as a result of outstanding legal cases against DWP not reflected in the data.

## Forecast uncertainty

5.115 The PIP forecast is subject to a high level of uncertainty. The forecast not only depends on the ongoing reform of the UK welfare system, but also on the introduction of the new benefits delivered by Social Security Scotland.

5.116 Our estimates of the number of cases coming in and out the caseload are based on previous years' trends. PIP was introduced in 2013, and although trends have started to emerge, it may take many years to reach a steady state after such a major reform.

5.117 The oldest people in the caseload are currently 71 years old, which will increase to 75 by the end of 2024-25. We do not yet have data for people at those older ages so we assume that the trends that apply at younger ages will also apply. An older caseload could result in higher exit rates, the rate at which people stop receiving payments, than is currently forecasted.

5.118 We have made some adjustment for the potential effect of legal cases but there are several legal challenges against DWP which could have a significant effect on our spending forecast. Court rulings on current legal challenges could result in PIP payments being backdated or an increase in payment amounts.

5.119 The Conservative Party has pledged to increase the minimum award length for PIP from 9 to 18 months.[97] This change will increase spending on PIP and it is not currently included in our forecasts. We expect further information will become available as part of the upcoming UK Budget and we will include it in our next forecasts.

[97] Conservative Manifesto 2019 (link)

# Disability Living Allowance Adult

## Forecast

**Table 5.19: Forecast spending for Disability Living Allowance Adult**

| | | | Forecast on UK Government policy | | |
|---|---|---|---|---|---|
| £ million | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| | 502 | 470 | 440 | 410 | 380 |

Source: Scottish Fiscal Commission

5.120 We use the term ‘Disability Living Allowance (DLA) Adult’ to describe individuals over the age of 18 receiving DLA, this includes working age and pension age individuals. Annual spending on DLA Adult is forecast to decrease by 24 per cent over the forecast period from £502 million in 2020-21 to £380 million in 2024-25.

## Background

5.121 In April 2013, the UK Government introduced PIP to replace DLA for working age individuals. DWP is currently migrating working age DLA recipients to PIP. This migration will stop in Scotland when both payments are devolved to the Scottish Government in April 2020.

5.122 People who were over State Pension age and receiving DLA payments when PIP was introduced have not been migrated into PIP and remain on DLA. We have assumed that these individuals continue to remain on DLA where eligible and, with the exception of natural exits, for the remainder of the forecast period.

## Main assumptions

5.123 We split the DLA Adult caseload in two groups, DLA Working Age and DLA Pensioners, depending on the age people were when PIP was introduced in 2013. The first group is made of working age people and people who were working age when PIP was introduced but since have reached State Pension age. The latter group, DLA Pensioners, are people who were over State Pension age in April 2013 (and currently aged over 71) and who continue to be eligible for DLA payments. This allows us to account for the characteristics of the people in each group.

5.124 The DLA Working Age caseload is decreasing as people are migrated from DLA to PIP. This managed migration will stop once devolved to Scotland, but we expect a small number of working age DLA recipients will be migrated to PIP in April and May 2020 as their migration will have begun before the devolution date.

5.125 It is no longer possible to apply for DLA Adult so the caseload will continue to decrease over the next five years, for example as people reach the end of their award or have a change in circumstances. Our caseload forecast is shown in Supplementary Table S5.25.

5.126 The caseload for DLA Adult depends on the rate at which people stop receiving payments, known as the exit rate. We link the exit rate to the age of the individual. The exit rate of some individuals who were already over State Pension age when PIP was introduced can be more than double the working age exit rate.

5.127 Our forecast of spend is based on the forecast caseload and average payment. For the average payment we consider how many people are in receipt of the two components, care and mobility, and what levels they are paid. Older individuals tend to require more support and, therefore, receive higher payments. We estimate the forecast payments by separately projecting forward the historical average payment of the working age and pensioners groups.

5.128 The average weekly payments are uprated by inflation each year. This increases over time because of inflation but also as the caseload ages. The underlying payment rates we have used for our DLA Adult forecast are within Supplementary Table S5.26.

## Forecast uncertainty

5.129 The future DLA Adult caseload depends on the migration of people from DLA to PIP taking place up to April 2020. We estimate that approximately 109,000 individuals will remain on DLA Adult when it is devolved to Scotland in April 2020, of which 44,000 would be in the working age group and 65,000 in the pensioners group. While we are more confident about the number of people in the DLA pensioners group, we are less certain about the number of working age cases that are currently eligible for the migration to DLA but will not migrate by April 2020.

5.130 This forecast also depends on the Scottish Government's plans either to keep these groups on some form of DLA award or transfer them to its new Disability Assistance for Working Age People. We do not yet know the Scottish Government's plans for these groups and we will revise our forecasts when further details become available.

# Attendance Allowance

## Forecast

**Table 5.20: Forecast spending for Attendance Allowance**

| | | | Forecast on UK Government policy | | |
|---|---|---|---|---|---|
| £ million | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| | 532 | 546 | 562 | 582 | 601 |

Source: Scottish Fiscal Commission

5.131 Spending on Attendance Allowance is forecast to increase year on year throughout the forecast period. These forecasts are produced based on current UK Government policy.

## Background

5.132 Attendance Allowance helps with extra costs if an individual is over State Pension age and has a disability severe enough that they need someone to help look after them. Attendance Allowance will be devolved to the Scottish Parliament on 1 April 2020. DWP will continue to administer Attendance Allowance on behalf of the Scottish Government. Attendance Allowance will be replaced by the Scottish Government's Disability Assistance for Older People, with the Scottish Government expecting to publish draft regulations in winter 2020.[98]

## Main assumptions

5.133 There are two main assumptions within the Attendance Allowance model. The first relates to the number of people we expect to be supported, known as the caseload; and the second relates to how much we expect they will receive, the payment rate.

5.134 The caseload is calculated by considering the historic growth in the proportion of the population who receive Attendance Allowance payments. We take a three year average of the growth in the proportion of the population receiving Attendance Allowance and apply this to population projections to forecast the caseload. Our caseload forecast can be found in Supplementary Table S5.28.

5.135 To determine our forecast of the payment rate, we split the caseload into age bands and look at how the proportion of people on the higher or lower payment rate has changed over time. An increasing proportion of those in the 65 to 69 age band are receiving the higher rate payment. The proportion of those in the 90 and over age band who are receiving the higher rate payment

[98] Correspondence (2019) Cabinet Secretary for Social Security and Older People to Social Security Committee (link)

is decreasing. If younger recipients continue to receive higher payment amounts then this would gradually increase spending. We take an average of the historic trends to determine our forecast of what proportion of the caseload will be on the higher or lower rate.

