Scottish Fiscal Commission

Scotland's Economic and Fiscal Forecasts

May 2023 (revised version June 2023)

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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 the Scottish economy, devolved taxes and devolved social security spending. Our forecasts represent the collective view of the four Commissioners of the Scottish Fiscal Commission and we take full responsibility for them.

Our forecasts have been used to inform the Scottish Government's Medium-Term Financial Strategy 2023, also published today. Our protocol for engagement with the Scottish Government guides our interaction with the Government during the forecasting process. We would like to thank the staff of the Commission as well as officials from the Scottish Government, Revenue Scotland, Social Security Scotland, Department for Work and Pensions, HM Treasury, HM Revenue and Customs, and the Office for Budget Responsibility for their support in creating this report.

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25 May 2023

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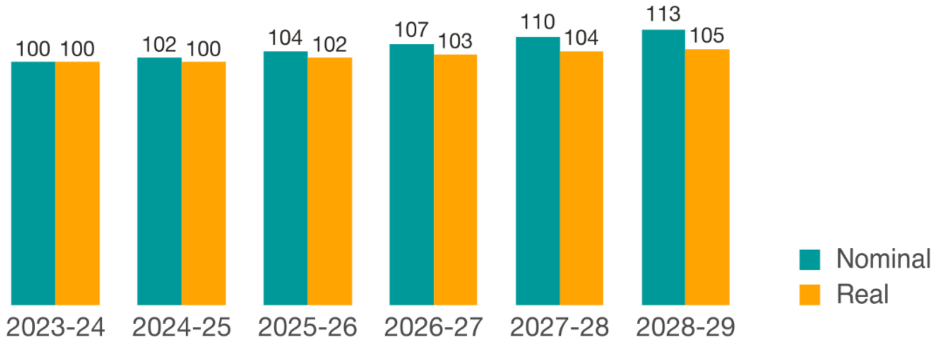
Fiscal Overview

Total funding is forecast to increase in all years in nominal terms until in 2028-29 it is 13 per cent greater than in 2023-24. Inflation will erode that growth to 5 per cent.

Resource drives this growth with increases in all years. Nominal capital funding will remain 8 per cent below 2023-24 levels throughout the period.

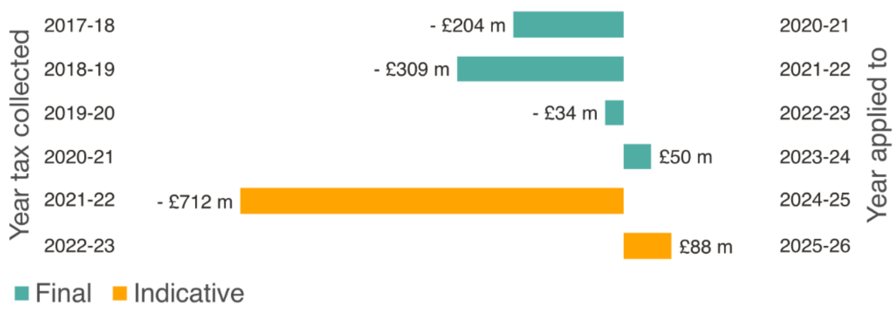
Medium-term outlook for total funding



Income tax reconciliations take place three years after the Budget when the funding was originally set.

In 2024-25 we still expect a large negative income tax reconciliation relating to 2021-22 revenues, which will exceed the fiscal framework borrowing limits. This will have a negative effect on resource funding.

Significant income tax reconciliation expected in 2024-25

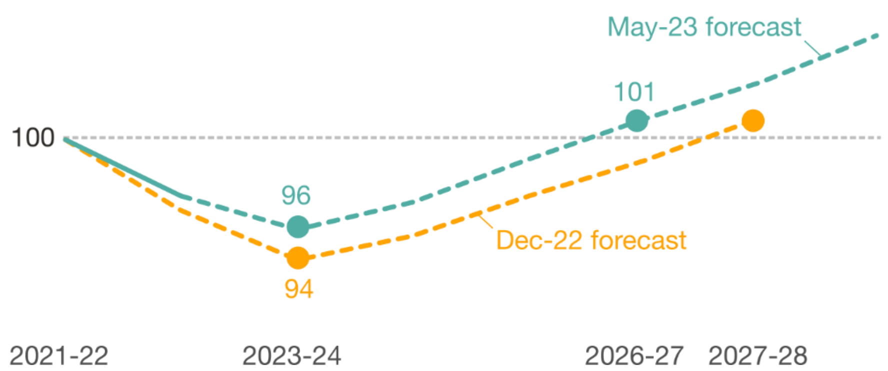


Economy

High inflation sees real disposable incomes per person fall by 4 per cent by the end of 2023-24, Scotland's highest fall in living standards on record.

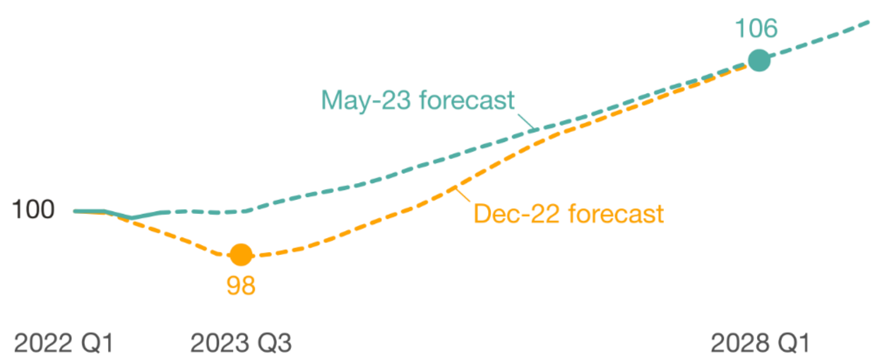
Living standards will take until 2026-27 to recover to their 2021-22 level. This outlook is improved since our December 2022 forecast reflecting lower energy price expectations.

Living standards to fall by less than previously expected

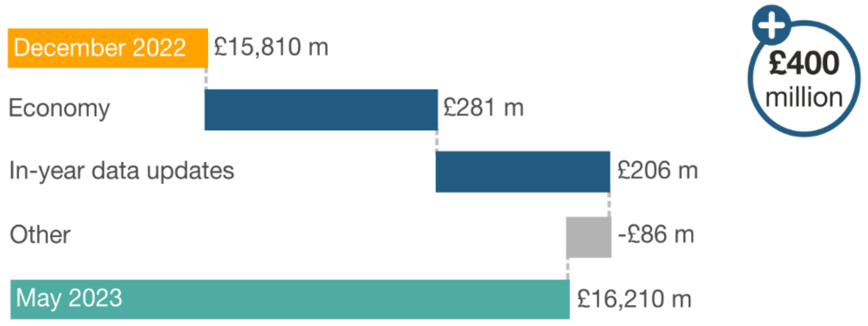


In line with the latest Gross Domestic Product (GDP) data and the improved outlook for energy prices we now forecast the economy to remain broadly flat in 2023-24 rather than fall into a shallow recession.

GDP to remain broadly flat this year



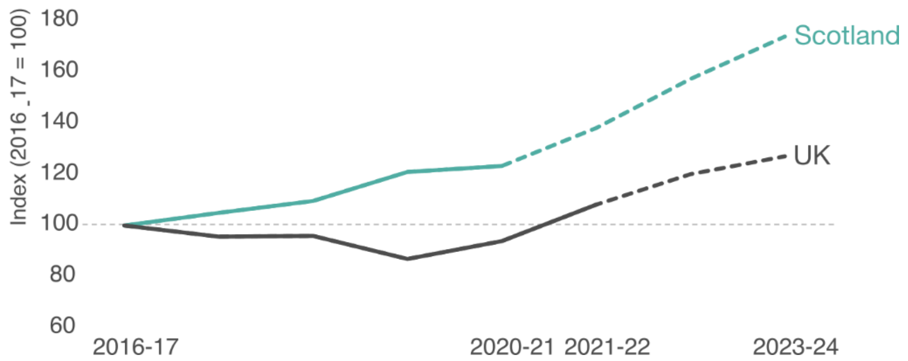
Income tax changes since December 2022 forecast



Our income tax forecast has been increased by higher employment growth, and nominal earnings growth.

Higher than expected RTI data on PAYE income tax receipts for 2022-23 also contribute positively.

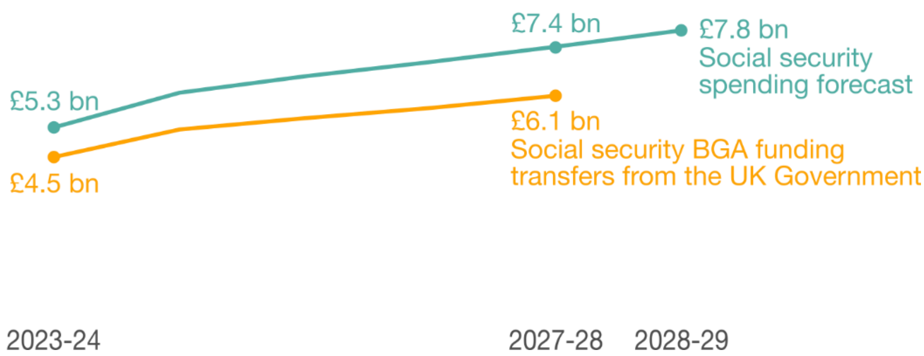
Growth in number of higher rate taxpayers



Since 2016-17, the Scottish higher rate threshold has largely been frozen. The number of higher rate taxpayers is expected to have increased by over 70 per cent in this time. The higher rate threshold freeze in the UK means the number of UK higher rate taxpayers is now also rising.

Social Security

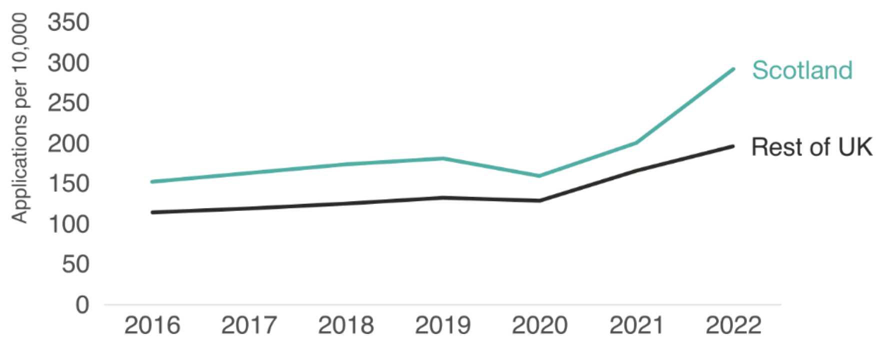
Spending increasing to £7.8 bn by 2028-29



Social security spending forecast to increase from £5.3 bn in 2023-24 to £7.8 bn in 2028-29.

By 2027-28, we expect the Scottish Government to spend £1.3 bn more on social security than the funding received from the UK Government through the BGAs.

Increased demand for disability payments for working age population



Demand for disability payments across the UK has increased substantially since 2020.

Disability payment forecasts have been revised up to reflect sustained demand at a higher-than-expected level.

	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Budget funding, £ million						
Total budget (nominal)	51,674	52,584	53,799	55,318	56,880	58,475
Total budget (2023-24 prices)	51,674	51,772	52,462	53,305	53,919	54,344
Economy, % growth						
GDP	0.3	1.0	1.3	1.3	1.4	1.4
Consumer Price Index	4.1	0.6	0.0	0.8	1.7	2.0
Average real earnings	0.9	1.8	2.1	1.5	1.1	0.9
Employment	0.3	0.0	0.3	0.3	0.3	0.3
Tax, £ million						
Income tax	16,210	17,080	17,808	18,591	19,646	20,799
Non-Domestic Rates	3,046	3,133	3,158	3,437	3,328	3,374
LBTT	772	733	792	905	992	1,053
Scottish Landfill Tax	92	83	58	16	16	16
Policy announcements, £ million						
Income tax	-14	-31	-75	-77	-81	-14
Non-Domestic Rates	-4	-2	0	0	0	-4
LBTT	1	5	2	-5	-5	1
Social Security, £ million						
All devolved social security	5,290	6,192	6,638	7,000	7,389	7,831

Summary

Introduction

1 The outlook for the Scottish economy, devolved taxes and social security presented in this report has remained broadly unchanged since our previous December 2022 forecasts. This contrasts with the volatility seen in recent years, which has resulted in regular and significant updates to our forecasts between recent publications. Though a technical recession has been avoided, economic activity remains muted, with falling living standards as the rising cost of living continues to put pressure on households.

2 Looking at our tax and social security forecasts, the updates we have made are largely incremental. Income tax revenues have been revised up in line with higher employment growth and higher nominal earnings growth driven by inflation. Following similar revisions by the Office for Budget Responsibility (OBR) to the income tax forecast for England and Northern Ireland, the income tax net position is largely unchanged, with a small upwards revision. As we have highlighted in previous reports, we continue to expect the income tax outturn data for 2021-22, due to be published this summer, to result in a large and negative income tax reconciliation in 2024-25, currently estimated at -£712 million.

3 As with the tax forecasts, there have been upward revisions to our forecasts of social security spending. The most important factor in the revisions has been an increase related to higher demand for disability benefits. This was something we included in our forecasts in December 2022, but the latest information shows the effect is stronger than previously anticipated.

4 The overall outlook for resource funding is for modest increases in real terms throughout the five-year forecast horizon. However, the Scottish Government's Medium-Term Financial Strategy (MTFS) provides projections for resource spending for 2024-25 to 2027-28 which show spending growing more quickly than funding in the central scenario, presenting a challenge for the Government in setting the Budget in future years. For capital funding the outlook is more constrained and it is projected to fall in both nominal and real terms over the next five years.

Economy

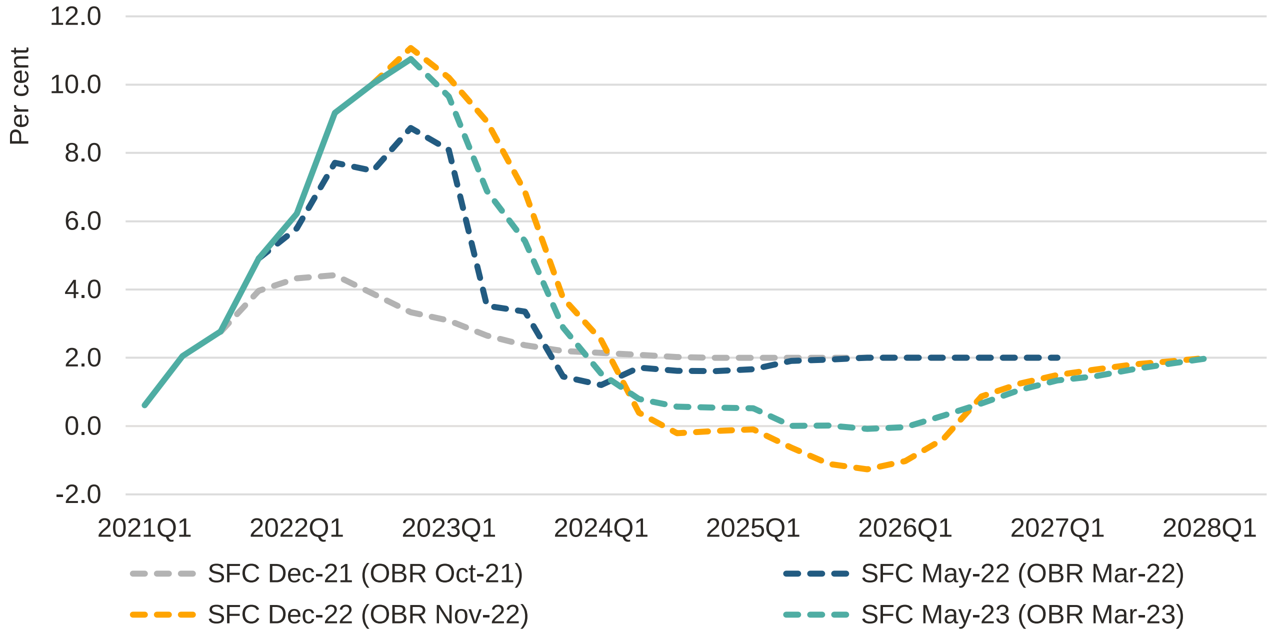
5 The overall outlook for the Scottish economy is largely unchanged since our December 2022 forecasts, with slow and fragile economic growth over the short term. In line with the latest Gross Domestic Product (GDP) data which have been mildly above expectations, we now forecast the economy to remain broadly flat this year rather than fall into a shallow recession.