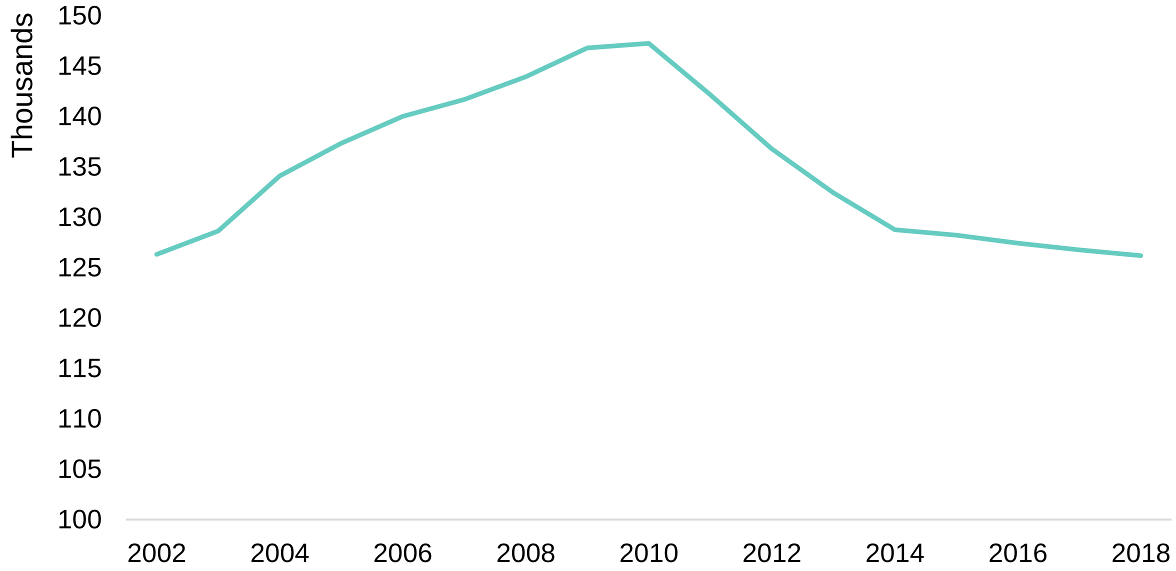
5.136 Attendance Allowance payment rates increase by inflation each year. The payment rates used in our Attendance Allowance forecast are in Supplementary Table S5.29.

5.137 We then combine our caseload forecast with our estimate of the caseload receiving each payment rate and the uprated payment rates to produce our spending forecast.

## Forecast uncertainty

5.138 From 2010 onwards there was a drop in the Attendance Allowance caseload as shown in Figure 5.6. It is noted in the OBR's January 2019 Welfare Trends Report that the proportion of the pensioner population receiving Attendance Allowance fell in the fifteen year period between May 2003 and May 2018, whereas the proportion of the pensioner population receiving DLA or PIP increased.[99] We expect that more working-age DLA and PIP claims continuing beyond State Pension age would decrease the number of applications to Attendance Allowance. We will continue to monitor the effect of trends in working-age disability benefits on the Attendance Allowance caseload for our future forecasts.

**Figure 5.6: Attendance Allowance historic caseload**




Source: Scottish Fiscal Commission, DWP (2019) Stat-Xplore (link).

[99] OBR (2019) Welfare Trends Report (link)

# Industrial Injuries Disablement Scheme

## Forecast

**Table 5.21: Forecast spending for Industrial Injuries Disablement Scheme**

| | Forecast on UK Government policy | | | | |
|---|---|---|---|---|---|
| £ million | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| | 80 | 79 | 78 | 78 | 77 |

Source: Scottish Fiscal Commission

5.139 Annual spending on the Industrial Injuries Disablement Scheme is forecast to decrease year on year throughout the forecast period. These forecasts are produced based on current UK Government policy. In 2020-21 spending is forecast to be £80 million.

## Background

5.140 We use the term Industrial Injuries Disablement Scheme (IIDS) to refer to a number of different forms of assistance that are being devolved to Scotland.[100] IIDS provides payments to eligible people who become ill or are disabled because of a disease or accident which took place at work or on an approved employment training course. IIDS will be replaced by Employment Injury Assistance, with the Scottish Government intending to publish draft regulations in winter 2021.[101]

## Main assumptions

5.141 Industrial Injuries Disablement Benefit (IIDB) forms the majority of the IIDS spend with over 70 per cent of the caseload in Scotland in March 2019.[102] We use a more complex methodology to forecast IIDB, and this is partly because this is effectively the only benefit that receives new applications.

5.142 People can move between different benefit types, for example between Reduced Earning Allowance and Retirement Allowance, but we do not expect new applications to the scheme for these smaller benefits. For our forecast, we use a more simplistic approach of trending spend downwards based on historic data.

5.143 For IIDB, we consider the historic trends in the caseload, split down into different age bands and by sex. It is important to distinguish the trends we are

[100] IIDS refers to the following benefits: Industrial Injuries Disablement Benefit, Reduced Earning Allowance, Retirement Allowance, Constant Attendance Allowance and Exceptionally Severe Disablement Allowance

[101] Correspondence (2019) Cabinet Secretary for Social Security and Older People to the Social Security Committee (link)

[102] DWP (2019) Industrial Injuries Disablement Benefit quarterly statistics: data to March 2019 – Table 2.2 (link)

seeing for different groups. Historically IIDB has been a form of support received mostly by men but there are increasing numbers of women accessing the benefit. The forecast number of individuals expected to receive Industrial Injuries Disablement Benefit payments can be found in Supplementary Table S5.31.

5.144 The amount that an individual receives is dependent on their individual circumstances. We look at the trends in the average weekly payment amount and assume these continue over the forecast period. The payment rate also increases by inflation each year. The forecast average payment amount can be found in Supplementary Table S5.32.

5.145 We combine our caseload forecast with our estimate of the average weekly payment amount to produce our spending forecast.

## Forecast uncertainty

5.146 The Industrial Injuries Advisory Council (IIAC) scrutinises the regulations for the Industrial Injuries Disablement Scheme and advise ministers on whether new diseases should be added to the list of prescribed diseases. The inclusion of new diseases on the advice of the IIAC would increase spend so this is an additional uncertainty for our forecasts.

5.147 We are using unpublished DWP data to forecast the IIDB spend. This is because the published data are not broken down for Scotland into age bands or by sex. Compared to other benefits which we forecast, we receive these unpublished data more infrequently and they are more out of date by the time we produce our forecasts. DWP does not have this information readily available and we are working with DWP to receive the data on a more frequent and timely basis.