6 Comparing to our December 2022 forecasts, energy prices have fallen back more quickly than expected, leading to slightly lower expectations for inflation and interest rates in the near term. This contributes to the marginally improved forecast for short-run GDP. Living standards, however, are still likely to fall this year because the overall rate of inflation – now reflecting a broader range of price rises than just energy – will continue to outpace growth in nominal household disposable

incomes. As we outlined in December, this means the coming years will continue to be difficult for many households, especially those with lower incomes.

7 Annual Consumer Price Index (CPI) inflation has come down from its peak of around 11 per cent in 2022 Q4 and is still expected to drop sharply over the course of this year, broadly on track with predictions from December.

Figure 1: Consumer Price Index inflation, year-on-year growth



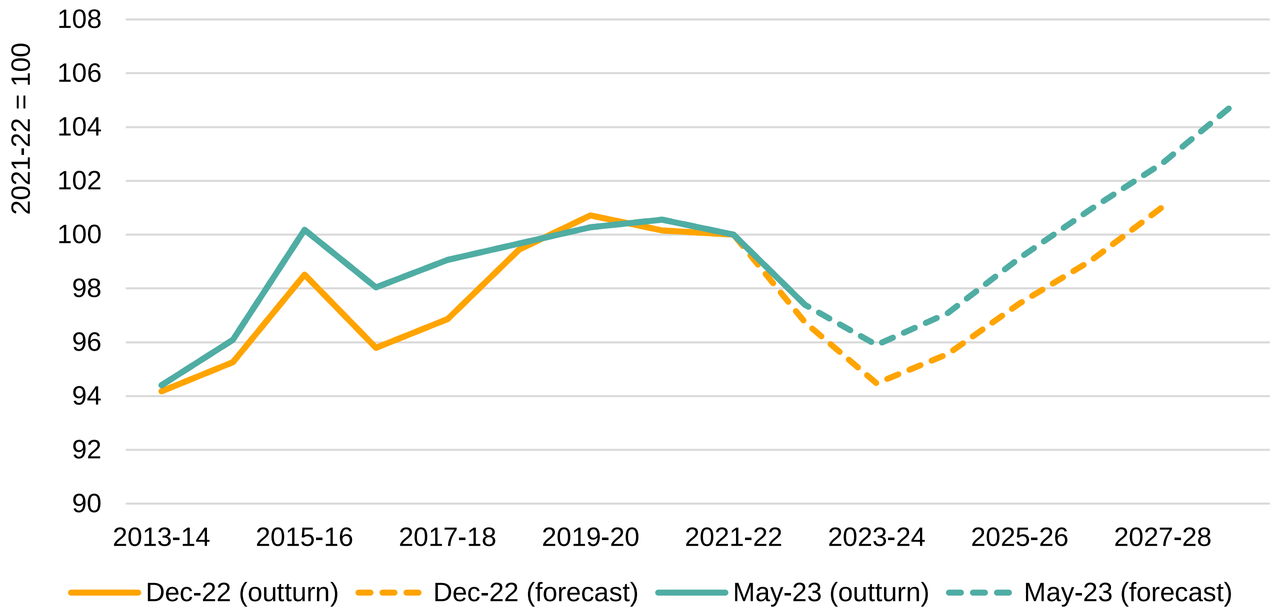
Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link), Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – May 2022 (link), Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – December 2021 (link), OBR (2023) Economic and fiscal outlook – March 2023 (link), OBR (2022) Economic and fiscal outlook – November 2022 (link), OBR (2022) Economic and fiscal outlook – March 2022 (link), OBR (2021) Economic and fiscal outlook – October 2021 (link).
Solid lines refer to outturn available at time of publication and dashed lines refer to forecasts.

8 Below the headline rate, we continue to see some variation in inflation among different items. Energy prices are expected to stabilise at current levels or fall further. This means energy price inflation, comparing today's prices to last year's very high levels, is on track to drop substantially. In contrast, food price inflation has been accelerating and is currently almost 20 per cent.

9 As in our December 2022 forecast, Scottish households are still expected to see the biggest fall in living standards – as measured by real disposable income per person – since Scottish records began in 1998, of 4.1 per cent between 2021-22 and 2023-24. This fall is slightly shallower than we forecast in December, reflecting the lower expectations for inflation and interest rates. Even once inflation returns to lower levels and real disposable incomes start to grow again in 2024-25, living standards will take time to recover to the 2021-22 level. Our forecast suggests that, by 2025-26, real disposable income per person will be no higher than a decade earlier. The energy price shock has prolonged a period of slow growth in living standards since the 2008-09 Global Financial Crisis, with real disposable income per person growing on average by only 0.6 per cent per year between 2008-09 and 2021-22 compared to 2.5 per cent per year before 2008-09.

10 Higher living costs affect everyone, but there are particular pressures on lower-income households, as they spend a larger share of income on essentials such as energy and food. Higher interest rates add to the costs of mortgages and other forms of debt for some households. However, Scotland has lower average house prices and lower average household debt as a share of income than the UK as a whole, so higher interest rates will tend to have a smaller effect in Scotland.

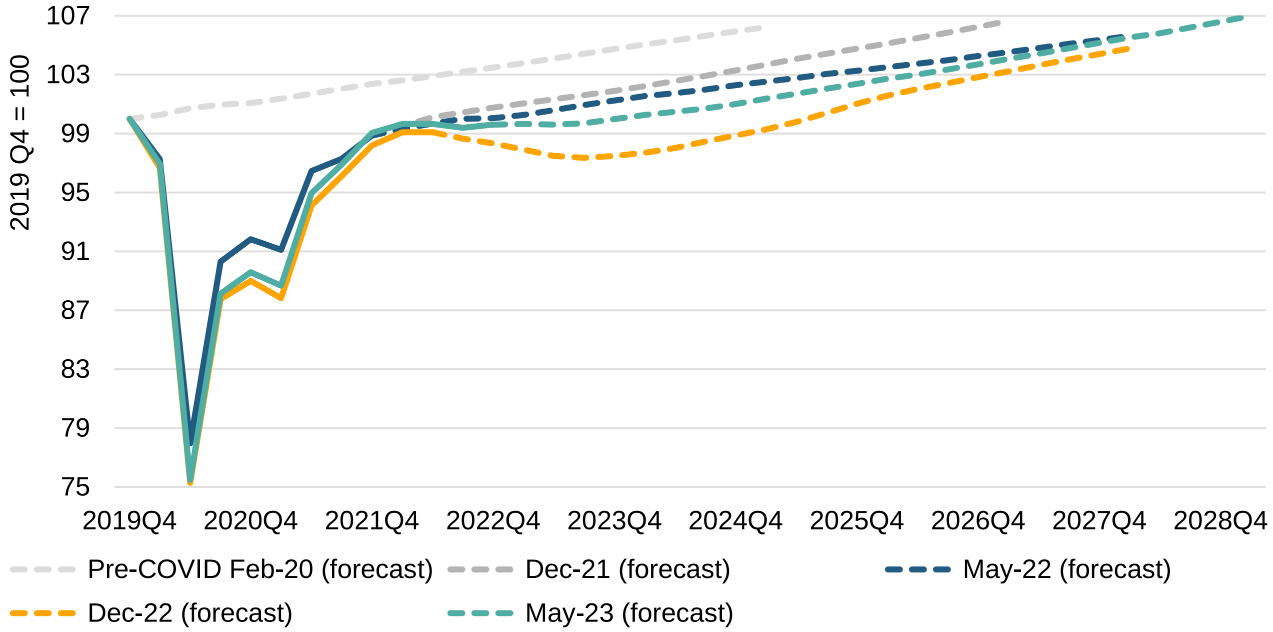
Figure 2: Real disposable income per person, 2021-22 equals 100



Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link).
Solid lines refer to outturn available at time of publication and dashed lines refer to forecasts. Amounts indexed so that 2021-22 is equal to 100.

11 As emphasised in our December 2022 report, when looking at GDP, we consider that the level of GDP in Scotland over the longer term is more important than the specific path for growth over the short term. Although we are no longer forecasting a technical recession, the overall environment remains one of slow and fragile economic growth. Even if a recession was to occur later in the year, or emerge in future revised data, we do not expect the underlying economic picture to be meaningfully different from that in this report.

Figure 3: Scottish GDP, 2019 Q4 equals 100



Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link), Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – May 2022 (link), Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – December 2021 (link), Scottish Fiscal Commission (2020) Scotland's Economic and Fiscal Forecasts – February 2020 (link).
Solid lines refer to outturn available at time of publication and dashed lines refer to forecasts. Amounts indexed so that 2019 Q4 is equal to 100.

12 As we noted in recent reports, the uncertainty around our economy forecasts has been greater than usual and, generally, this is also true this time around. The main source of uncertainty continues to be inflation, particularly its 'core' component which excludes energy and food. A wage-price spiral, which would keep inflation and interest rates higher for longer, also remains a risk.

13 Figure 4 shows further detail on our latest economy forecast and compares it to our December 2022 forecast.

Figure 4: Headline economy forecasts, growth rates unless otherwise specified

Per cent	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
GDP							
December 2022	1.7	-1.0	1.2	2.1	1.9	1.5	
May 2023	2.0	0.3	1.0	1.3	1.3	1.4	1.4
Consumer Price Index							
December 2022	10.1	5.5	0.0	-1.0	0.8	1.8	
May 2023	10.0	4.1	0.6	0.0	0.8	1.7	2.0
Unemployment rate							
December 2022	3.4	4.3	4.7	4.6	4.3	4.1	
May 2023	3.3	3.8	4.1	4.1	4.1	4.1	4.1

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link).
Shaded cells refer to outturn available at time of publication.

Tax

14 We expect devolved Scottish taxes to raise £20.1 billion of revenue in 2023-24, which is £384 million higher than in our December 2022 forecasts. Much of this change can be attributed to an increase in our forecast for income tax. We have seen a slight improvement in the underlying economy forecast as well as higher than expected Real Time Information (RTI) data on Scottish income tax Pay As You Earn (PAYE) receipts. Rising nominal earnings growth combined with tax thresholds that are fixed in nominal terms are driving up income tax revenues.

15 For Non-Domestic Rates (NDR) a new valuation roll was published on 1 April 2023, resulting in a small revision when included in our forecast. Our forecast for residential Land and Buildings Transaction Tax (LBTT) has increased because we revised our house prices forecast up slightly since December 2022 in light of a slightly more positive outlook for the economy. We have revised up our estimate of the amount of waste produced in 2022-23 and this has increased our forecast for Scottish Landfill Tax (SLfT).

The income tax net position

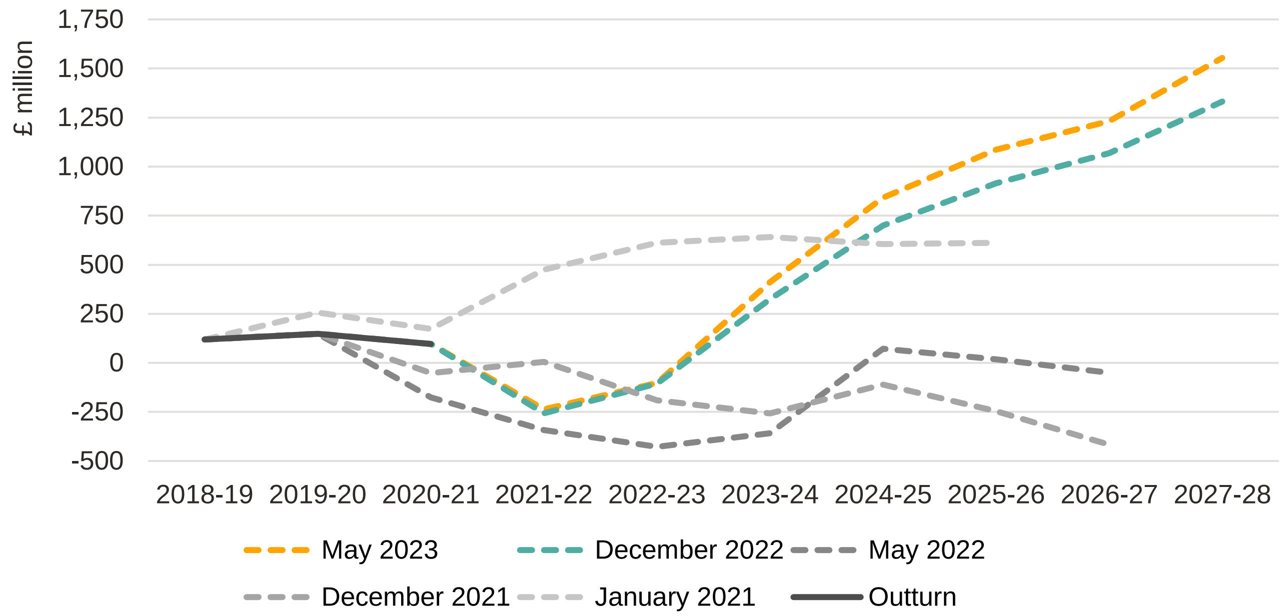
16 The income tax net position shows how the funding received from Scottish income tax revenues compares to the reduction in funding from the income tax Block Grant Adjustment (BGA). Estimates of the income tax net position can be calculated by comparing our forecasts to forecasts of BGA which is based on the OBR's forecasts.

17 In December 2022 our forecasts showed improvements in the net tax position over the five-year horizon compared to previous forecasts. Since then there have been further, although less substantial, improvements in the income tax net position in light of our and the OBR's latest forecasts. Figure 5 shows the different estimates of the income tax position since January 2021.

18 As we have stressed in previous reports, we continue to advise caution over the high outlook for the income tax net position. From experience, we can see that revisions to the outlook are quite common. The underlying Scottish and UK income tax forecasts are very large, with the income tax net position driven by the difference between the two. Relatively small changes in either forecast can lead to significant changes in estimates of the net position. In Figure 5 we show previous estimates of the net position back to January 2021 to illustrate this variability. Caution over the estimated income tax net position is particularly relevant now as the uncertainty around inflation makes variations in forecasts of income tax revenues in Scotland and the rest of the UK more likely.

19 As in December 2022, a divergence in earnings growth between our and the OBR's forecasts continues to be the main driver of the strongly positive estimated income tax net position for Scotland. In March 2023, the OBR forecast UK average nominal earnings growth of 2.0 per cent per year between 2024-25 and 2027-28, the same as in their previous forecast. This is lower than both our forecast of 2.6 per cent per year average nominal earnings growth in Scotland across the same period and the average UK earnings growth of 2.7 per cent per year between 2011 and 2022. If Scottish and UK earnings growth turn out to be closer in the coming years, the net position is likely to be materially lower than currently estimated.

Figure 5: The income tax net position comparison



Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link), Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – May 2022 (link), Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – December 2021 (link), Scottish Fiscal Commission (2021), Scotland's Economic and Fiscal Forecasts – January 2021 (link).
Solid lines refer to outturn available at time of publication and dashed lines refer to forecasts.

Income tax reconciliations

20 When the Scottish Budget is set, funding from Scottish income tax for the financial year is based on forecasts and does not change during the year. Only when outturn information on income tax revenues becomes available is funding brought in line with outturn and a reconciliation applied to the following Scottish Budget. We can derive indicative estimates of future income tax reconciliations by comparing our latest forecasts and the latest forecast Block Grant Adjustments (BGAs) to those used in the Budget setting forecasts.

21 As we have highlighted in recent publications, we continue to expect a large and negative income tax reconciliation for the Budget year 2021-22. Comparing our and the OBR's latest forecasts indicates a large negative reconciliation for 2021-22 of -£712 million. Final outturn data should be available in July 2023, with the resulting reconciliation being applied to the Scottish Budget for 2024-25.

22 The forecasts underpinning the Scottish Budget for 2021-22 were made during a time of significant uncertainty around Coronavirus (COVID-19). Figure 6 shows how forecasts of Scottish income tax revenues and the BGA have been updated since the 2021-22 Scottish Budget was set based on our January 2021 forecasts.