5.148 We use a simplistic approach to forecast the spending for payments, other than IIDB, from the Industrial Injuries Disablement Scheme. Our preference is to use published data where possible and the published statistics do not provide a breakdown of the caseload or payment amounts for each scheme benefit. As the total spending for these smaller benefits is decreasing, we are comfortable with our approach, but may look to revise it if more granular data become available in the future.

# Severe Disablement Allowance

## Forecast

**Table 5.22: Forecast spending for Severe Disablement Allowance**

| | | | Forecast on UK Government policy | | |
|---|---|---|---|---|---|
| £ million | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| | 7 | 7 | 6 | 6 | 5 |

Source: Scottish Fiscal Commission

5.149 Spending on Severe Disablement Allowance is forecast to decrease year on year as it is closed to new applicants.

## Background

5.150 Severe Disablement Allowance is a form of disability assistance which was closed to new applications in 2001. The Scottish Government intends for DWP to continue to administer the payments on behalf of Social Security Scotland.[103]

## Main assumptions

5.151 The rate at which the caseload declined between 2017-18 and 2018-19 is assumed to continue in future years and is used to obtain the forecast caseload. The payment rates are increased in line with inflation each year and can be found in Supplementary Table S5.33. The caseload and payment rates are combined to produce our forecast.

5.152 The main judgement we make is how we allow for variation between the reported spending in Scotland each financial year and the spending calculated using DWP caseload and payment rate statistics. There have been historic differences between these figures and we may be understating the true spending by looking at the caseload and payment rate statistics alone. Part of this difference may be because of clerical cases which do not appear in the DWP caseload and payment rate statistics. We take an average of the historic difference and assume this applies in future years.

## Forecast uncertainty

5.153 As this benefit is no longer open to new applicants, the number of people receiving Severe Disablement Allowance support is declining. There is uncertainty regarding the rate of this decline. Variation from the historic rate of decline would result in differences in forecast spend.

[103] Scottish Government (2019) Severe Disablement Allowance: policy position paper (link)

## Illustrative Forecast – Cold Weather Payment

**Table 5.23: Illustrative spending for Cold Weather Payment**

| | | | Forecast on UK Government policy | | |
|---|---|---|---|---|---|
| £ million | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| | 16 | 16 | 16 | 16 | 16 |

Source: Scottish Fiscal Commission

5.154 This is an illustrative forecast based on current UK Government policy for Cold Weather Payment. Cold Weather Payment will be devolved at a later date. The Scottish Government has announced plans to replace Cold Weather Payment with Cold Spell Heating Assistance in winter 2021.[104]

5.155 A payment of £25 will be made to eligible individuals for each consecutive seven day period their area is forecast or recorded as being zero degrees Celsius or below, between 1 November and 31 March.

5.156 Our forecast of Cold Weather Payment spend is based on a historic average of the spending in previous years. There is significant uncertainty on the level of spending because of the unpredictable nature of the weather. Therefore a simplistic approach has been taken to forecast expenditure, aligned with the funding arrangements in the fiscal framework.[105]

[104] Correspondence (August 2019) Cabinet Secretary for Social Security and Older People to Social Security Committee (link)

[105] The agreement between the Scottish Government and the United Kingdom government on the Scottish Government's fiscal framework (link)

## Illustrative Forecast – Winter Fuel Payment

**Table 5.24: Illustrative spending for Winter Fuel Payment**

| | | | Forecast on UK Government policy | | |
|---|---|---|---|---|---|
| **£ million** | **2020-21** | **2021-22** | **2022-23** | **2023-24** | **2024-25** |
| | 169 | 171 | 174 | 177 | 180 |

Source: Scottish Fiscal Commission

5.157 This is an illustrative forecast based on UK Government policy for Winter Fuel Payment. Winter Fuel Payment will be devolved at a later date. The Scottish Government has announced plans to replace Winter Fuel Payment with Winter Heating Assistance in winter 2021.[106]

5.158 This payment, between £100 and £300, is designed to help an individual pay for their heating bills. To qualify in 2019-20, a person must be born on or before 5 April 1954 and be living in the UK at some point in a qualifying week.

5.159 Spending on Winter Fuel Payment increases over time because the population aged over State Pension age in Scotland is forecast to increase.

[106] Correspondence (August 2019) Cabinet Secretary for Social Security and Older People to Social Security Committee (link)

# Annex A
# Policy Costings

## Introduction

A.1 This annex sets out the different steps and judgments taken to arrive at our costings of the Scottish Government's new policy proposals. As ever, we welcome discussion about the approaches and judgments we have taken.

## Previous policy costings

A.2 Our May 2019 publication included costings for policies announced by the Scottish Government at their Medium Term Financial Strategy.

A.3 In December 2019, we updated our forecasts of income from Non-Domestic Rates (NDR) and produced policy costings for a number of policies introduced in the Non-Domestic Rates (Scotland) Bill. The Bill was introduced on 25 March 2019 and completed Stage 2 on 4 December 2019. On 18 December 2019, the Scottish Government published a Financial Memorandum ahead of the Stage 3 debate. We published our supplementary costings of policies included in the Bill, including those changed at Stage 2, on the same date.[107]

A.4 This section only provides costings for policy changes which we have not previously costed. Where we have previously provided a policy costing, any further changes will be captured in Annex B on policy recostings.

A.5 Annex C sets out our approach to handling policies with a very small fiscal effect that we do not consider to be material in cost. It also sets out the Scottish Government's policy on the Reverse Vending Machine Relief and explains why we have not produced a costing for this policy.

## New policy costings

A.6 Table A.1 provides a summary of new policy costings included in our forecasts. Negative figures indicate a reduction in the Scottish Budget through

[107] Scottish Fiscal Commission (2019), Non-Domestic Rates (Scotland) Bill Supplementary Costings – December 2019 (link).

lower tax revenue or higher social security spending, and positive figures indicate an increase.

A.7 The Scottish Government plans to introduce the Scottish Child Payment later this year. This is an entirely new payment that is not replacing any UK benefit so the costing is simply the forecast presented in the Social Security chapter.[108]

A.8 The Scottish Government has announced an increase of £2.5 million to the funding of the Scottish Welfare Fund, and additional funds for Discretionary Housing Payments to support care-experienced young people. In both cases we assume that this extra funding continues over the forecast period. We have not produced policy costings as these are simply changes in the funding levels decided by the Scottish Government. These are shown in Table A.1.