Figure 6: Scottish income tax (SIT) revenue forecast and BGA for 2021-22

£ million	Budget setting	Latest	Total Change
SIT	12,263	13,387	1,124
BGA	-11,788	-13,624	-1,836
Net position	475	-237	-712

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

23 In January 2021 we stated that the high Budget setting net position of £475 million largely arose because of the significant uncertainty around COVID-19 and its effects on the data and judgements used in our and the OBR's forecasts, as well as issues with the timing of forecasts.[1] We did not expect Scottish tax revenues to perform significantly differently to the UK in 2021-22. We cautioned that a negative reconciliation was likely, suggesting a value of -£300 million if the net position was closer to the lower 2020-21 value. Given the latest forecasts, the net position is now estimated to be -£237 million in 2021-22, leading to an indicative reconciliation estimate of -£712 million.

24 The reconciliation can still change between the final indicative estimate and the outturn data. For example, for the 2020-21 reconciliation, the final indicative estimate published in May 2022 was out by £221 million, a 1.8 per cent error when compared to the 2020-21 outturn. However, in general, as we get closer to the publication of outturn, we expect indicative reconciliation estimates to become more accurate. Some uncertainty always remains about the precise value of the reconciliation, with potential errors in both our and the OBR's forecasts.

25 Despite the uncertainty, we expect the 2021-22 reconciliation will be large, negative, and greater than the Scottish Government's borrowing powers or potential use of the Scotland Reserve. We are expecting to receive final outturn data for 2021-22 from HM Revenue and Customs (HMRC) in July 2023 and we will discuss the final reconciliation that will be applied to the 2024-25 Scottish Budget in our next Forecast Evaluation Report.

The effect of fiscal drag

26 Tax thresholds in Scotland and the UK have been rising by less than inflation. Over time, this is leading to increased fiscal drag, with the bulk of taxpayers paying a higher average effective tax rate and many taxpayers moving into higher tax bands. While this is happening in both Scotland and the UK, the effect is greater in Scotland.

27 The personal allowance, which is set by the UK Government but applies across the whole of the UK, has risen by only £70 since 2019-20 and is set to stay at £12,570 until 2027-28. As peoples' incomes rise with inflation, this means a greater proportion of their earnings will be subject to taxation.

28 On top of the freezing of the personal allowance, since 2017-18 the Scottish Government has increased income tax rates and largely frozen thresholds. The introduction of the intermediate rate of 21 pence in 2018-19, the freezing of the higher rate threshold, the increase in the higher rate of tax to 42 pence, and the increase in the top rate of tax to 47 pence have led to higher average effective tax rates for many taxpayers.

29 In 2016-17, prior to the devolution of income tax to Scotland, the higher rate threshold was £43,000 in both Scotland and the rest of the UK. Since income tax was devolved in 2017-18, the Scottish Government has largely kept the higher rate threshold frozen, or limited it to only small increases. In 2023-24, the higher rate threshold in Scotland is £43,662, a £662 increase over seven years. In contrast, the UK Government increased the higher rate threshold in the rest of the UK rapidly from 2016-17, reaching £50,000 by 2019-20. Since 2020-21, the UK higher rate threshold has risen more slowly and is set at £50,270 in 2023-24, then frozen until 2027-28.

30 These policies have had a large effect on the number of higher rate taxpayers. Figure 7 shows how the number of higher rate taxpayers has changed in Scotland and the UK since 2016-17. The

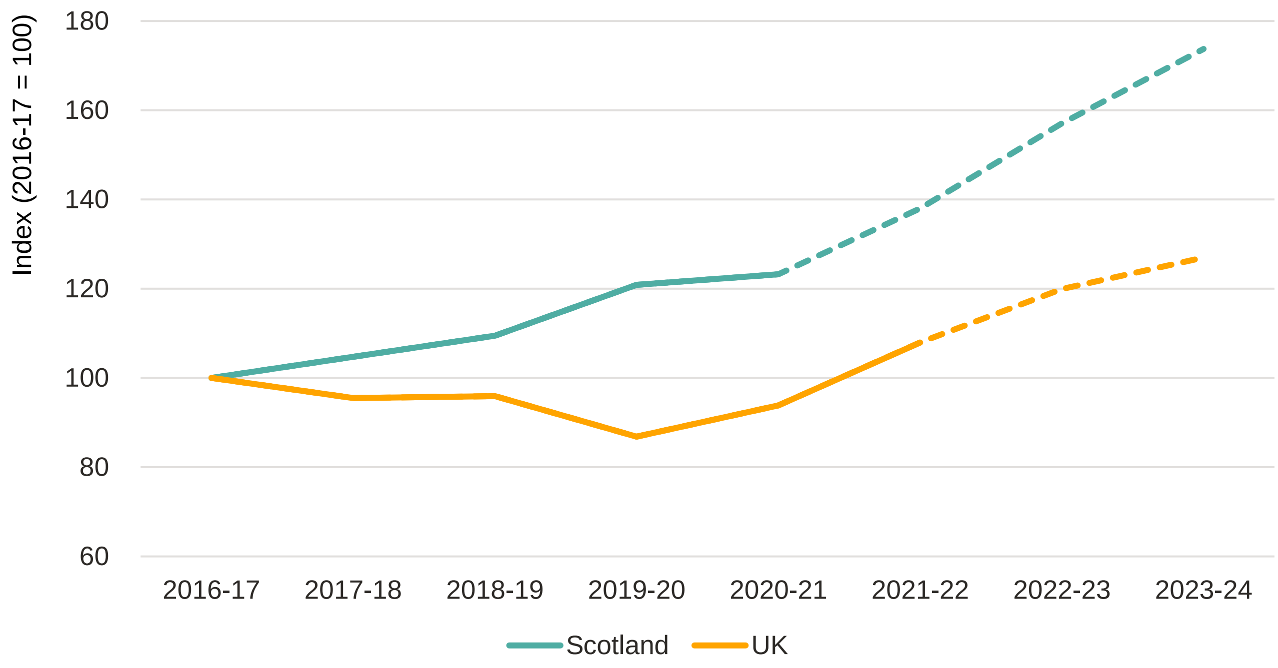
[1] Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – January 2021 (link), see paragraphs 2.8 and 2.22 to 2.26

number of higher rate taxpayers in Scotland is expected to have grown by about 74 per cent between 2016-17 and 2023-24. In 2023-24, we expect 17.8 per cent of all Scottish taxpayers to pay the higher rate of tax, compared to 11.6 per cent in 2016-17.

31 In contrast, the number of higher rate taxpayers in the UK fell between 2016-17 and 2019-20, when the higher rate threshold was being increased rapidly. With the UK higher rate threshold largely frozen since 2020-21, the number of higher rate taxpayers in the UK is gradually climbing again, though at a slower rate than in Scotland. Overall, we estimate that the number of higher rate taxpayers in the UK will have increased by around 27 per cent since 2016-17.

32 The growth in the number of higher rate taxpayers as well as the differences between Scotland and the UK are almost entirely driven by policies around the higher rate threshold and the general increase in nominal earnings driven by inflation across the whole of the UK. The more rapid growth in the number of higher rate taxpayers in Scotland is not driven by faster earnings growth or shifts in the income distribution relative to the UK.

Figure 7: Growth in higher rate income taxpayers in Scotland and UK



Source: Scottish Fiscal Commission
Solid lines show outturn available at time of publication and dashed line shows forecast. Amounts indexed so that 2016-17 is equal to 100.
The Scottish series is from the Scottish Fiscal Commission forecast and is consistent with HMRC income tax outturn data on the number of NSND income taxpayers. UK values are on a different basis, consistent with SPI data and covering all of income tax, not just the NSND element (link).
Forecast UK values are from the OBR (2023) and are for the whole of the UK, including Scotland: OBR (2023) Economic and Fiscal Outlook – March 2023 (link).

Social Security

33 We forecast that spending on social security will increase from £5.3 billion in 2023-24 to £7.8 billion in 2028-29. This increase arises because we expect the number of people receiving payments to increase. Furthermore, the average amount people receive increases overtime primarily due to most of the payments being uprated with inflation. The largest increase for the number of people receiving

payment is for Adult Disability Payment where we forecast the caseload will increase from around 420,000 in 2023-24 to 660,000 in 2028-29.[2]

Figure 8: Change in social security spending forecast since December 2022

£ million	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
December 2022	3,682	4,187	5,244	6,163	6,554	6,903	7,267	
May 2023	3,682	4,208	5,290	6,192	6,638	7,000	7,389	7,831
Change since December 2022		21	45	30	84	97	122	

Source: Scottish Fiscal Commission

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

34 Our forecast for spending in 2027-28 has increased by £122 million since December 2022. The change in the forecast mainly reflects the higher than previously expected demand for disability payments seen across the UK and the higher number of successful applications to Child Disability Payment (CDP). This increase in spending is partly offset by refinements to our Adult Disability Payment (ADP) modelling, a lower inflation forecast, adjustments to the number of carers eligible for Carer Support Payment (CSP), and a lower caseload forecast for Scottish Child Payment (SCP).

35 The increase in CDP is informed by new data received from Social Security Scotland in March 2023. These data were not available to us when we prepared our forecasts in December 2022. It shows that compared to our forecasts in December 2022 the number of applications approved has been higher and their average payment is lower. The effect from the higher number of approved applications outweighs the effect of lower payment amounts so incorporating these data increase the forecast for the number of children and young people receiving CDP by 7,000 and spending by £41 million in 2027-28.

36 The Scottish Government receives funding for devolved social security payments from the UK Government in the form of Block Grant Adjustments (BGAs). The level of BGAs is based on spending on the UK payments they replace and does not include the effect of Scottish Government reforms. The Scottish Government has also introduced new payments for which there are no UK equivalents and which are only available in Scotland. Any spending above the level of funding received from the BGAs and on new payments must be met from the overall Scottish Budget.

[2] The Adult Disability Payment figures include people receiving Personal Independence Payment.

Figure 9: Social security net position and new payments

£ million	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
Social security net position [1]	-19	-210	-369	-495	-581	-654
New social security payments [2]	-353	-546	-584	-598	-611	-620
Total	-372	-756	-953	-1,093	-1,191	-1,274

Source: Scottish Fiscal Commission.
Figures may not sum because of rounding.
[1] Social security net position includes Adult Disability Payment (covered by the Personal Independence Payment BGA), Child Disability Payment and Scottish Adult Disability Living Allowance (covered by the Disability Living Allowance BGA), Pension Age Disability Payment (covered by the Attendance Allowance BGA), Carer Support Payment and Carer's Additional Person Payment (covered by the Carer's Allowance BGA), Employment Injury Assistance (covered by the Industrial Injuries Disablement Scheme BGA), Winter Heating Payment (covered by the Cold Weather Payment BGA), Pension Age Winter Heating Payment (covered by the Winter Fuel Payment BGA) and Severe Disablement Allowance (covered by Severe Disablement Allowance BGA).
[2] New social security payments include Scottish Child Payment, Carer's Allowance Supplement, Child Winter Heating Assistance, Best Start Grant Early Learning Payment and Best Start Grant School Age Payment. We also include spending through Discretionary Housing Payments on bedroom tax mitigation and the extra costs of the new commitment to mitigating Benefit Cap deductions.

37 We estimate that by 2027-28 total spending on social security payments will be £1.3 billion more than the funding received through BGAs. While our forecast of spending has increased since December 2022, the estimate of the BGA funding for social security has increased by more, meaning that the gap between spending and BGA funding in 2027-28 has narrowed by £142 million. This narrowing of the gap only represents a small proportion of the overall social security spending. Estimates for the net position are determined by our forecasts for spending in Scotland and the OBR's forecasts for England and Wales, so changes to either forecast can lead to changes in the net position.

38 In our December 2022 forecasts, we revised up our forecast for Adult Disability Payment (ADP) to account for an increase in successful applications for working age disability payments across the UK. This was considered to be the result of multiple interlinking factors, including more people on NHS waiting lists for diagnoses and treatment, the increasing number of people economically inactive because of long-term sickness, and the financial pressures people were experiencing with the cost of living crisis. This increase in demand has strengthened for working age groups and is also now evident for child and pension age payments too. Therefore, since December 2022, we have increased the level of the effect for ADP and extended this higher demand assumption to Child Disability Payment (CDP) and Pension Age Disability Payment (PADP). As this is a UK-wide effect, the social security BGAs reflect a similar increase in the OBR's forecasts for spending on equivalent benefits in England and Wales.

39 The largest difference between spending and funding is for working age disability payments. Our forecast for expenditure on ADP is £569 million higher than the level of funding from the Personal Independence Payment (PIP) BGA in 2027-28. This difference reflects our assessment of the effect of the Scottish Government reforms introduced with ADP as it replaces PIP. These reforms include the ambition to maximise the take-up of the payment amongst those eligible and improvements to the payment delivery in terms of support available, application process, the types of supporting information used for the decision-making and appeal processes. The additional spending associated with these reforms is more uncertain than other parts of the forecast as it is based on our judgements of the scale of the overall effect. We have been refining our assumptions for ADP since

we produced our initial costing in August 2021.[3] Further adjustments will be introduced to the forecast as new data become available, however, it may take several years for the full effect of the reforms to be assessed.

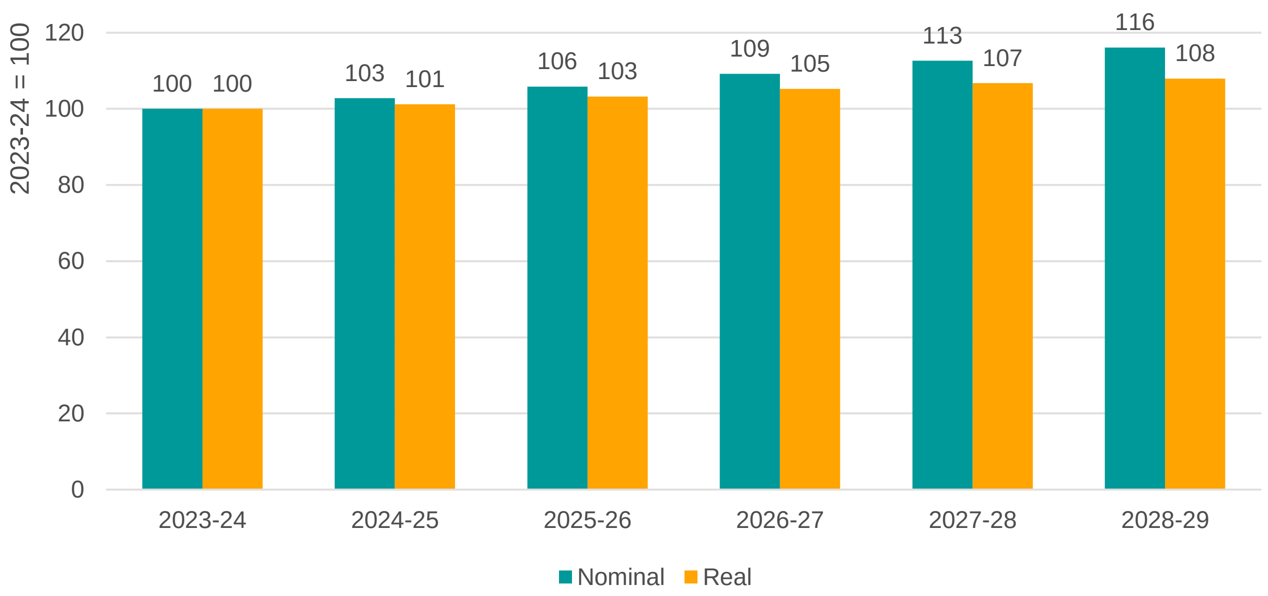
Fiscal Overview

40 The five-year funding position for the Scottish Government depends on UK Government funding, tax revenues, borrowing and reserve plans, and other funding sources. Within the funding position the Scottish Government has made assumptions about future funding from the UK Government and income from other sources. We consider the Scottish Government's resource and capital borrowing plans to be reasonable.

Resource funding

41 Total resource funding is forecast to grow from £45.3 billion in 2023-24 to £52.6 billion in 2028-29, an increase of 16 per cent in nominal terms. In real terms, after accounting for inflation, resource funding grows by 8 per cent over the same period.

Figure 10: Five-year resource funding trends



Source: Scottish Fiscal Commission, Scottish Government.
Amounts indexed so that 2023-24 is equal to 100.
Real amounts have been calculated adjusting nominal amounts by the GDP deflators published in OBR (2023) Economic and Fiscal Outlook – March 2023 (link).