**Table A.1: Policy costings to accompany the Scottish Budget 2020-21**

| £ million | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|
| Income tax: | | | | | | |
| Higher rate threshold of £43,430 in 2020-21 | | 51.4 | 54.2 | 56.4 | 59.3 | 63.3 |
| Non Domestic Rates: | | | | | | |
| Intermediate Property Rate | | -7.3 | -7.4 | -8.0 | -8.0 | 0.0 |
| Land and Buildings Transaction Tax: | | | | | | |
| New tax rate for leases | 1.6 | 10.1 | 10.5 | 11.0 | 11.4 | 11.9 |
| Social Security: | | | | | | |
| DACYP | | -5.7 | -12.8 | -16.0 | -19.1 | -22.6 |
| Scottish Child Payment | | -21.2 | -64.9 | -94.4 | -157.2 | -161.8 |
| FSP fixed rate rise | | -1.4 | -1.5 | -1.6 | -1.6 | -1.7 |
| Increased SWF funding | | -2.5 | -2.5 | -2.5 | -2.5 | -2.5 |
| Increased DHP funding | | -2.0 | -2.0 | -2.0 | -2.0 | -2.0 |
| **Overall effect of new policy proposals** | **1.6** | **21.3** | **-26.4** | **-57.1** | **-119.7** | **-115.4** |

Source: Scottish Fiscal Commission
Figures may not sum because of rounding.

108 It is likely that in the absence of the Scottish Child Payment announcement we would have reduced our take-up assumptions for some elements of Best Start Grant, so Scottish Child Payment could be seen as carrying a small additional cost associated with higher take-up of other payments for young children.

# Income Tax

## Title of Measure

**Higher rate threshold freeze in 2020-21**

## Measure Description

A.9 The higher rate threshold for Scottish Non-Savings Non-Dividend (NSND) income tax will be frozen at £43,430 in 2020-21. All other bands except the top rate threshold, including the higher rate threshold from 2021-22 onwards, will be increased with CPI inflation.

A.10 Table A.2 compares the higher rate threshold announced in the 2020-21 Scottish Budget to our baseline assumption. All other tax rates and bands used to produce our forecast can be found in Supplementary Table S4.3.

**Table A.2: Comparison of policy and baseline higher rate threshold assumptions**

| £ | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|
| Baseline | 44,175 | 45,007 | 45,907 | 46,826 | 47,763 |
| Policy | 43,430 | 44,248 | 45,133 | 46,036 | 46,957 |
| Difference | -745 | -759 | -774 | -790 | -806 |

Source: Scottish Fiscal Commission
Figures may not sum because of rounding.

## The cost base

A.11 The cost base is all taxpayers in Scotland who earn more than £43,430. Our forecast of the number of taxpayers in Scotland can be found in Supplementary Table S4.6.

A.12 We estimate that in 2020-21 there are 19,000 taxpayers, who we had previously expected to be intermediate rate taxpayers, who will now be higher rate taxpayers. These taxpayers will pay an extra 20 per cent on each pound earned, up to a maximum increase of £149 in their income tax liabilities.

A.13 The freeze in the higher rate threshold will also affect all existing higher and top rate taxpayers. We estimate that there are around 370,000 higher and top rate taxpayers who will see an increase in their income tax liabilities of £149.

## The costing

A.14 Table A.3 shows our costing for this policy. We expect the policy to raise £51 million in 2020-21.

**Table A.3: Costing of the 2020-21 higher rate threshold freeze**

| £ million | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|
| Static costing | 59 | 62 | 66 | 71 | 75 |
| Behavioural response | -7 | -8 | -10 | -11 | -12 |
| Post-Behavioural costing | 51 | 54 | 56 | 59 | 63 |

Source: Scottish Fiscal Commission
Figures may not sum because of rounding.

A.15 We have changed our approach to policy costings to account for behavioural responses to the difference between the income tax systems in Scotland and the rest of the UK. More detail on the policy costing can be found in Supplementary Table S4.9.

## Uncertainties around the costing

A.16 The main uncertainty around the costing is the size of the behavioural responses. Because we do not yet know what UK income tax policy will be in 2002-21, the size of the behavioural response to the divergence between Scotland and the rest of the UK is highly uncertain.

A.17 Other sources of uncertainty are the size of the tax base in Scotland and Scottish taxpayers' earnings growth. If the number of higher rate taxpayers or growth in earnings in Scotland are significantly different to our forecast, this will affect income tax revenue.

# Non-Domestic Rates

## Title of measure

**Introduction of an Intermediate Property Rate**

## Measure description

A.18 The Scottish Government has announced the introduction of an Intermediate Property Rate (IPR) as of 1 April 2020. While properties with a rateable (RV) above £95,000 will continue to be charged the Higher Property Rate (formerly Large Business Supplement) of 2.6p on top of the poundage, properties with an RV of between £51,000 and £95,000 will now be charged a supplement of 1.3p on the standard poundage.

A.19 The power to set the IPR by subordinate legislation was introduced by Section 153 of the Local Government etc. (Scotland) Act 1994.[109] Section 8C of the Non-Domestic Rates (Scotland) Bill, introduced at Stage 2, repeals Section 153.[110] As a result, any NDR supplement introduced using Section 153, including IPR, will be abolished when section 8C is commenced. As in our December 2019 supplementary costing we assume that this will take effect on 1 April 2024, and our costing for IPR becomes zero in 2024-25.

## The cost base

A.20 The cost base is all non-domestic properties with an RV between £51,000 and £95,000. We estimate this to be around 10,000 properties.

## The costing

A.21 The costing proceeds in two steps. We use the valuation roll to identify all properties with an RV between £51,000 and £95,000 and we apply the IPR to these, in place of the HPR. This lowers gross NDR income. Reliefs are forecast using the growth rate of gross income. Since this growth rate will be lowered in 2020-21 by the introduction of the IPR, our forecast for relief income is also affected by this change. The second step is to adjust our forecasts for the effect of the IPR on our policy costings for the Non-Domestic Rates (Scotland) Bill. Table A.4 shows the total reduction in NDR income as a result of the introduction of the IPR.

[109] Local Government (etc.) (Scotland) Act 1994 (link)

[110] Scottish Parliament (2020) Non-Domestic Rates (Scotland) Bill (link)

**Table A.4: Costing of the Intermediate Property Rate**

| £ million | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|
| | -7 | -7 | -8 | -8 | 0 |

Source: Scottish Fiscal Commission

## Uncertainties around the costing

A.22 There are several uncertainties around the costing. First, our costing is based on information available before Stage 3 of the Non-Domestic Rates (Scotland) Bill. Should any further amendments be made that might affect our IPR costing, we will not have accounted for them. Second, while we are able to capture current properties that will be affected, we are unable to know exactly how many new properties with an RV between £51,000 and £95,000 will be entered onto the valuation roll in the future. Finally, we do not include any estimate of any potential behavioural response to the tax change, as we have no evidence base on which to do so.

# Land & Buildings Transaction Tax (LBTT)

## Title of measure

**Introduction of a new tax band for non-residential leases**

## Measure description

A.23 As of midnight on 7 February 2020, the Scottish Government is creating a new tax band for non-residential leases where the net present value (NPV) of the rent is above £2 million. These will pay 2 per cent on the portion of the NPV of the rental value above £2 million. Table A.5 sets out the change to the tax.

**Table A.5: Non-Residential LBTT tax rates and bands for leases**

| | NPV of rent (£) | LBTT rate (per cent) |
|---|---|---|
| Pre-7 February 2020 | Up to 150k | 0 |
| | Over 150k | 1 |
| 7 February 2020 onwards | Up to 150k | 0 |
| | 150k to 2m | 1 |
| | Over 2m | 2 |

Source: Revenue Scotland (link)

## The cost base

A.24 The cost base is all non-residential lease transactions where the net present value of the rent is over £2 million. We expect that around 300 leases will be affected by the policy change in 2020-21.

## The costing

A.25 Our starting point is our forecast for non-residential LBTT from leases before the tax change. We apply the new tax system to our forecast for the distribution of leases to calculate the effect of the higher tax rate. We then estimate the effect of changes in taxpayer behaviour as a result of the rate increase using the OBR semi-elasticities for non-residential prices and transactions.[111] The 2019-20 figure of £2 million in Table A.6 reflects the fact that the policy change takes effect with only two months left to go in the financial year.

[111] Office for Budget Responsibility (2017), Supplementary forecast information release – Non-residential SLDT elasticities (link)

**Table A.6: Costing of the new tax rate for leases**

| £ million | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|
| | 2 | 10 | 11 | 11 | 11 | 12 |

Source: Scottish Fiscal Commission

## Forestalling

A.26 As the policy takes effect within hours of its announcement, we have made no further adjustment to our costing for forestalling. We also make no adjustment for the transitional arrangements for the same reason.

## Three yearly reviews of leases

A.27 We note that on three yearly reviews, the review will be carried out based on the tax rates and bands that were in place at the time the lease was originally taken out. This will also be the case where leases are assigned, extended or terminated. We make no further adjustments to the costing to account for reviews.

## Uncertainties around the costing

A.28 There are two main uncertainties around the costing. Significant deviations in our forecasts for price and transactions growth from what we eventually observe will lead to errors in our costing estimates. Secondly, our estimate of the behavioural response by taxpayers may differ from what eventually transpires. In particular, we have no evidence on whether the change in tax rate might lead to some lease transactions being replaced by conveyances or not.

# Social Security

## Title of Measure

**Disability Assistance for Children and Young People**

## Measure Description

A.29 Disability Assistance for Children and Young People (DACYP) will replace DLA for Children in Scotland from summer 2020. The new benefit will continue providing financial assistance to meet the increased cost incurred as a result of a disability or long term condition. The structure of DACYP is aligned with DLA for Children but there are differences in the application and review processes as well as a widening of eligibility for some groups, such as terminally ill people and increasing the age a claimant can remain on the caseload.[112]

A.30 We detail the policy changes we expect to affect spending below. Full details on the proposals for DACYP can be found in the Scottish Government's policy paper.[113]

## The cost base

A.31 We estimate spending and caseload for DACYP using our DLA for Children model as a baseline, then cumulatively add the additional caseload and spending for each policy change. We also consider the effect these policy changes will have on the Personal Independence Payment (PIP) caseload and spending, given the corresponding effect of the change in the age restriction.

A.32 Office for National Statistics (ONS) population projections inform our assumptions on caseload and new applications, and National Records of Scotland (NRS) death statistics help inform our assumptions for terminal illness claims.

## The costing

A.33 Policy changes lead to an additional spend of £6 million in 2020-21 and £23 million by the end of the forecast period in 2024-25. This represents a nine per cent increase in cost by the end of the forecast period compared to if DLA for Children had continued without any policy changes.

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[112] Scottish Government (2019) Disability assistance: comparison of provision (link)

[113] Scottish Government (2019) Social Security (link)

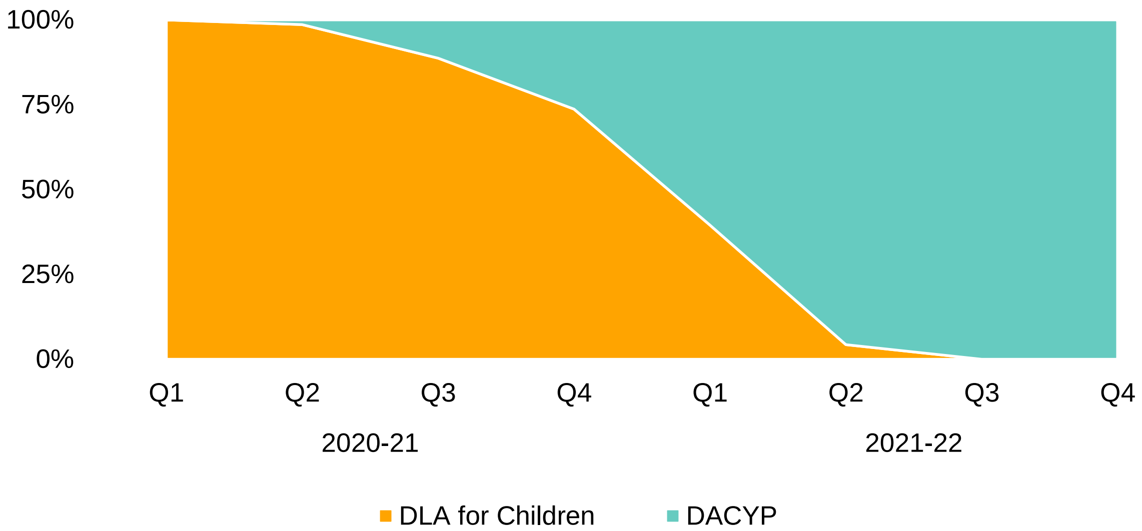
**Table A.7: Costing of the overall policy change to Child Disability Assistance**

| £ million | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|
| Overall Policy Cost | 6 | 13 | 16 | 19 | 23 |
| Policy Cost to DLA for Children/DACYP | 14 | 36 | 49 | 58 | 66 |
| Effect on PIP spending | -9 | -23 | -33 | -39 | -43 |

Source: Scottish Fiscal Commission
Figures may not sum because of rounding.