42 The largest component of resource funding is the Block Grant from the UK Government. The level of the funding up to 2024-25 is based on funding set out in the UK Spending Review 2021, with updates applied to reflect changes from subsequent UK fiscal events. From 2025-26 onwards the Scottish Government anticipates that the resource funding will grow with the OBR's March 2023 forecasts of total UK Government spending.

43 Resource funding also rises as a result of improvements over the forecast horizon in the tax net position, which is the difference between Scottish tax revenues and their BGAs. The largest factor in

[3] Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – August 2021 (link).

the increasing revenue net position is the positive income tax net position, which is forecast to grow from £325 million in 2023-24 to £1,554 million in 2027-28. The income tax net position should be interpreted with caution as it is sensitive to changes in our and the OBR's forecasts – relatively small changes in either forecast can lead to substantial changes in the projected net position.

Figure 11: Summary of the Scottish Government's resource funding position

£ million	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
UK Government funding [1]	36,832	37,383	38,153	39,038	40,135	41,263
Social security BGAs	4,434	5,132	5,435	5,697	6,003	6,325
Revenue net position [2]	569	1,053	1,235	1,339	1,656	1,752
Reconciliations [3]	46	-687	88	86		
Other fiscal framework powers [4]	41	300	0	0	0	0
Other funding [5]	3,339	3,354	3,007	3,255	3,177	3,225
Total resource funding available	45,260	46,535	47,917	49,415	50,971	52,566
Social security spending	5,290	6,192	6,638	7,000	7,389	7,831
NDR Distributable Amount	3,047	3,069	3,158	3,437	3,328	3,374
Total resource funding for all other devolved spending areas	36,923	37,274	38,121	38,978	40,254	41,361

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding.
[1] UK Government funding includes the 2021 Spending Review settlement and any Barnett consequentials generated since then.
[2] Revenue net position includes tax revenues, Proceeds of Crime (POC), and Fines, Forfeitures, and Fixed Penalties (FFFPs).
[3] Reconciliations for any years other than 2023-24 are indicative and subject to change. They are based on the most recent forecasts (Scottish Fiscal Commission May 2023 for revenues, OBR March 2023 for tax and social security BGAs). Indicative reconciliations in 2024-25 are mostly for income tax relating to 2021-22 (-£712 million), but also include the remainder of 2022-23 BGA reconciliation not already adjusted in-year in Autumn 2022 (-£2 million for fully devolved taxes, +£25 million for social security, +£3 million for non-tax elements).
[4] Other fiscal framework powers consist of resource borrowing and drawdowns from resource reserve. However, there are no plans to draw down any funding from the Scotland Reserve, so the amounts shown are entirely resource borrowing plans.
[5] Other funding includes the NDR distributable amount and 'other' funding sources such as income from the Migration Surcharge. It also removes the cost of capital and resource borrowing repayments from available funding.

44 The overall outlook is for resource funding to increase in nominal and real terms over the next five years. However, after accounting for social security spending and NDR being ring-fenced to local authorities, the funding available to all other portfolios is expected to fall in real terms between 2023-24 and 2024-25.

45 If the UK Government alter departmental allocations in future UK Budgets or Spending Reviews to reduce spending in devolved areas, the Block Grant funding available for the Scottish Government will be lower than currently assumed.

46 Devolved social security spending is forecast to cost more than the funding received from the social security BGAs and social security spending is forecast to grow more quickly than the overall level of funding available to the Scottish Government. This means social security spending will account for a larger proportion of total resource spending in future years.

47 There will be pressure on the Scottish Government Budget in 2024-25 from a large negative revenue reconciliation, currently forecast to be -£687 million, primarily because of a large negative

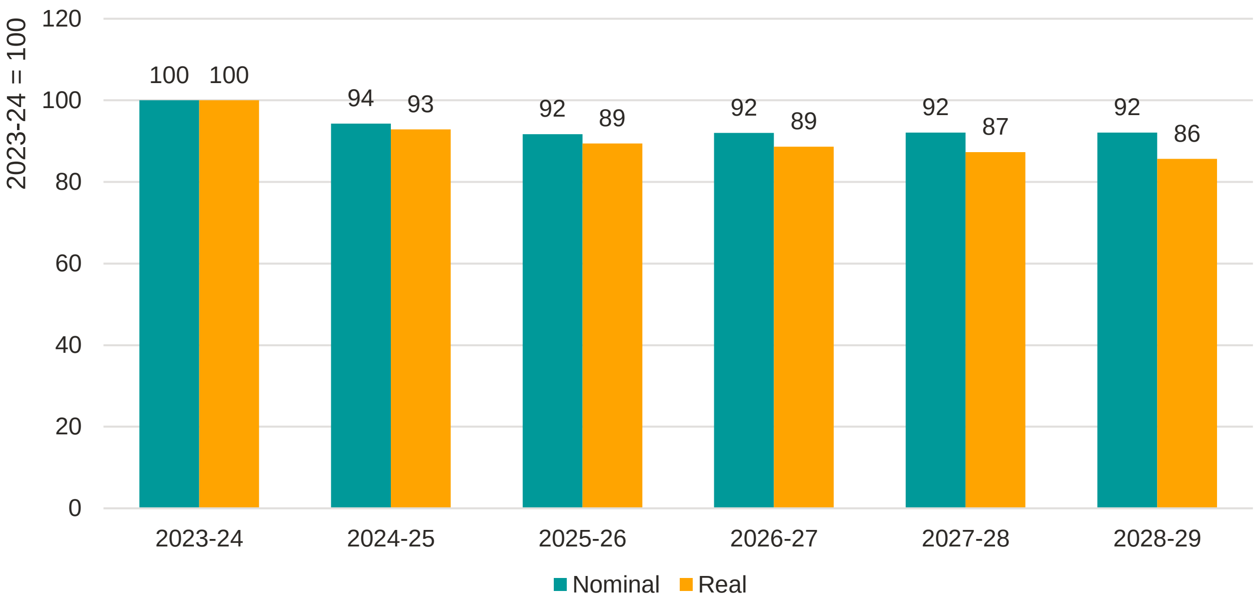
income tax reconciliation. The Scottish Government plans to use its borrowing powers in full to offset these reconciliations, but because there is a resource borrowing limit of £300 million under the fiscal framework, the remaining £387 million will need to be met from elsewhere within the Scottish Government's resource funding.

48 The Scottish Government's MTFS presents Government projections for overall resource spending, providing additional context for the consideration of the funding outlook. These projections draw upon our latest forecasts but also the Government's own assessment of the Scottish Government spending demands for areas such as health and education, which are not within our remit to forecast. Based on the Scottish Government's judgements, its projections show resource spending growing by more than funding. The Government estimates that in its central scenario spending could exceed funding by 2 per cent (£1 billion) in 2024-25 rising to 4 per cent (£1.9 billion) in 2027-28. As the Scottish Government is required to have a balanced budget, the challenge of such a gap will have to be addressed each year in the budget setting process.

Capital Funding

49 Capital funding is used to fund long-term investments such as infrastructure, hospitals, and research and development. It is projected to fall in nominal terms the first half of the forecast horizon before stabilising at 92 per cent of the current level. In real terms, the capital budget in 2028-29 is expected to be 14 per cent smaller than in 2023-24.

Figure 12: Five-year capital funding trends



Source: Scottish Fiscal Commission, Scottish Government.
Amounts indexed so that 2023-24 is equal to 100.
Real amounts have been calculated adjusting nominal amounts by the GDP deflators published in OBR (2023) Economic and Fiscal Outlook – March 2023 (link).

50 Block Grant funding from the UK Government is the largest component of capital funding. The Scottish Government expects it to fall between 2023-24 and 2024-25 before remaining at roughly the same level until 2028-29. For 2023-24 and 2024-25 this is based on the UK Spending Review 2021, updated for the UK Spring Budget 2023. From 2025-26 onwards the Scottish Government assumes it will follow the OBR's March 2023 forecasts of Public Sector Gross Investment, which is effectively zero growth.

51 The Scottish Government plans to use its borrowing powers to contribute to capital funding at a level of £250 million each year. It assumes further funding of £200 million from sources other than the Block Grant. If this other funding does not materialise in full then the Scottish Government plans to increase borrowing to meet the shortfall, so annual capital borrowing could reach up to £450 million in future years. Successive years of borrowing more than £250 million would move the total debt stock closer to the limit of £3 billion. We expect the total debt stock to meet 90 per cent of the limit in 2028-29 if £250 million is borrowed in each year of the forecast.

52 As the debt stock and annual borrowing limits have been fixed in cash terms since 2016, the ability of the Scottish Government to invest in more capital spending is constrained with inflation eroding the real value of the limits. However, increases in borrowing would lead to increased debt repayments in future years, which could place pressure on resource funding in future.

Chapter 1 Introduction

What is in this report?

1.1 In this report, published on 25 May 2023, we present our latest official five-year economic and fiscal forecasts. We create our forecasts independently, representing the collective judgements of our Commissioners. Our forecasts have been used to inform the Scottish Government's Medium-Term Financial Strategy (MTFS) 2023, which has been published on the same day. We show how our latest May 2023 forecasts have changed compared to those we published in December 2022, which informed the 2023-24 Scottish Budget.

1.2 In this introduction we explain the process we have followed in the creation of our forecasts and then how the different elements of our forecasts relate to the Scottish Government's MTFS.

1.3 The report contains the following chapters:

Summary	A summary of our economic and fiscal forecasts, the fiscal overview and the key points from this round of forecasts.
Chapter 2: Fiscal Overview	Discusses the main fiscal changes since our last forecasts. This includes UK Government funding and tax revenues. We also assess the Scottish Government's planned borrowing and use of the Scotland Reserve.
Chapter 3: Economy	Our five-year forecasts for the Scottish economy, including the underlying judgements.
Chapter 4: Tax	Our forecasts of devolved tax revenue.
Chapter 5: Social Security	Our forecast of devolved social security spending.
Annex A: Policy Costings	Our estimates of how much any new policies will cost or raise and explanations of how the Commission has arrived at those estimates.
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	Our approach to handling policies which have a very small fiscal effect.
Annex D: Fiscal Update	Our fiscal update, explaining changes to the 2022-23 and 2023-24 Scottish Budgets since December 2022.

1.4 Some additional information such as comparisons to our previous forecasts are in our supplementary figures available for download from our website.[4] If there is any information you are looking for that is not in this report or the supplementary figures, please get in touch with us at info@fiscalcommission.scot.

[4] Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – May 2023 (link).

The process behind creating these forecasts

1.5 On 1 March 2023, we received 11 weeks' notice from the then-Deputy First Minister and Cabinet Secretary for COVID Recovery of the publication of a MTFS on 25 May 2023. Throughout this period, our interaction with the Scottish Government has been guided by our Protocol for engagement.[5]

1.6 Since the formal notification, the Commission has had two rounds of meetings to discuss our forecasts. Attendees have included the Scottish Government, Revenue Scotland, and Social Security Scotland. In accordance with the Protocol, details of timings and attendees are published on our website.[6]

1.7 To finalise our forecasts for publication, our cut-off date for incorporating new data into the forecasts was 24 April 2023. The only exception was Scotland's Quarterly National Accounts data published on 26 April 2023.

1.8 Headline dates are:

1 March	Then-Deputy First Minister and Cabinet Secretary for COVID Recovery wrote to advise that the Scottish Government intended to publish its Medium-Term Financial Strategy on 25 May 2023.
24 April	Deadline for inclusion of new data in the forecasts.
26 April	Deadline for inclusion of policy measures that may affect the economy forecasts and closure of the economy forecasts.
4 May	Deadline for the Scottish Government to provide the Commission with any final policy measures and funding information to be included in the forecasts.
10 May	The Commission presented the Scottish Government with final forecasts.
19 May	The Commission's near-final report was shared with the Deputy First Minister and Cabinet Secretary for Finance, Cabinet Secretary for Social Justice, and Cabinet Secretary for Wellbeing Economy, Fair Work and Energy.
24 May	Call between Professor Graeme Roy, Chair of the Commission and the new Deputy First Minister and Cabinet Secretary for Finance.
24 May	A pre-release version of the Commission's report was shared with the Deputy First Minister and Cabinet Secretary for Finance, Cabinet Secretary for Social Justice, and Cabinet Secretary for Wellbeing Economy, Fair Work and Energy.
25 May	Scotland's Economic and Fiscal Forecasts – May 2023 published.

How the Scottish Government uses our forecasts

1.9 On 25 May 2023, the Scottish Government published the Medium-Term Financial Strategy (MTFS) 2023 which is informed, in part, by our forecast. The MTFS sets out the Scottish Government's

[5] Scottish Fiscal Commission (2022) Protocol for engagement between the Scottish Fiscal Commission and the Scottish Government (link).
[6] Scottish Fiscal Commission (2023) Scotland's Economic and Fiscal Forecasts – May 2023 (link).

five-year funding position, based on our forecasts of tax revenues, social security and assumptions about future funding and borrowing. We discuss these funding plans in **Chapter 2**. Our tax and social security forecasts are detailed in **Chapter 4** and **Chapter 5**, respectively.

Consultation on setting policy baselines

1.10 Alongside this report we are launching a consultation on how we set policy baselines.[7] An important part of our role is to estimate the effect policy changes introduced by the Scottish Government will have on tax revenues and social security spending in future years. Each time we produce a forecast we have a pre-measures forecast reflecting all previously announced policies and a post-measures forecast reflecting any new policy announcements. Our pre-measures forecast uses what we call our policy baseline, for example that tax thresholds will be held frozen or increase by inflation each year. How we set our policy baseline has a significant effect on our forecasts and also how government policy changes are framed. We recognise there are a number of approaches we could adopt to setting policy baselines, and we are keen to hear from stakeholders their views on this subject.

1.11 Full information can be found in our consultation paper. The consultation will remain open to responses until 15 September 2023.

[7] Scottish Fiscal Commission (2023) Consultation on our approach to policy baselines (link).

Chapter 2
Fiscal Overview

Overview

2.1 This chapter sets out the Scottish Government's medium-term resource and capital funding to 2028-29. We discuss updates to the funding for 2022-23 and 2023-24 Scottish Budgets in **Annex D**.

2.2 We forecast that total resource funding will grow steadily over the five-year forecast period, by 16 per cent in nominal terms between 2023-24 and 2028-29. Once we account for social security spending plans and ring-fenced Scottish local authority funding, we expect there to be less real-terms funding in 2024-25 than there is in 2023-24.

2.3 The expected decrease in real-terms funding in 2024-25 is in part because we estimate a negative reconciliation that will be larger than the Scottish Government's borrowing and Scotland Reserve funds. The Scottish Government's borrowing limits are currently fixed in cash terms and the normal resource borrowing limit is less than half of the expected negative reconciliation in 2024-25. Inflation, economic growth, as well as increasing levels of devolved revenue and spending mean that such events are likely to become increasingly common.

2.4 On capital funding, we expect the amount available to fall over the five-year horizon in nominal and real terms. In real terms, we forecast that capital funding will fall by 16 per cent between 2023-24 and 2028-29.

2.5 Under the fiscal framework it is in our legislative duty to assess the reasonableness of the Scottish Government's borrowing plans. We assess current resource and capital borrowing plans to be reasonable.

2.6 A review of the current fiscal framework is ongoing. The review will involve negotiations between the Scottish and UK Governments on changes to the current arrangements. The Scottish Government plans to conclude the review by 2026, subject to agreement with the UK Government.[8] We will comment on the implications of any changes to the fiscal framework in our future reports once they are confirmed.

Resource funding

Overall position

2.7 Figure 2.1 shows the resource funding position over the next five years. In nominal terms, total resource funding is forecast to grow from £45.3 billion in 2023-24 to £52.6 billion in 2028-29, an increase of 16 per cent.

[8] Scottish Government (2023) Equality, opportunity, community: New leadership – A fresh start (link).

Figure 2.1: Resource funding forecast

£ million		2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Block Grant funding	Barnett baseline [1]	34,942	35,577	37,438	38,323	39,420	40,548
	Barnett consequentials [2]	1,176	1,091				
	Non-Barnett funding [3]	715	715	715	715	715	715
Fiscal framework funding	Revenue net position [4]	569	1,053	1,235	1,339	1,656	1,752
	Social security BGAs [5]	4,434	5,132	5,435	5,697	6,003	6,325
	Reconciliations [6]	46	-687	88	86		
	Resource borrowing	41	300				
	Scotland Reserve drawdown	0	0	0	0	0	0
Other funding sources	Other funding [7]	508	536	165	165	165	165
	NDR distributable amount	3,047	3,069	3,158	3,437	3,328	3,374
Borrowing costs	Resource	-114	-124	-166	-174	-120	-81
	Capital	-103	-127	-150	-173	-197	-233
Total resource funding		45,260	46,535	47,917	49,415	50,971	52,566

Source: Scottish Fiscal Commission, Scottish Government.