A.34 In the absence of a start date, we assume DACYP is launched at the start of September 2020, when new claims will stop being accepted into DLA for Children and start going into DACYP. Once DACYP has launched people receiving DLA for Children will gradually be transferred from the DWP system to DACYP, which will be administered by Social Security Scotland (SSS). We assume this transfer also begins in September 2020. Figure A.1 shows the proportion of the Child Disability Assistance caseload receiving DLA for Children and DACYP based on the assumption of a gradual transition of cases.

**Figure A.1: DLA for Children and DACYP caseload breakdown illustration**




Source: Scottish Fiscal Commission

A.35 Table A.8 shows the forecast additional spending for Child Disability Assistance, resulting from the Scottish Government’s policy changes to DACYP and the transition from DLA for Children.

**Table A.8: Disability Assistance for Children and Young People policy costing**

| £ million | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|
| Policy Cost to DACYP [1] | 14 | 36 | 49 | 58 | 66 |
| Application process | 2 | 7 | 9 | 12 | 14 |
| Child Winter Heating Assistance | 3 | 3 | 4 | 4 | 4 |
| Other costs | 0 | 2 | 3 | 4 | 5 |
| Extension to 16 & 17 year olds | 9 | 23 | 33 | 39 | 43 |

Source: Scottish Fiscal Commission

Figures may not sum because of rounding. Case transfer is cost neutral so not shown above.

[1] This is the policy cost to Child Disability Assistance – it is not the overall policy cost as a result of introducing DACYP as the effect on PIP spending is not factored in here.

### Application process

A.36 The Scottish Government will introduce a set of measures to widen the application channels and provide support to applicants. We anticipate that the proposed changes to the application process will lead to an increase in new claims and therefore inflows. We forecast a spike in inflows when DACYP is launched, as this will be a high profile benefit with significant media coverage.

A.37 From 2021-22 onwards, we expect the number of new cases to have stabilised at a consistently higher level than the historical inflows into DLA for Children. Our assumption is that inflows from 2021-22 will be 10 per cent higher than what we would have seen if DLA for Children had continued without any policy changes, with an initial 50 per cent spike for the first three months after DACYP is launched, falling to a 20 per cent increase after this until the end of the 2020-21 financial year. This increase in inflows increases the caseload and spending.

### Child Winter Heating Assistance

A.38 The Scottish Government plans to introduce a new payment as part of DACYP, Child Winter Heating Assistance (CWHA). Children receiving the highest rate of the care component on either DACYP or DLA for Children will receive an annual CWHA payment of £200 each year, in addition to their existing disability payments.

A.39 Additional payments will start in winter 2020, with those receiving the highest rate of care in September 2020 qualifying for the payment. We use historical data to estimate the proportion of people on the highest rate of care and project this forward for the forecast horizon.

### Other Costs

A.40 The first component of other costs is the changes to the terminal illness definition.[114] We estimate that changes to the terminal illness definition has no material effect on spending, given the low number of terminally ill children in Scotland and the duration of their awards.

A.41 The next component of other costs is the introduction of short-term assistance (STA). The estimated additional cost of providing STA to non-successful reviewed cases is less than £2 million as the success rate of DLA for Children cases at award reviews is high, so the number of children who get their award disallowed or decreased and thus could claim STA is low.

A.42 The final component is the set of measures that will affect the award duration and the award review process.[115] We model three effects that we expect to observe once this is introduced: less frequent award reviews, an increase in the average initial award length and light-touch award reviews.

A.43 We expect an increase in the average initial award length to mean a higher percentage of reviews will be reduced or ended instead of being maintained, as a person’s circumstances are more likely to have changed given the extra time that has elapsed.

A.44 We expect an increase in the average initial award length to increase the number of people on the caseload.

A.45 The final component is that reviews will be light-touch, where the award decision is reliant on supporting information and the self-reported needs of the claimant. We expect this to also increase the number of people on the caseload.

A.46 We forecast the combined effect of these three components to increase the number of people of the caseload and increase spending. Award reviews will be less frequent and although this will lead to more award being reduced or ended, light-touch reviews and longer initial awards will increase the number of people on the caseload to a greater extent.

### Cost neutral policy changes

A.47 The extension to 16 and 17 year olds is a cost neutral change when all disability benefits are considered together. The additional cost for DACYP is offset by the corresponding saving for PIP. Extending the age someone can stay on Child Disability Assistance means more people continue receiving an award for longer as not all those on DLA for Children are successfully reassessed in PIP. The average payment for DLA for Children is lower than

[114] Scottish Government (2019) Terminal illness and Disability Assistance: policy position paper (link)

[115] Scottish Government (2019) Disability Assistance awards and entitlement: policy position paper (link)

the average payment received for PIP, so these two effects cancel each other out.

A.48 We modelled the case transfer between DLA for Children and DACYP and forecast this to be cost neutral, so it is not shown in Table A.8 but is illustrated in Figure A.1.

## Uncertainties around the costing

A.49 Our costing is based on a number of assumptions. If any of these assumptions turn out to be incorrect then there is a risk the costing may not reflect actual additional spending. We detail the main assumptions and uncertainties that could pose a risk to the forecast in this section.

A.50 The Scottish Government has announced it intends to introduce DACYP in summer 2020. In the absence of information on a specific start date, we have assumed the benefit commences on 1 September. Any variation from the assumed start date will affect spending.

A.51 One of the biggest risks to the costing is the number of additional people in the caseload. Given that the application process is going to be made more accessible, reviews will be light-touch, initial awards will be longer, the eligible group will be widened to include 16 and 17 year olds and more people will qualify as terminally ill, it is difficult to forecast the additional caseload. This is a sizeable risk to the forecast.

A.52 We anticipate there will be a spike in new claims when DACYP first opens. The size of this effect is a significant risk to the first year's costing. The behavioural effect from new claims from people not currently on DLA for Children is unknown. The size of this spike in year one will also depend on the launch campaign conducted by the Scottish Government. This occurred with our September 2018 costing of the Best Start Grant where take-up was far higher than expected, in part because of promotion activity, leading to a large error in the forecast.

A.53 The expansion of the age restriction to allow 16 and 17 year olds to remain on the benefit is another uncertainty around the costing. We forecast this to be cost neutral between DACYP and PIP. This depends on our judgments on the DLA for Children and PIP payments and our estimate of the migration rate between DLA and PIP. If this turns out to differ from our judgements and is not cost neutral then it is likely to introduce an error into our forecast.

## Title of Measure

**Funeral Support Payment increase to £1,000**

## Measure Description

A.54 The amount paid for Funeral Support Payment (FSP) is comprised of two parts. The first covers reasonable burial or cremation costs. The second part is a flat rate that is paid to cover 'other funeral costs', such as funeral directors and venue hire.

A.55 The flat rate amount paid for other funeral costs will be increased from £700 in 2019-20 to £1000 in 2020-21,[116] and will be uprated using CPI inflation over the rest of the forecast horizon. In the baseline forecast it would have risen in line with inflation to £712 in 2020-21.

**Table A.9: Comparison of policy and baseline other funeral costs rate**

| £ | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|
| Baseline | 712 | 725 | 740 | 755 | 770 |
| Policy | 1,000 | 1,019 | 1,039 | 1,060 | 1,081 |
| Difference | 288 | 294 | 299 | 305 | 312 |

Source: Scottish Fiscal Commission, Scottish Government.

## The cost base

A.56 The cost base for this policy change is all FSP payments that include the standard rate for other funeral costs. Our forecast for the number of people expected to receive FSP each year is around five thousand and can be found in supplementary table S5.15.

## The costing

A.57 Table A.10 provides the forecast additional spending resulting from the Scottish Government's policy changes to the FSP payment amount. The increase of around £300 to around 5,000 payments expected to be made each year gives a costing of between £1 million and £2 million each year.

**Table A.10: Costing of the 2020-21 increase in other funeral costs payment**

| £ million | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|
| | 1 | 2 | 2 | 2 | 2 |

Source: Scottish Fiscal Commission

A.58 It is possible that the larger payment or publicity surrounding the increase may encourage more people to claim. Our baseline forecast already assumes that

[116] Scottish Government (2020) Funeral Support Payment to be increased (link)

take-up rates will increase, so we have made no adjustment for any behavioural response.

## Uncertainties around the costing

A.59 The main source of uncertainty is any error in the underlying forecast of FSP. This could come through our assumptions on eligibility and take-up rates, or through the OBR inflation forecasts and ONS deaths projections that we use.

A.60 Another source of uncertainty is the number of payments involving the death of a person with funeral plans or insurance. In these cases a rate of £120 is paid, which will increase in line with inflation as usual. There is limited information available and our judgement is that only a small proportion of payments include this lower rate. If this assumption proves wrong the costs of the policy will be lower.

A.61 Finally, a larger payment amount may encourage more people to claim, increasing the take-up rate.

# Annex B
# Policy Recostings

## Introduction

B.1 A policy recosting is a revised estimate of a policy that has been previously costed. There are two main reasons why we may recost previously announced or implemented policies.

- The outturn administrative data that includes the effects of the policy change is not yet available. For example, the 2018-19 income tax policy will not be present in the outturn data until summer 2020.
- We revise main judgements or assumptions relating to our previous policy costings – particular in response to new evidence.

B.2 This Annex sets out the latest policy recosting estimates and how they have changed from the previous costing. We publish this Annex twice a year as part of our Scotland's Economic Fiscal Forecast (SEFF) series.

**Table B.1: Latest policy recostings**

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| **Income Tax [1]** | | | | | | | |
| 2018-19 five band policy, *of which* | 197 | 197 | 205 | 212 | 219 | 226 | 238 |
| *Introduction of starter rate* | -47 | -48 | -50 | -52 | -53 | -55 | -57 |
| *Introduction of intermediate rate* | 131 | 133 | 142 | 150 | 157 | 166 | 174 |
| *Higher rate threshold adjustment* | 51 | 53 | 56 | 60 | 64 | 68 | 72 |
| *Increase in higher rate* | 59 | 61 | 64 | 67 | 70 | 73 | 77 |
| *Introduction of top rate* | 4 | 4 | 4 | 4 | 4 | 4 | 4 |
| 2019-20 policy | | 67 | 70 | 73 | 77 | 80 | 85 |
| | | | | | | | |
| **NDR [2]** | | | | | | | |
| Devolution of Empty Property Relief | | | | | 102 | 103 | 102 |
| Student Accommodation | | | | | 18 | 19 | 18 |
| Properties not in active occupation | | | 11 | 17 | 22 | 22 | 21 |
| Mainstream independent schools no longer eligible for charitable relief | | | 4 | 7 | 8 | 8 | 7 |
| Empty Property Relief reset period | | | 3 | 3 | | | |
| Commercial activity in currently exempt parks | | | | | 2 | 2 | 2 |
| Reliefs and Higher Property Rate terminated by Repeal of section 153 | | | | | | | 226 |
| | | | | | | | |
| **LBTT** | | | | | | | |
| ADS rate change, *of which* | | 34 | 27 | 26 | 26 | 27 | 27 |
| *ADS component [3]* | | 37 | 30 | 29 | 30 | 30 | 31 |
| *Residential component* | | -3 | -3 | -3 | -3 | -3 | -3 |
| Non-residential rate change | | 12 | 13 | 13 | 14 | 14 | 15 |

Source: Scottish Fiscal Commission

Figures may not sum because of rounding.

[1] These recostings are not a direct comparison to income tax policy for the rest of the UK, but to our baseline assumptions of uprating in line with CPI inflation for Scottish income tax bands (other than the top rate, which is assumed to be frozen). We have adjusted our costings to account for behavioural responses to the different tax systems in Scotland and the rest of the UK. The full static costing, behavioural reduction and post-behavioural income tax costing breakdowns can be found in Supplementary Tables S4.6, S4.7 and S4.8.

[2] These policies were costed for our publication "Supplementary Costings: Non-Domestic Rates (Scotland) Bill December 2019" which was published on 18 December 2019 (link). No changes have been made since then.