Figures may not sum because of rounding.

Breakdowns for 2022-23 amounts, which are updated with changes since the December 2021 and May 2022 forecasts, can be found in Figure D.1 in Annex D.

[1] As set until 2024-25 in the latest UK Spending Review 2021 and estimated with the OBR's forecasts beyond then.

[2] Based on UK Spring Budget 2023 and updated for UK Main Estimates 2023-24.

[3] Based on UK Spring Budget 2023 until 2023-24 and held constant in cash terms beyond then.

[4] Revenue net position includes tax revenues, Proceeds of Crime (POC), and Fines, Forfeitures, and Fixed Penalties (FFFPs). It is based on the latest forecasts available – our May 2023 forecasts for devolved taxes, the HM Treasury estimates of the Block Grant Adjustments (BGAs) based on the OBR's March 2023 forecasts for the BGAs, and the latest forecasts from the Scottish and UK Governments of court revenues for the funding and their BGAs. However, for 2023-24, the net position for income tax is as forecast at the time of setting the Budget (December 2022, with the BGAs based on the OBR's forecasts from November 2022).

[5] Social security BGAs for 2023-24 have been updated based on the OBR's forecasts from March 2023. However, this is an indicative change. Funding levels for this year will not change until Autumn 2023 and the actual adjustment will be based on a later set of forecasts. From 2024-25 the figures include an assumed BGA for Winter Fuel Payment. The Scottish Government estimated this BGA with agreement from HM Treasury as the funding for this benefit will not be agreed until the year of devolution.

[6] Reconciliations for any years other than 2023-24 are indicative and subject to change. They are based on the most recent forecasts (Scottish Fiscal Commission May 2023 for revenues, OBR March 2023 for tax and social security BGAs). Indicative reconciliations in 2024-25 are mostly for income tax in 2021-22 (-£712 million), but also include the remainder of 2022-23 BGA reconciliation not already adjusted in-year in Autumn 2022 (-£2 million for fully devolved taxes, +£25 million for social security, +£3 million for non-tax elements).

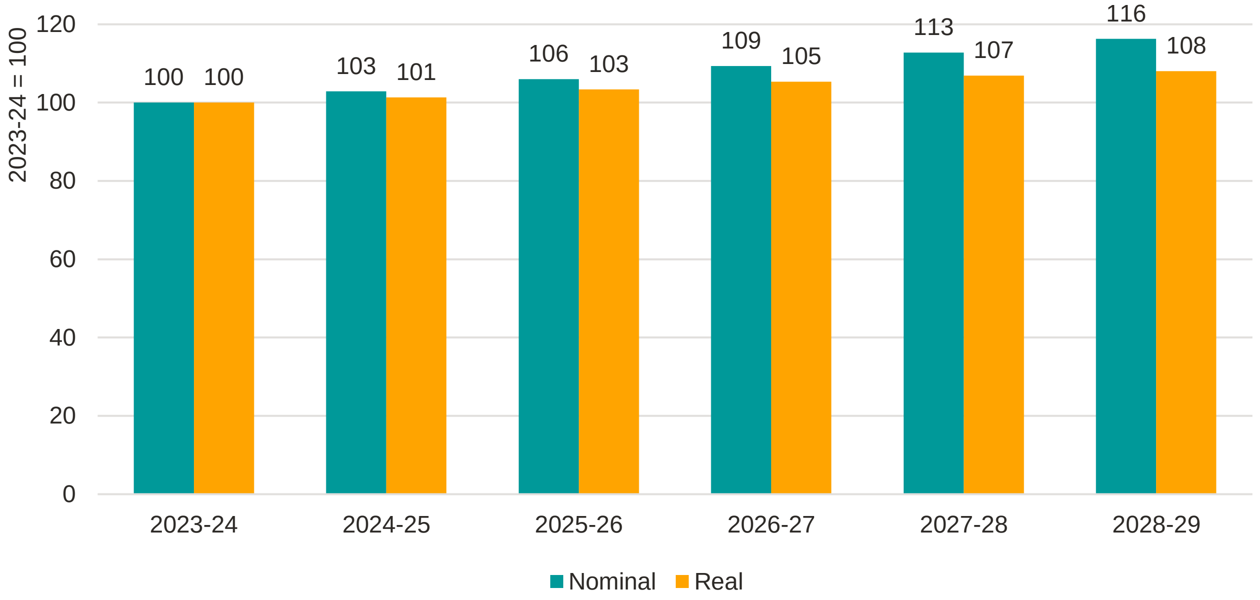
[7] The main components are ScotWind proceeds (£310 million in 2023-24, £350 million in 2024-25) and Migrant Surcharge (£160 million each year). Full details are in Figure S2.1 in the supplementary figures accompanying this publication and available on our website.

Five-year outlook

2.8 Figure 2.2 presents the outlook for total resource funding over the next five years. In nominal terms, funding is forecast to grow steadily until it is 16 per cent greater in 2028-29 than in the current financial year, 2023-24.

2.9 Real-terms funding grows by approximately 1 per cent between 2023-24 and 2024-25. Over the five-year forecast period real-terms funding growth is half of nominal funding growth. Inflationary pressures are still expected to be greater than in the recent past, but more moderate than in 2022-23.

Figure 2.2: Five-year resource funding trends



Source: Scottish Fiscal Commission, Scottish Government.
Amounts indexed so that 2023-24 is equal to 100.
Real amounts have been calculated adjusting nominal amounts by the GDP deflators published in OBR (2023) Economic and Fiscal Outlook – March 2023 (link).

2.10 Increases in Block Grant funding from the UK Government make up most of the growth in the Scottish Government's funding in future years. The OBR forecasts that UK Government spending will grow from 2025-26, beyond the plans for the current UK Government Spending Review period. We use the Scottish Government forecast of the Block Grant which anticipates that the Block Grant will grow in line with total UK Government spending.

2.11 We forecast the revenue net position will grow substantially over the forecast period, from £569 million in 2023-24 to £1,656 million in 2027-28. Figure 2.3 shows the net position for each devolved revenue. The difference between devolved revenues and their Block Grant Adjustments (BGAs) will determine the funding the Scottish Government gets from these revenues.

2.12 The total revenue net position is forecast to be positive in all years, meaning that overall revenues will be larger than the overall BGAs. The positive income tax net position is the biggest contributor to this funding. The biggest year-on-year change will come in 2024-25, when the forecast income tax net position will more than double in size. Land and Buildings Transaction Tax will have a sustained positive contribution, while Scottish Landfill Tax, Proceeds of Crime, as well as Fines, Forfeitures, and Fixed Penalties will offset part of the overall gain.

Figure 2.3: Devolved revenue net positions

£ million	2023-24	2024-25	2025-26	2026-27	2027-28
Income tax [1]	325	841	1,086	1,232	1,554
Land and Buildings Transaction Tax	254	225	179	183	183
Scottish Landfill Tax	-5	-8	-26	-71	-76
Proceeds of Crime	-4	-4	-4	-4	-4
Fines, Forfeitures, and Fixed Penalties	-1	-1	-1	-1	-1
Total revenue net position	569	1,053	1,235	1,339	1,656

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding.
Even though our forecasts cover 2028-29, the OBR have not yet produced the corresponding forecasts for the rest of the UK, which inform the Block Grant Adjustments (BGAs). We therefore show each revenue's net position until 2027-28.
[1] The income tax net position in 2023-24 is as forecast at the time of setting the 2023-24 Budget in December 2022. Fluctuations in the forecast of the income tax net position for this year will not affect funding levels until outturn data are published and a final reconciliation can be calculated, affecting funding in 2026-27 instead. Figure 4.3 shows the tax net position implied by the latest forecasts of income tax revenue and the BGA.

2.13 It is important to note that tax net positions are based on two sets of forecasts. Estimates of Scottish tax revenues are based on our forecasts. BGAs are based on the OBR's forecasts of tax revenues in England and Northern Ireland. We discuss what drives the increasing divergence between tax revenues and BGAs in Chapter 4. Small changes in either forecast can lead to substantial changes in the forecast revenue net position.

2.14 Increases in the social security BGAs are also an important driver of the expected growth in future funding. However, to see their net effect on funding, these must be considered alongside forecast spending on devolved social security payments. Figure 2.4 shows forecast social security spending on devolved benefits will exceed the BGA funding forecast to be coming from the UK Government. This does not include spending on new social security payments introduced by the Scottish Government without corresponding funding through the BGAs. Chapter 5 contains further details on what drives the increasing divergence between the forecast for devolved social security payments and their BGAs.

Figure 2.4: Net position on devolved social security payments

£ million	2023-24	2024-25	2025-26	2026-27	2027-28
Forecast BGA funding [1]	4,434	5,132	5,435	5,697	6,003
Spending forecast [2]	-4,644	-5,501	-5,930	-6,278	-6,657
Devolved social security net position	-210	-369	-495	-581	-654

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding.
[1] The Block Grant Adjustments (BGA) funding for 2023-24 shown is indicative, as it is based on the OBR's March 2023 forecasts of social security spending in England and Wales. BGA funding for this year is not adjusted until the autumn of this financial year, with the adjustment being based on a later set of forecasts.
[2] Scottish replacements of social security payments included in the net position are Adult Disability Payment, Child Disability Payment, Scottish Adult Disability Living Allowance, Pension Age Disability Payment, Carer Support Payment and Carer's Additional Person Payment, Employment Injury Assistance, Winter Heating Payment, Pension Age Winter Heating Payment, and Severe Disablement Allowance.

2.15 Non-Domestic Rates (NDR) will grow throughout the forecast period. NDR is ring-fenced to return to Scottish local authorities.[9] We show how the NDR distributable amount is set using our forecast of the contributable amount in Box 2.1.

Box 2.1: Forecast of the Non-Domestic Rating Account

NDR operates from a separate account, called the Non-Domestic Rating Account or NDR pool. NDR is ring-fenced, remaining separate from the rest of the Scottish Budget. All revenues collected are ultimately paid back to local authorities.

In Chapter 4 we forecast the contributable amount of NDR, the revenue collected by Scotland's local authorities and transferred to the Scottish Government. The Scottish Budget is set based on the distributable amount, the funding given to local authorities in each financial year. Full details on how NDR funding works can be found in our occasional paper on funding for the Scottish Budget.[10]

The distributable amount for 2023-24 was set at £3,047 million in December 2022. This will remain fixed until the 2024-25 Scottish Budget. This means that the Scottish Government does not need to manage any NDR forecast error during 2023-24. Figure 2.5 shows the Scottish Government's plans for the Non-Domestic Rating Account over our forecast period.

The Scottish Government plans to bring the account back into balance in 2024-25. The cumulative balance peaks at -£83 million at the end of 2022-23 and is then reduced to zero by 2025-26. From 2025-26 onwards, the Scottish Government plans to match the distributable amount to our forecast of the contributable amount.

Figure 2.5: Illustrative projected balance of the Non-Domestic Rating Account

£ million	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Provisional contributable amount (A)	2,829	3,046	3,133	3,158	3,437	3,328	3,374
Net effect of prior year adjustments (B)	54	19	0	0	0	0	0
Distributable amount (C)	2,766	3,047	3,069	3,158	3,437	3,328	3,374
Annual balance (D) (A + B - C)	117	18	65	0	0	0	0
Cumulative balance (E) (Previous year E + current year D)	-83	-65	0	0	0	0	0

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

Funding assumptions

2.16 In order to estimate funding levels for the five years of the forecast, the Scottish Government has made several assumptions. We summarise the assumptions here.

[9] The NDR distributable amount is included in Scottish Budgets so that the Scottish Government has legal authority to withdraw the money from the Scottish Consolidated Fund. This funding is then redistributed to Scottish local authorities and the Scottish Government cannot use these funds for any other purpose.
[10] Scottish Fiscal Commission (2021) Funding for the Scottish Budget (link).

Block Grant

2.17 Barnett funding until 2024-25 is based on the funding set out in the UK Spending Review 2021, as updated in subsequent UK fiscal events. The 2024-25 Block Grant includes consequentials for that year generated at the UK Autumn Statement 2022 and the UK Spring Budget 2023.

2.18 From 2025-26 the Scottish Government assumes it will grow in line with the OBR's March 2023 forecasts of Public Sector Current Expenditure. We assume that Barnett resource funding will grow at the same rate in 2028-29 as it does in 2027-28.

2.19 The Scottish Government assumes the enhanced UK Government spending 2024-25 in devolved areas (such as education, social care and health) will be protected, with their uplift in funding to be deemed permanent at the next Spending Review.

2.20 Non-Barnett funding is kept constant at the UK Spending Review 2021 levels. This means that it will fall in real terms over the forecast period.

Block Grant Adjustments

2.21 From 2022-23 to 2027-28, we assume the tax BGAs will grow in line with the OBR's March 2023 forecasts of devolved tax revenues in England and Northern Ireland. We assume that social security BGAs will grow in line with the OBR's forecasts of social security spending in England and Wales.

2.22 The OBR's forecasts end at 2027-28, so we make assumptions on how the BGAs will grow in 2028-29. We assume that tax BGAs grow at the same rate as our forecast of growth in each devolved tax revenue for the Scottish Government. We assume that social security BGAs will grow at the same rate between 2027-28 and 2028-29 as the forecast growth in BGAs between 2026-27 and 2027-28.

Other funding

2.23 The profiling of ScotWind proceeds is still as outlined in the Scottish Government's Resource Spending Review.[11] ScotWind proceeds are assumed to be exhausted after 2024-25.

2.24 The Scottish share of the UK Migrant Surcharge is assumed to remain constant at £160 million.

Discretionary funding

2.25 Figure 2.4 shows that we forecast the Scottish Government's spending on devolved social security payments will be greater than the social security BGA funding received from the UK Government. The Scottish Government has also introduced new social security payments, such as the Scottish Child Payment, which do not receive funding from the UK Government and are funded from the overall Scottish Budget. Figure 2.6 shows the total additional spending on social security, above BGA funding from the Scottish Budget.

[11] Scottish Government (2022) Investing in Scotland's Future: Resource Spending Review (link).

Figure 2.6: Additional spending on social security in Scotland

£ million	2023-24	2024-25	2025-26	2026-27	2027-28
Social security net position [1] [2]	-210	-369	-495	-581	-654
New social security payments [3]	-546	-584	-598	-611	-620
Total additional spending	-756	-953	-1,093	-1,191	-1,274

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding.
[1] The net position for 2023-24 is indicative, as the Block Grant Adjustment (BGA) is as calculated with the OBR's March 2023 forecasts of social security spending in England and Wales. However, BGA funding for this year is not adjusted until the autumn of this financial year, with the adjustment being based on a later set of forecasts.
[2] Scottish replacements of social security payments included in the net position are Adult Disability Payment, Child Disability Payment, Scottish Adult Disability Living Allowance, Pension Age Disability Payment, Carer Support Payment and Carer's Additional Person Payment, Employment Injury Assistance, Winter Heating Payment, Pension Age Winter Heating Payment, and Severe Disablement Allowance.
[3] New social security payments include Scottish Child Payment, Carer's Allowance Supplement, Child Winter Heating Assistance, Best Start Grant Early Learning Payment and Best Start Grant School Age Payment. We also include spending through Discretionary Housing Payments on bedroom tax mitigation and the extra costs of the new commitment to mitigating Benefit Cap deductions.

2.26 When setting each budget, the Scottish Government uses our forecasts to determine how much will be allocated to social security spending.[12] NDR can only be used to provide funding for Scotland's local authorities. In setting the spending allocations for all other devolved areas, the Scottish Government only has available the funding after allowing for forecast social security spending and the NDR distributable amount. Figure 2.7 shows these amounts. It shows more modest increases in this metric, growing by 12 per cent in nominal terms rather than the 16 per cent growth in total funding by 2028-29.