[3] Effect on net ADS revenue

**Table B.2: Change since December 2018**

| £ million | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|---|
| **Income Tax** | | | | | | |
| 2018-19 five band policy, *of which [1]* | -5.6 | -9.6 | -12.7 | -16.7 | -22.4 | -28.4 |
| *Introduction of starter rate* | 0.8 | 0.1 | 1.1 | 0.4 | 0.6 | 0.7 |
| *Introduction of intermediate rate* | -0.9 | 0.9 | 1.1 | 1.7 | 2.4 | 3.8 |
| *Higher rate threshold adjustment* | -0.5 | 0.2 | 1.4 | 1.9 | 2.7 | 3.0 |
| *Increase in higher rate* | -6.9 | -6.9 | -6.4 | -6.0 | -6.0 | -6.6 |
| *Introduction of top rate* | 1.8 | 2.0 | 2.0 | 2.1 | 2.1 | 2.2 |
| 2019-20 policy | | -1.5 | -1.7 | -2.4 | -2.9 | -3.9 |
| **LBTT** | | | | | | |
| ADS rate change, *of which* | | 8.8 | 2.6 | 0.6 | 0.8 | 0.9 |
| *ADS component [2]* | | 9.7 | 4.1 | 2.2 | 2.2 | 2.2 |
| *Residential component* | | -0.9 | -1.6 | -1.6 | -1.4 | -1.3 |
| Non-residential rate change | | -0.9 | -0.9 | -0.9 | -1.0 | -1.1 |

Source: Scottish Fiscal Commission

Figures may not sum because of rounding.

[1] We have revised our policy costings methodology to account for responses to the difference between Scotland and the rest of the UK. We have not accounted for this in our costings of individual components of the 2018-19 policy. Because of this, the costings below do not sum to the total. For more detail, see our breakdown of the 2018-19 policy costing in supplementary table S4.6.

[2] Effect on net ADS revenue.

# Annex C Materiality and policy costings

## Introduction

C.1 The Commission produces policy costings alongside our forecasts to show the effect changes made by the Scottish Government have on tax revenues and social security spending. We produce forecasts to accompany the Scottish Budget, and cost policies announced at these fiscal events.

C.2 Annex A of our report sets out the costings for policies announced since our last publication, which we have not already costed. Annex B provides information on revised estimates of previously costed policies, known as recostings.

C.3 The tax revenues devolved and assigned to Scotland will amount to over £20 billion a year, once fully implemented. The social security spending being devolved to Scotland equates to around £3.5 billion a year. Some policies announced by the Scottish Government will have a very small fiscal effect. This annex sets out our approach to handling policies we do not consider to be material in cost.

## Materiality Policy

C.4 The Commission has set thresholds under which policies will be deemed to be immaterial and therefore will not be costed.

C.5 Where a policy is estimated to cost less than £0.5 million per year it is considered negligible and therefore will not be costed. For policies with an estimated cost of £2 million or lower per year, a decision will be made whether to cost the policy or not.

C.6 Our decision as to whether or not to cost a policy require some, or all, of the following criteria to be met:

- high degree of confidence that the cost of the policy is low, even if there is a high degree of uncertainty as to the precise cost

- the cumulative changes being made do not push the policy above the materiality threshold
- limited risk of significant behavioural response.

C.7 The Commission's approach to corrections and revisions published in our statement of compliance with the code of practice for statistics categorises errors based on material/not material and important/not important.[117] This policy of materiality will also be applied in those circumstances.

C.8 The Commission has decided not to cost the following policies:

- Non-Domestic Rates (Reverse Vending Machine Relief) (Scotland) Regulations 2020. All Reverse Vending Machines will be eligible for 100 per cent relief and as such the impact on NDR income is zero. Our estimate of the gross cost of the relief is included in supplementary table S4.12.
- The Revenue Scotland Tax Powers Act 2014 (Amendment) Regulations 2020. This is an administrative change for which we believe there will be no financial implications as a result.

C.9 We will keep under review both our materiality policy, and the policies we have previously not costed to ensure that none of these are now above the thresholds.

[117] Scottish Fiscal Commission (2018) Compliance with the Code of Practice for Official Statistics (link)

# Abbreviations

| | |
|---|---|
| ADS | Additional Dwelling Supplement |
| ADT | Air Departure Tax |
| APD | Air Passengers Duty |
| ASHE | Annual Survey of Hours and Earnings |
| BGA | Block Grant Adjustment |
| BMW | Biodegradable Municipal Waste |
| CA | Carer’s Allowance |
| CAS | Carer’s Allowance Supplement |
| CAA | Civil Aviation Authority |
| CDEL | Capital Departmental Expenditure Limit |
| COE | Compensation of Employees |
| CPI | Consumer Price Index |
| CWHA | Child Winter Heating Assistance |
| DACYP | Disability Assistance for Children and Young People |
| DAWAP | Disability Assistance for Working Age People |
| DHP | Discretionary Housing Payment |
| DLA | Disability Living Allowance |
| DWP | Department for Work and Pensions |
| EU | European Union |
| FSP | Funeral Support Payment |
| FTA | Free Trade Agreement |
| FTB | First Time Buyer |
| GDP | Gross Domestic Product |
| HMRC | Her Majesty’s Revenue and Customs |
| HMT | Her Majesty’s Treasury |
| HPR | Higher Property Rate |
| IIAC | Industrial Injuries Advisory Council |
| IIDB | Industrial Injuries Disablement Benefit |
| IIDS | Industrial Injuries Disablement Scheme |
| IPR | Intermediate Property Rate |
| LBTT | Land and Buildings Transaction Tax |
| LFS | Labour Force Survey |
| MTFS | Medium Term Financial Strategy |
| NDR | Non-Domestic Rates |
| NIESR | National Institute of Economic and Social Research |
| NPV | Net Present Value |
| NRS | National Records of Scotland |

| | |
|---|---|
| NSND | Non-Savings and Non-Dividends |
| OBR | Office for Budget Responsibility |
| ONS | Office for National Statistics |
| PAYE | Pay As You Earn |
| PIP | Personal Independence Payment |
| PMI | Purchasing Managers’ Index |
| PUT | Public Use Tape |
| QNAS | Quarterly National Accounts Scotland |
| RDEL | Resource Departmental Expenditure Limit |
| RTI | Real Time Information |
| RV | Rateable Value |
| SEFF | Scotland’s Economic and Fiscal Forecasts |
| SFC | Scottish Fiscal Commission |
| SG | The Scottish Government |
| SLfT | Scottish Landfill Tax |
| SPI | Survey of Personal Incomes |
| SSS | Social Security Scotland |
| STA | Short-Term Assistance |
| SWF | Scottish Welfare Fund |
| TMI | Tax Motivated Incorporations |
| UC | Universal Credit |
| VAT | Value Added Tax |
| WA | Withdrawal Agreement |
| WTO | World Trade Organisation |

A full glossary of terms is available on our website:

http://www.fiscalcommission.scot/about-us/glossary-of-terms/

**Voluntary compliance with the Code of Practice for Statistics**

The Commission seeks to adhere to the highest standards for analysis possible. While we do not produce official statistics (we produce forecasts), the Commission and our work voluntarily complies as much as possible with the UK Statistic Authority's Code of Practice for Statistics. Further details and our statement of voluntary compliance can be found on our website.

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