Figure 2.7: Funding available after demand-led or ring-fenced spending

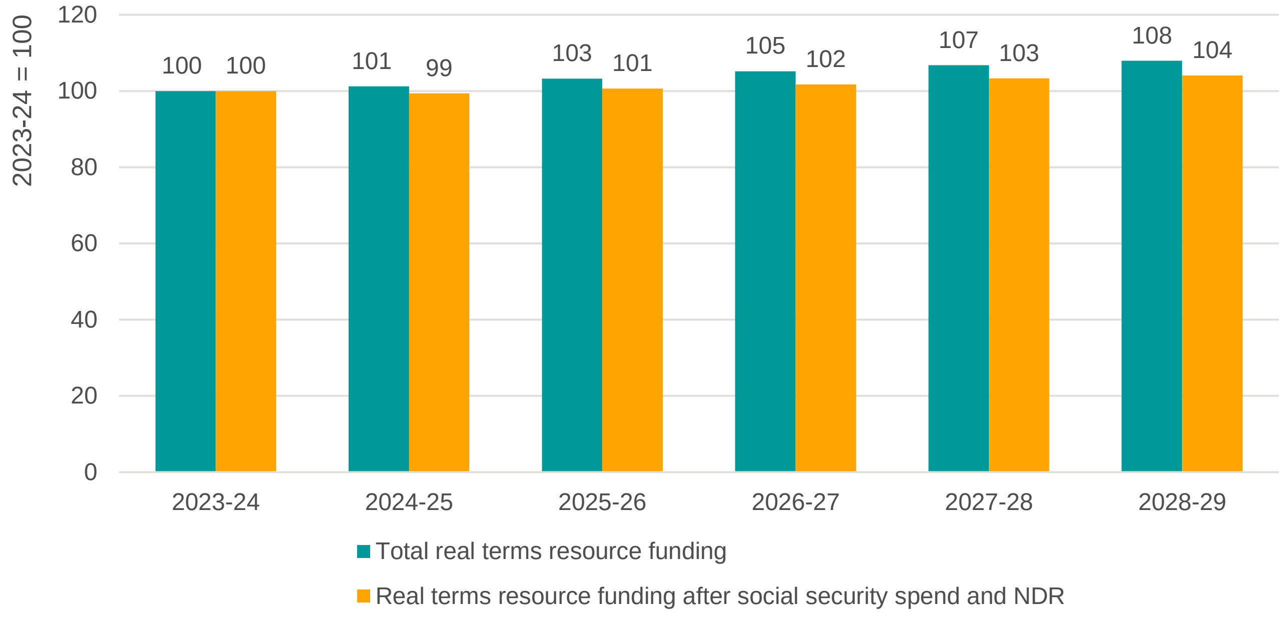
£ million	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Total resource funding available	45,260	46,535	47,917	49,415	50,971	52,566
Social security spending	5,290	6,192	6,638	7,000	7,389	7,831
NDR distributable amount [1]	3,047	3,069	3,158	3,437	3,328	3,374
Resource funding for all other devolved spending areas	36,923	37,273	38,121	38,979	40,254	41,361

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding.
[1] Non-Domestic Rates (NDR) distributable amount is as decided by the Scottish Government until 2027-28. For 2028-29 no plans have yet been made, therefore this figure is our forecast of the contributable amount for that year.

2.27 Figure 2.7 compares the real-terms outlook for total resource funding and that of real-terms funding after social security spend and NDR. We expect that the Scottish Government will in 2024-25 have slightly less resources than in 2023-24 in real terms after accounting for social security and ring-fenced NDR funding to local authorities. However, we expect this narrower definition of funding to grow in real terms from 2025-26 onwards.

[12] Scottish Fiscal Commission (2021) Funding for the Scottish Budget (link).

Figure 2.8: Trends in total resource funding and funding after social security expenditure and Non-Domestic Rates (real terms)



Source: Scottish Fiscal Commission, Scottish Government.
Real amounts have been calculated adjusting nominal amounts by the GDP deflators published in OBR (2023) Economic and Fiscal Outlook – March 2023 (link).

Resource borrowing

2.28 Under the fiscal framework, the Scottish Government's resource borrowing powers can only be used in the event of negative forecast errors.[13] The Scottish Government can borrow for any negative forecast errors in each year, normally up to a maximum borrowing of £300 million.[14] Resource borrowing is subject to a total cap of £1,750 million. These limits have been fixed in cash terms since 2017-18.

2.29 Figure 2.9 shows current resource borrowing plans. The resource debt stock reaches a maximum of 34 per cent of the debt cap in 2024-25. It then falls in future years as we do not currently anticipate negative reconciliations or forecast errors after 2024-25.

[13] The Scottish Government can borrow for negative forecast errors involving negative reconciliations, higher devolved social security spending than forecast, or devolved lower tax revenues than forecast. These can be caused by forecast errors by the SFC or the OBR. For more information see UK Government (2016) The agreement between the Scottish government and the United Kingdom government on the Scottish government's fiscal framework (link).
[14] In the event of a Scotland Specific Economic Shock, the Scottish Government can borrow up to £600 million for negative forecast errors. For more information, see UK Government (2016) The agreement between the Scottish government and the United Kingdom government on the Scottish government's fiscal framework (link).

Figure 2.9: Resource borrowing plans

£ million	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Borrowing	41	300				
Repayment period (years)	5	5				
Interest rate (per cent)	3.9	3.8				
Repayments	-108	-117	-150	-160	-110	-75
Debt stock	414	596	446	286	175	101
Share of debt cap (per cent)	24	34	25	16	10	6

Source: Scottish Fiscal Commission, Scottish Government.

2.30 Figure 2.10 shows the latest forecasts of reconciliations applied to each year of the Scottish Government's funding. Income tax reconciliations occur three years after the Budget where the funding is originally set, because outturn data become available 16 months after the end of the tax year. For social security and fully devolved taxes, there is a final reconciliation of the BGAs upon publication of outturn data applied two years after the relevant Budget.[15]

Figure 2.10: Final and indicative reconciliations

£ million	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
Total reconciliations	-207	-319	-15	46	-687	88	86
Income tax	-204	-309	-34	50	-712	88	86
LBTT and SLfT (BGAs only) [1]	-5	-8	-6	-35	-2		
Social security (BGAs only) [1]	0	-3	22	30	25		
Non-tax revenues (BGAs only)	2	2	4	0	3		
Reconciliation relates to financial year:							
Income tax	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24
All others	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding. Shaded cells refer to outturn at the time of publication.
The reconciliation applying to 2023-24 is not shaded as there are outstanding matters with regard to the 2021-22 social security Block Grant Adjustments (BGAs).
[1] Although the OBR's March 2023 forecasts already point to some forecast error on the BGAs used to set the 2023-24 Budget, we assume that most of it will be corrected with the in-year adjustment to the 2023-24 funding levels. This adjustment will be based on a later set of OBR forecasts (Autumn 2023). We do not make assumptions about the final reconciliation, which will be applied to the 2025-26 Scottish Budget.

2.31 We currently estimate a total reconciliation of -£687 million to apply to the 2024-25 Budget. This is largely because of the income tax negative reconciliation of -£712 million.

[15] The BGAs will have already been adjusted once in-year, based on the OBR autumn forecast. The reconciliation is on the final forecast error.

2.32 The largest reconciliations happen because of forecast error in the income tax net position. Because income tax revenue and the associated BGA are so large, even small forecast errors can lead to large reconciliations. We will not know the actual income tax net position for 2021-22 until outturn data are published later this year. When we know this, the final reconciliation will apply to the 2024-25 Scottish Budget.

2.33 Current estimates of the reconciliation are based on updated income tax forecasts published since January 2021. Although our forecast of Scottish income tax revenues in 2021-22 has increased since January 2021, the forecast of the BGA has increased more due to the OBR's greater upward revisions of non-savings, non-dividend (NSND) income tax revenues in England and Northern Ireland. We show the changes to the income tax net position in Figure 4.4 in **Chapter 4**.

2.34 The Scottish Government plans to use its borrowing powers in full to offset these reconciliations. However, the reconciliations will exceed the £300 million limit to the resource borrowing under the current fiscal framework. The remaining £387 million will need to be met from the Scottish Government's resource funding.

2.35 As Figure 2.10 shows, we expect reconciliations greater than the normal resource borrowing limit to have taken place in two of the first five years since the current fiscal framework was implemented.[16] In January 2021 we estimated that income tax reconciliations could exceed the normal £300 million borrowing limit between one and four times in each decade.[17]

Scotland Reserve

2.36 The Scotland Reserve is an instrument available to the Scottish Government to transfer funding between financial years. Its total balance is capped at £700 million. The Scotland Reserve has separate accounts for resource, capital, and financial transactions, even though no limits for the components are specified. Drawdowns for resource funding are normally limited to £250 million a year.

2.37 As Figure 2.11 shows, the Scottish Government fully used the Scotland Reserve in 2021-22. It had a closing balance of £700 million and all funds were then used in 2022-23 to support spending.[18] The planned drawdown from the reserve was already known at the time of setting the 2023-24 Budget in December 2022. Therefore, the 2023-24 Budget was set with no assumed drawdowns from the resource reserve. There has been no update to that position at the time of the May 2023 Medium-Term Financial Strategy (MTFS).

[16] In January 2021 we forecast a Scotland-specific economic shock (SSES) in 2021-22, which meant that Scottish Government could borrow up to £600 million to meet reconciliations in 2021-22, 2022-23 and 2023-24. We do not forecast a SSES in this report and expect resource borrowing in 2024-25 to be limited to a maximum of £300 million.

[17] Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – January 2021 (link)

[18] Our January 2021 forecast of a SSES in 2021-22 meant that the drawdown limits of the Scotland Reserve did not apply in 2021-22, 2022-23 and 2023-24.

Figure 2.11: Use of the Scotland Reserve

£ million	2021-22	2022-23	2023-24
Resource			
Opening balance	405	605	0
Drawdowns	-405	-605	0
Additions	605		
Closing balance	605	0	
Capital (excluding financial transactions)			
Opening balance	7	81	0
Drawdowns	-7	-81	0
Additions	81		
Closing balance	81	0	
Financial transactions			
Opening balance	197	14	50
Drawdowns	-197	-14	-50
Additions [1]	14	50	
Closing balance	14	50	
Total closing balance	700	50	0

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding. Shaded cells refer to outturn at the time of publication.
[1] Additions to the Scotland Reserve in 2022-23 depend on the finalisation of the accounts for this year. This has not yet happened, so the addition to the financial transactions account is an estimation.

Resource Assessment

2.38 On the surface, the outlook is one of increasing resource funding even after accounting for inflation. The growth is driven mostly by assumed increases in the Block Grant and supported by an increasingly positive tax net position, as well as more social security BGA funding.

2.39 Regarding Block Grant assumptions, it is not guaranteed that the uplifts to UK Government departments in devolved areas in Autumn 2022 and Spring 2023 Budgets will be permanent. The UK Government may alter departmental allocations in future UK Budgets or Spending Reviews. If these changes reduce spending in devolved areas, the Scottish Block Grant will be smaller than we have set out here.

2.40 The Scottish Government has pointed to the recent commitments the UK Government has made to spend more in devolved areas, with policies such as the universal expansion of early childcare.[19] This means that future departmental allocations could involve more spending in devolved areas than previously expected. Therefore, we find that growing the 2024-25 Barnett Block Grant as it currently stands in line with the OBR's forecasts of spending is reasonable.

[19] UK Government (2023) Spring Budget 2023 (link).

2.41 However, even if the Block Grant is to grow as assumed, devolved social security spending is forecast to cost more than the funding from BGAs. The devolved social security negative net position is forecast to grow in absolute value over time.

2.42 Once we account for our forecast of social security spending and that NDR revenue is ring-fenced for local authorities, we forecast that resource funding available for other portfolios will fall in 2024-25 in real terms. A contributing factor to this is the large negative income tax reconciliation in that year, which is greater than the fiscal framework borrowing limits. This implies a temporary reduction in funding.

2.43 The Scottish Government's MTFS presents Government projections for overall resource spending, providing additional context for the consideration of the funding outlook. These projections draw upon our latest forecasts but also the Government's own assessment of the Scottish Government spending demands for areas such as health and education, which are not within our remit to forecast. Based on the Scottish Government's judgements, its projections show resource spending growing by more than funding. The Government estimates that in its central scenario spending could exceed funding by 2 per cent (£1 billion) in 2024-25 rising to 4 per cent (£1.9 billion) in 2027-28. As the Scottish Government is required to have a balanced budget, the challenge of such a gap will have to be addressed each year in the budget setting process.

2.44 In future years, Scottish funding sources may provide flexibility to deal with a challenging outlook. For example, it is unlikely that ScotWind proceeds are one-off. The first batch of proceeds has been fully profiled, but once the wind farms are developed, the Scottish Government may expect a regular income from the operation of these leases.

2.45 Overall, we find the resource borrowing plans to be reasonable.

Capital funding

Overall position

2.46 Figure 2.12 shows the capital funding position over the next five years.[20] Budgets for direct capital investment are forecast to be broadly flat at around £5.9 billion throughout the forecast period. The total capital budget, including financial transactions, will fall from £6.4 billion in 2023-24 to £5.9 billion in 2028-29, a decrease of 8 per cent.[21]

[20] The Scottish Government can use resource funding for capital spending. This would increase the funding shown in Figure 2.12 available for capital spending but reduce the resource funding shown in Figure 2.1.

[21] FTs are a ring-fenced part of the Scottish Block Grant only available to lend to or buy equity in the private sector to deliver capital projects that are aligned with policy goals. Because the OBR do not forecast FTs at the UK level, the Scottish Government assumes that spending on FTs will be zero beyond the period included in the 2021 UK Government Spending Review.

Figure 2.12: Capital funding forecast

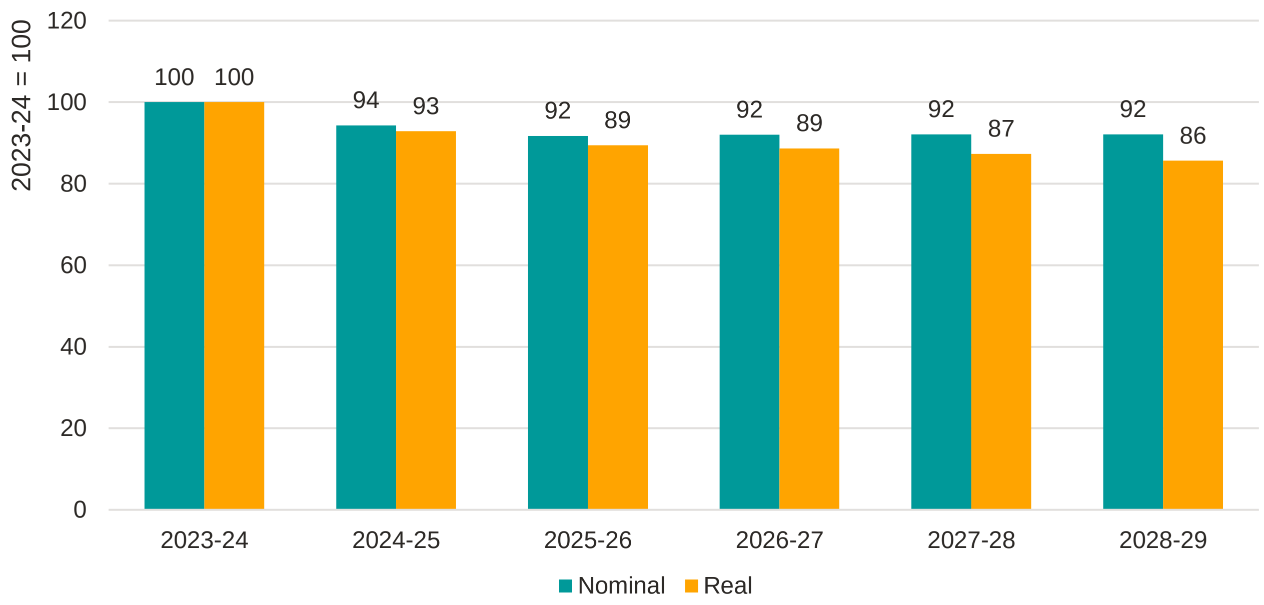
£ million		2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Capital (excluding financial transactions)							
Block Grant funding	Barnett baseline [1]	4,757	4,690	4,700	4,720	4,727	4,727
	Barnett consequentials [2]	63	1				
	Non-Barnett funding [3]	632	632	632	632	632	632
Fiscal framework funding	Capital borrowing	250	250	250	250	250	250
	Scotland Reserve drawdown	0	0	0	0	0	0
Other funding sources	Other funding [4]	302	300	300	300	300	300
Total capital funding (excluding financial transactions)		6,004	5,872	5,882	5,902	5,909	5,909
Financial transactions							
Block Grant funding	Barnett baseline	186	176				
	Barnett consequentials [2]	-14					
Fiscal framework funding	Scotland Reserve drawdown	50					
Other funding sources	Other funding [5]	188					
Total financial transactions		410	176				
Total capital funding		6,414	6,048	5,882	5,902	5,909	5,909

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding.
Breakdowns for 2022-23 amounts, which are updated taking into account changes since the December 2021 and May 2022 forecasts, can be found in Figure D.2 in Annex D.
[1] As set until 2024-25 in the latest UK Spending Review 2021 and estimated with the OBR's forecasts beyond then.
[2] Based on UK Spring Budget 2023 and updated for UK Main Estimates 2023-24.
[3] Based on UK Spring Budget 2023 until 2024-25 and held constant in cash terms beyond then.
[4] Includes £100 million of assumed capital City Deals and a further £200 million of assumed capital funding from other sources which, if not forthcoming, can be borrowed.
[5] Relates to compensation from HM Treasury for a historical error in how financial transactions had been allocated. An amount for 2024-25 has not yet been agreed.

Five-year outlook

2.47 Figure 2.13 shows the trend of the funding position outlined in the Figure 2.12 and its real-terms value once we account for inflation. Total capital funding is expected to fall in the first half of the forecast horizon, because funding for financial transactions is assumed to be zero beyond 2024-25. Capital funding will then stabilise at 92 per cent of the 2023-24 level. In real terms, we expect that the capital budget in 2028-29 will be 14 per cent smaller than in the current financial year.

Figure 2.13: Five-year capital funding trends



Source: Scottish Fiscal Commission, Scottish Government.
Amounts indexed so that 2023-24 is equal to 100.
Real amounts have been calculated adjusting nominal amounts by the GDP deflators published in OBR (2023) Economic and Fiscal Outlook – March 2023 (link).

Funding assumptions

2.48 In order to forecast capital funding levels for next five years, the Scottish Government has made several assumptions. We assess their reasonableness in the Capital Assessment section.

Block grant

2.49 Barnett funding until 2024-25 is based on the UK Spending Review 2021, updated for the UK Spring Budget 2023. From 2025-26 the Scottish Government assumes it will follow the OBR's March 2023 forecasts of Public Sector Gross Investment, which is effectively zero growth. We assume that this trend will continue to apply in 2028-29.

2.50 Non-Barnett funding is assumed to remain at the UK Spending Review levels until 2027-28. We assume it will remain flat in 2028-29.

Other funding

2.51 The Scottish Government assumes there will be £100 million of recurrent capital City Deals. It also assumes £200 million will be generated from other sources, such as unanticipated capital Barnett consequentials or Scotland Reserve drawdowns. If any of these £200 million do not emerge, capital borrowing can be increased to address the shortfall, adjusting loan durations so as to remain within fiscal framework limits, while also being mindful of the cost to future resource budgets.

Capital borrowing

2.52 Under the current fiscal framework, the Scottish Government has powers to borrow to support capital investment. It can borrow up to £450 million a year, with an overall limit to the debt stock of £3,000 million. These limits have been fixed in cash terms since 2017-18. Following the 2022-23 borrowing decisions, the debt stock currently stands at £2,026 million, or 68 per cent of the limit.

2.53 Figure 2.14 shows the Scottish Government's plans for capital borrowing through our forecast horizon. Under current plans, the capital debt stock will increase from 73 per cent of the debt cap in 2023-24 to 90 per cent in 2028-29. We discuss the outlook for the capital debt stock beyond our five-year forecast in Box 2.1.

Figure 2.14: Capital borrowing plans

£ million, unless specified	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Borrowing	250	250	250	250	250	250
Repayment period (years)	15	15	15	15	15	15
Interest rate (per cent)	3.9	3.9	4.0	4.0	4.1	4.2
Repayments	-99	-115	-129	-143	-159	-174
Debt stock	2,177	2,312	2,433	2,540	2,631	2,707
Share of debt cap (per cent)	73	77	81	85	88	90

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

2.54 As shown in Figure 2.14, the Scottish Government plans to set future capital budgets with £250 million of capital borrowing repayable in 15 years. However, this plan can be revisited if some of the other assumed funding does not materialise.

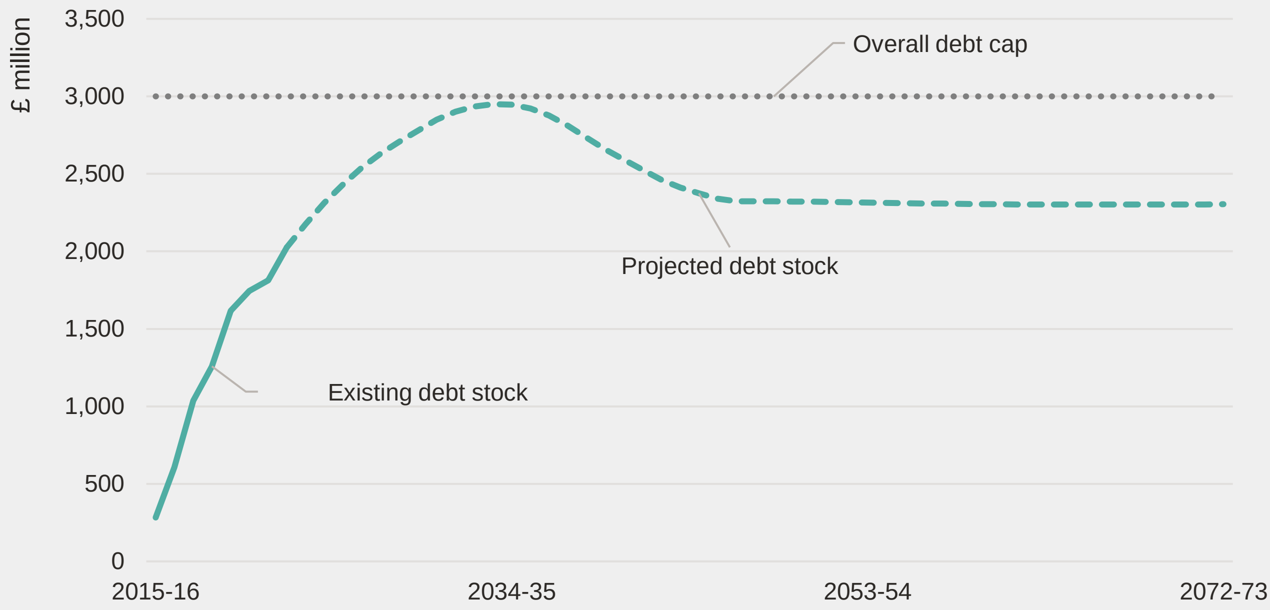
2.55 As Box 2.2 shows, if projected further into the future, current borrowing plans would take the debt stock close to the overall debt cap in the 2030s. If the Scottish Government decides to take on extra capital borrowing in any one year, there is a risk that future borrowing power will be restricted.

Box 2.2: Capital borrowing long-run outlook

Figure 2.14 sets out the Scottish Government's borrowing plans to 2028-29. Currently, the Scottish Government plans to borrow £250 million each year of the forecast, repayable within 15 years.

In Figure 2.15 we project that central scenario over the next 50 years. We use long-term expectations of interest rates from financial markets in the first few decades and then align with the OBR's assumptions that long-term interest rates will converge with nominal UK GDP growth plus 0.2 percentage points.

Figure 2.15: Long-term projection of capital borrowing



Source: Scottish Fiscal Commission, Scottish Government.
The detailed projection of capital borrowing can be found in Figure S2.2 in the supplementary figures accompanying this publication and available on our website.

Since loans taken out to date tend to have long repayment durations, our projection suggests that the debt stock would build progressively until the early 2030s, when it would peak just below the overall debt limit under the fiscal framework. From then on, as older loans expire and new loans bring the average repayment duration down, the debt stock would start to fall and by 2046-47 it would stabilise at around 77 per cent of the cap, when all loans in the portfolio are repayable within 15 years.

The central projection is feasible under the current fiscal framework limits. However, if less capital funding than forecast arrives in any one year, the Scottish Government will risk hitting the total debt cap in the 2030s. This would mean that funding through debt in that decade may be less available than current plans and the current borrowing policy would not be sustainable.

Capital Assessment

2.56 The five-year capital funding outlook is challenging. The Scottish Government expects the Block Grant to fall for the remainder of the UK Spending Review period and be flat from then on. Inflationary pressures will erode that stable but lower level of funding.

2.57 The Scottish Government does not plan to allocate any resource funding to the capital budgets. It intends to use borrowing powers to contribute to capital funding. However, the debt taken out so far means that there is little scope for the Government to borrow a large enough amount to make a difference to capital funding.

2.58 Under the current fiscal framework, the feasibility of the borrowing plans relies on an assumed £200 million of capital funding every year. For example, if borrowing increased by £60 million in the next two years to plug a partial gap in that assumption, the overall debt limit would be reached in the 2030s. The Scottish Government would then have to reduce its central borrowing plans and so would be less able to support future capital budgets. Conversely, if the Scottish Government managed to find more than £200 million of other capital funding in any one year and it reduced its central borrowing plans accordingly, this would safeguard additional borrowing capacity for the future.

2.59 The £200 million annually of assumed funding should be risk-assessed and reviewed each year. We will monitor how these emerge each year and how the Scottish Government's capital borrowing plans change in future. Overall, we conclude that the Scottish Government's current capital borrowing plans for the five years covered by our report are reasonable.

Chapter 3
Economy

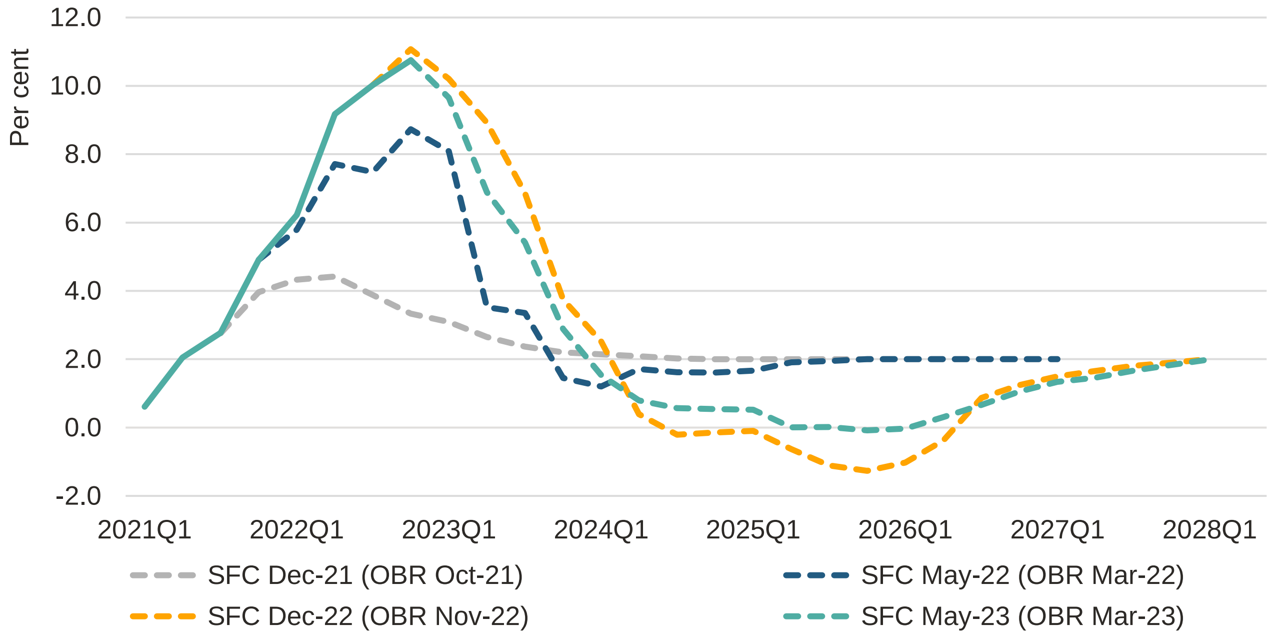
Forecast summary

3.1 The overall outlook for the Scottish economy is largely unchanged since our December 2022 forecasts, with slow and fragile economic growth over the short term. In line with the latest GDP data which have been mildly above expectations, we now forecast the economy to remain broadly flat this year rather than fall into a shallow recession.

3.2 Comparing to our December 2022 forecasts, energy prices have fallen back more quickly than expected, leading to slightly lower expectations for inflation and interest rates in the near term. This contributes to the marginally improved forecast for short-run GDP. Living standards, however, are still likely to fall this year because the overall rate of inflation – now reflecting a broader range of price rises than just energy – will continue to outpace growth in nominal household disposable incomes. In addition, Scottish Government and UK Government policy changes to freeze tax thresholds and increase tax rates will have increased average tax bills for taxpayers, further reducing disposable income. As we outlined in December, this means the coming years will continue to be difficult for many households, especially those with lower incomes.

3.3 Annual CPI inflation has come down from its peak of around 11 per cent in 2022 Q4 and is still expected to drop sharply over the course of this year, broadly on track with predictions from December.

Figure 3.1: Consumer Price Index inflation, year-on-year growth



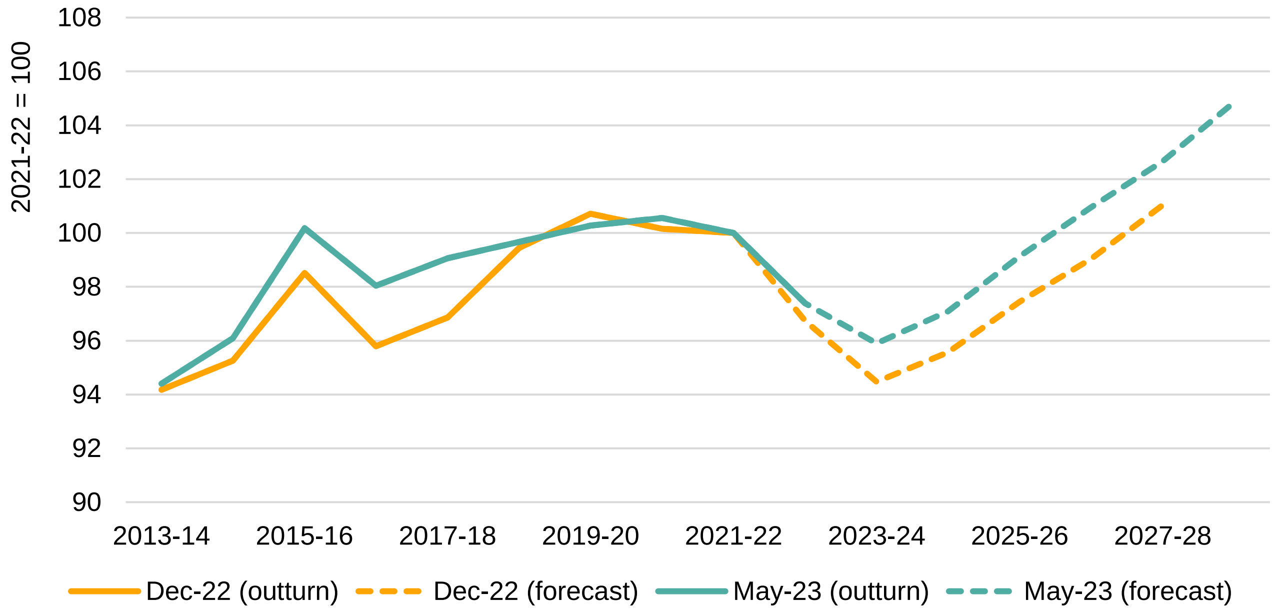
Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link), Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – May 2022 (link), Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – December 2021 (link), OBR (2023) Economic and fiscal outlook – March 2023 (link), OBR (2022) Economic and fiscal outlook – November 2022 (link), OBR (2022) Economic and fiscal outlook – March 2022 (link), OBR (2021) Economic and fiscal outlook – October 2021 (link).
Solid lines refer to outturn available at time of publication and dashed lines refer to forecasts.

3.4 Below the headline rate, we continue to see some variation in inflation among different items. Energy prices are expected to stabilise at current levels or fall further. This means energy price inflation, comparing today's prices to last year's very high levels, is on track to drop substantially. In contrast, food price inflation has been accelerating and is currently almost 20 per cent.

3.5 As in our December 2022 forecast, Scottish households are still expected to see the biggest fall in living standards – as measured by real disposable income per person – since Scottish records began in 1998, of 4.1 per cent between 2021-22 and 2023-24. This fall is slightly shallower than we forecast in December, reflecting the lower expectations for inflation and interest rates. Even once inflation returns to lower levels and real disposable incomes start to grow again in 2024-25, living standards will take time to recover to the 2021-22 level. Our forecast suggests that, by 2025-26, real disposable income per person will be no higher than a decade earlier. The energy price shock has prolonged a period of slow growth in living standards since the 2008-09 Global Financial Crisis, with real disposable income per person growing on average by only 0.6 per cent per year between 2008-09 and 2021-22 compared to 2.5 per cent per year before 2008-09.

3.6 Higher living costs affect everyone, but there are particular pressures on lower-income households, as they spend a larger share of income on essentials such as energy and food. Higher interest rates add to the costs of mortgages and other forms of debt for some households. However, Scotland has lower average house prices and lower average household debt as a share of income than the UK as a whole, so higher interest rates will tend to have a smaller effect in Scotland.

Figure 3.2: Real disposable income per person, 2021-22 equals 100



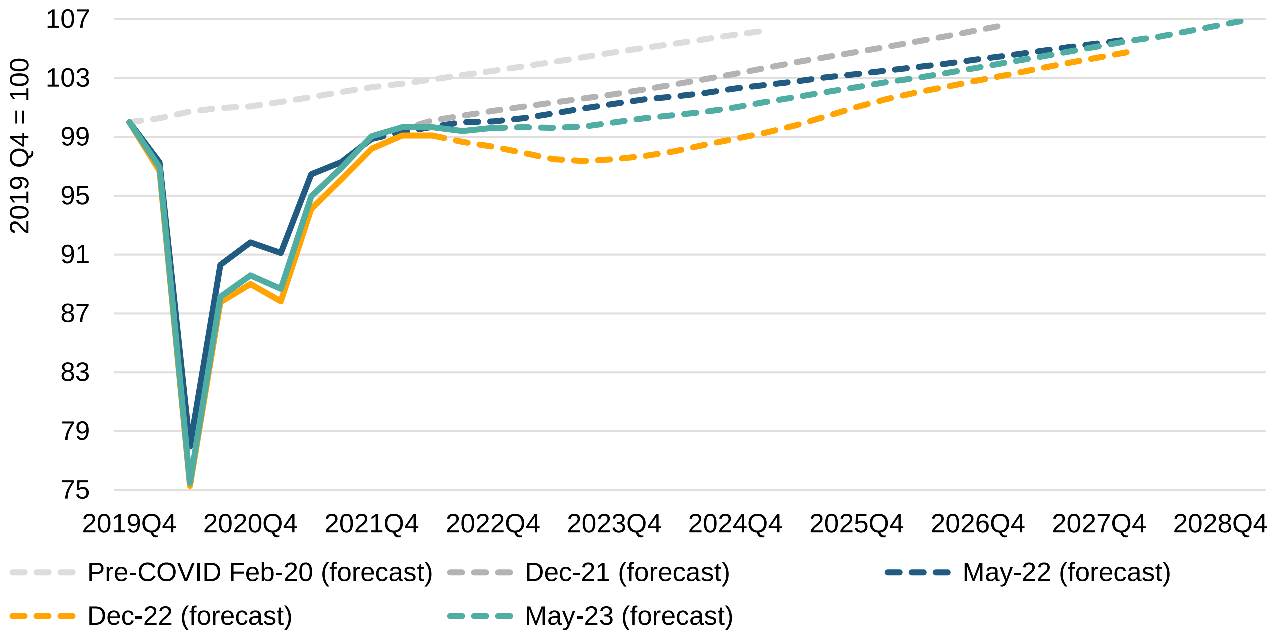
Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link).
Solid lines refer to outturn available at time of publication and dashed lines refer to forecasts. Amounts indexed so that 2021-22 is equal to 100.

3.7 Over the short term, our December 2022 forecast suggested a relatively shallow recession, as economic conditions had weakened significantly following the energy price shock in early 2022. Based on the latest GDP statistics, the performance of the Scottish and UK economies over the last few months has been mildly above expectations, with both economies avoiding recession last year and remaining relatively flat in early 2023-24. This has also been the case for other major global economies including the US, the EU, and China. Domestically, factors such as government energy support and the additional savings accumulated during the pandemic have likely dampened the impact of inflation by more than we had accounted for in our previous forecast. The labour market was also stronger than predicted and both consumer and business sentiment strengthened into the start of this year with the improved outlook for energy prices.

3.8 As emphasised in our December 2022 report, when looking at GDP, we consider that the level of GDP in Scotland over the longer term is more important than the specific path for growth over the short term. Although we are no longer forecasting a technical recession, the overall environment remains one of slow and fragile economic growth. Even if a recession was to occur later in the year, or emerge in future revised data, we do not expect the underlying economic picture to be meaningfully different from that in this report.

3.9 It is also important to see the current period of economic stagnation in the context of a prolonged period of slow economic growth. As we highlighted in December, this slow growth in Scotland is in line with globally slowing productivity growth as well as the result of the 2008-09 Global Financial Crisis and the more recent shocks. Sustained lower levels of GDP, relative to what we would have expected to be the case without these shocks, will mean ongoing lower incomes and will put pressure on tax receipts and public spending in the longer term.

Figure 3.3: Scottish GDP, 2019 Q4 equals 100



Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link), Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – May 2022 (link), Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – December 2021 (link), Scottish Fiscal Commission (2020) Scotland's Economic and Fiscal Forecasts – February 2020 (link).
Solid lines refer to outturn available at time of publication and dashed lines refer to forecasts. Amounts indexed so that 2019 Q4 is equal to 100.

3.10 As we noted in recent reports, the uncertainty around our economy forecasts has been greater than usual and, generally, this is also true this time around. The main source of uncertainty continues to be inflation, particularly its 'core' component which excludes energy and food. A wage-price spiral, which would keep inflation and interest rates higher for longer, also remains a risk.

3.11 Figure 3.4 shows further detail on our latest economy forecast and compares it to our December 2022 forecast.

Figure 3.4: Headline economy forecasts, growth rates unless otherwise specified

Per cent	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
GDP							
December 2022	1.7	-1.0	1.2	2.1	1.9	1.5	
May 2023	2.0	0.3	1.0	1.3	1.3	1.4	1.4
Consumer Price Index							
December 2022	10.1	5.5	0.0	-1.0	0.8	1.8	
May 2023	10.0	4.1	0.6	0.0	0.8	1.7	2.0
Average nominal earnings							
December 2022	4.4	4.1	2.5	2.1	2.7	3.2	
May 2023	4.0	4.6	2.6	2.3	2.6	2.9	3.0
Average real earnings							
December 2022	-4.4	-0.8	2.2	2.7	1.7	1.3	
May 2023	-3.8	0.9	1.8	2.1	1.5	1.1	0.9
Employment							
December 2022	1.7	-0.5	-0.2	0.3	0.5	0.4	
May 2023	2.0	0.3	0.0	0.3	0.3	0.3	0.3
Unemployment rate							
December 2022	3.4	4.3	4.7	4.6	4.3	4.1	
May 2023	3.3	3.8	4.1	4.1	4.1	4.1	4.1

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link).
Shaded cells refer to outturn available at time of publication. Nominal earnings are adjusted for inflation using the Consumer Expenditure Deflator.

3.12 We continue to monitor our Scottish Uncertainty Index, published for the first time in our August 2021 report.[22] The updated indicator, up to April 2023, can be found in the economy supplementary figures accompanying this report. It shows a decrease in uncertainty since the start of this year but remains relatively elevated. Overall, the level of uncertainty is comparable with that of the UK as a whole.

3.13 To finalise our forecasts for publication, our cut-off date for incorporating new data and information into the forecasts was 24 April 2023.[23]

Forecast comparisons

3.14 Figure 3.5 shows how our May 2023 forecast of GDP growth in calendar years compares to a range of other forecasts for Scotland and the UK.

[22] Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – August 2021 (link)
[23] The only exception was Scotland's Quarterly National Accounts data published on 26 April 2023.

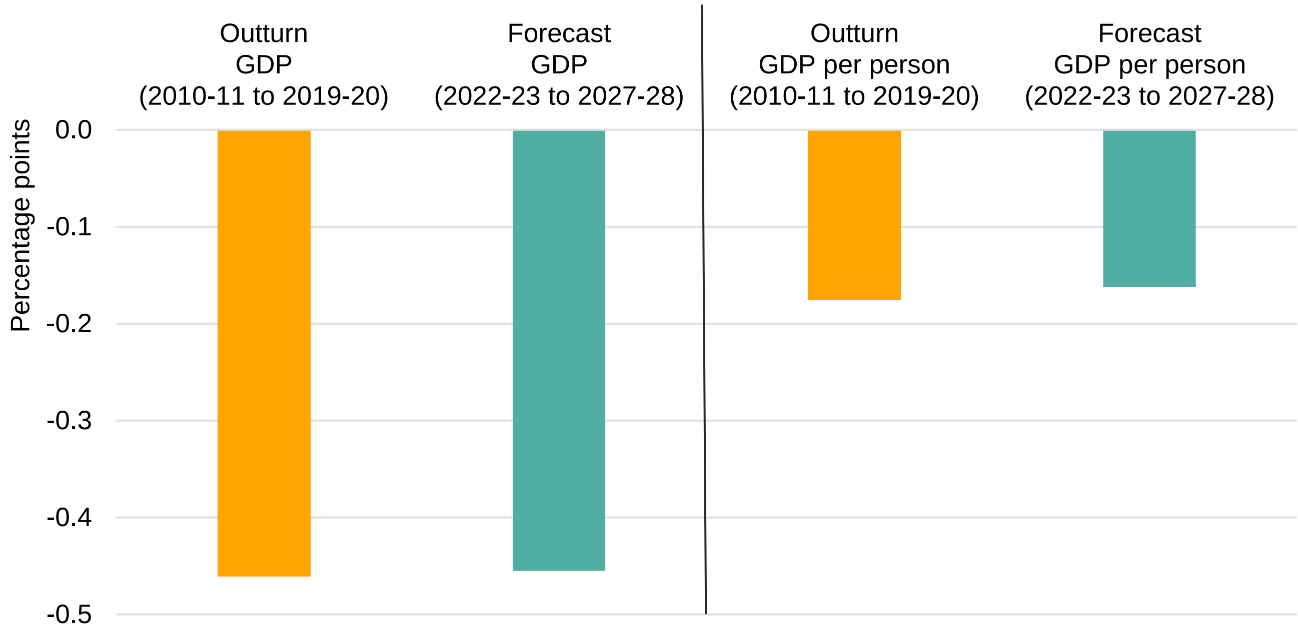
Figure 3.5: Forecast comparison, GDP growth rates in calendar years

Per cent	2022	2023	2024	2025	2026	2027	2028
Scotland: SFC May 2023	4.9	0.2	0.9	1.3	1.3	1.4	1.4
Scotland: FAI March 2023	4.9	-0.7	0.9	1.7			
UK: OBR March 2023	4.1	-0.2	1.8	2.5	2.1	1.9	
UK: NIESR May 2023	4.1	0.3	0.6	1.1	1.0	1.3	
UK: BoE May 2023	4.1	0.25	0.75	0.75			
UK: HMT average of forecasters May 2023	4.1	0.2	1.0				

Source: Scottish Fiscal Commission, Fraser of Allander Institute (2023) FAI Economic Commentary 2023 Q1 (link), OBR (2023) Economic and fiscal outlook – March 2023 (link), NIESR (2023) UK Economic Outlook – May 2023 (link), Bank of England (2023) Monetary Policy Report – May 2023 (link), HM Treasury (2023) Forecasts for the UK economy: May 2023 (link).

3.15 Compared to the OBR's forecasts for the UK, we forecast annual GDP growth in Scotland to be around 0.5 percentage points lower on average from 2022-23 to 2027-28. This divergence exists mainly because of slower population growth, with the gap reducing to 0.2 percentage points on a 'GDP per person' basis. Figure 3.6 shows these gaps in forecast growth rates are in line with historical outturn data over the last decade. The remaining divergence on a 'per person' basis exists mostly because of differences in our and the OBR's trajectories for the output gap and, therefore, for GDP growth.

Figure 3.6: Average annual gap in GDP growth between Scotland and UK, 2022-23 to 2027-28



Source: Scottish Fiscal Commission, OBR (2023) Economic and fiscal outlook – March 2023 (link).
Orange bar refers to outturn available at time of publication and teal bars refer to forecasts.

3.16 To allow comparisons of our headline GDP forecasts in financial and calendar year terms, Figures 3.7 and 3.8 show our latest and previous forecasts of GDP growth on both annual bases.

Figure 3.7: SFC latest and previous forecasts, GDP growth rates in financial years

Per cent	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
December 2022	1.7	-1.0	1.2	2.1	1.9	1.5	
May 2023	2.0	0.3	1.0	1.3	1.3	1.4	1.4

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link).
Shaded cells refer to outturn available at time of publication.

Figure 3.8: SFC latest and previous forecasts, GDP growth rates in calendar years

Per cent	2022	2023	2024	2025	2026	2027	2028
December 2022	5.0	-1.2	0.7	1.9	2.1	1.6	
May 2023	4.9	0.2	0.9	1.3	1.3	1.4	1.4

Source: Scottish Fiscal Commission, Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link).
Shaded cells refer to outturn available at time of publication.

Main judgements

Figure 3.9: Economy forecast main judgements

Issue	December 2022	May 2023
1. Spare capacity, or output gap	Output gap of around -2 per cent of trend GDP emerging in 2023-24, as GDP falls below trend following the recession, before gradually returning to zero.	Output gap of 0.3 per cent of trend GDP in 2023-24, closing at the end of the forecast.
2. Trend productivity	Growth of 0.1 per cent in 2022-23 and 0.5 per cent in 2023-24, increasing to 1.1 per cent in 2027-28 broadly in line with the OBR's November 2022 assumption.	Growth of 0.1 per cent in 2022-23 and 0.5 per cent in 2023-24, increasing to 1.2 per cent in 2028-29 broadly in line with the OBR's March 2023 assumption.
3. Long-run unemployment rate	4.1 per cent over the forecast period.	4.1 per cent over the forecast period.
4. Nominal average annual earnings	Growth of 4.4 per cent in 2022-23 and 4.1 per cent in 2023-24, reducing to 3.2 per cent in 2027-28.	Growth of 4.0 per cent in 2022-23 and 4.6 per cent in 2023-24, moderating to 3.0 per cent in 2028-29.
5. Population projections	Scottish population aged 16 to 64 peaks at mid-2023, then shrinks throughout the forecast.	Scottish population aged 16 to 64 peaks at mid-2023, then shrinks throughout the forecast.
	Net international migration of 19,000 in 2020-21 (outturn), 30,000 in 2021-22, and 29,000 in 2022-23. For 2023-24 onwards, revised up to the ONS interim 2020 based principal scenario of around 10,000 annually, in line with the OBR's November 2022 assumption.	Net international migration of 19,000 in 2020-21 (outturn), and 21,000 in 2021-22 and 2022-23. For 2023-24 onwards, revised up to the ONS January 2023 projection of 13,000 annually, in line with the OBR's March 2023 assumption.
6. Forecasts of the UK	Based on the OBR's UK November 2022 forecast.	Based on the OBR's UK March 2023 forecast.
7. Oil and gas	Neutral impact of UK Continental Shelf activity on onshore economy.	Neutral impact of UK Continental Shelf activity on onshore economy.
8. Savings ratio	Savings ratio in 2023-24 falling to its long-run average and remaining broadly stable at that level over the forecast.	Savings ratio falling over 2022-23 and 2023-24, before gradually rising towards its long-run average.
9. Second round effects	No material effect of any Scottish Government policy changes on economic growth.	No material effect of any Scottish Government policy changes on economic growth.

Source: Scottish Fiscal Commission

GDP and expenditure components

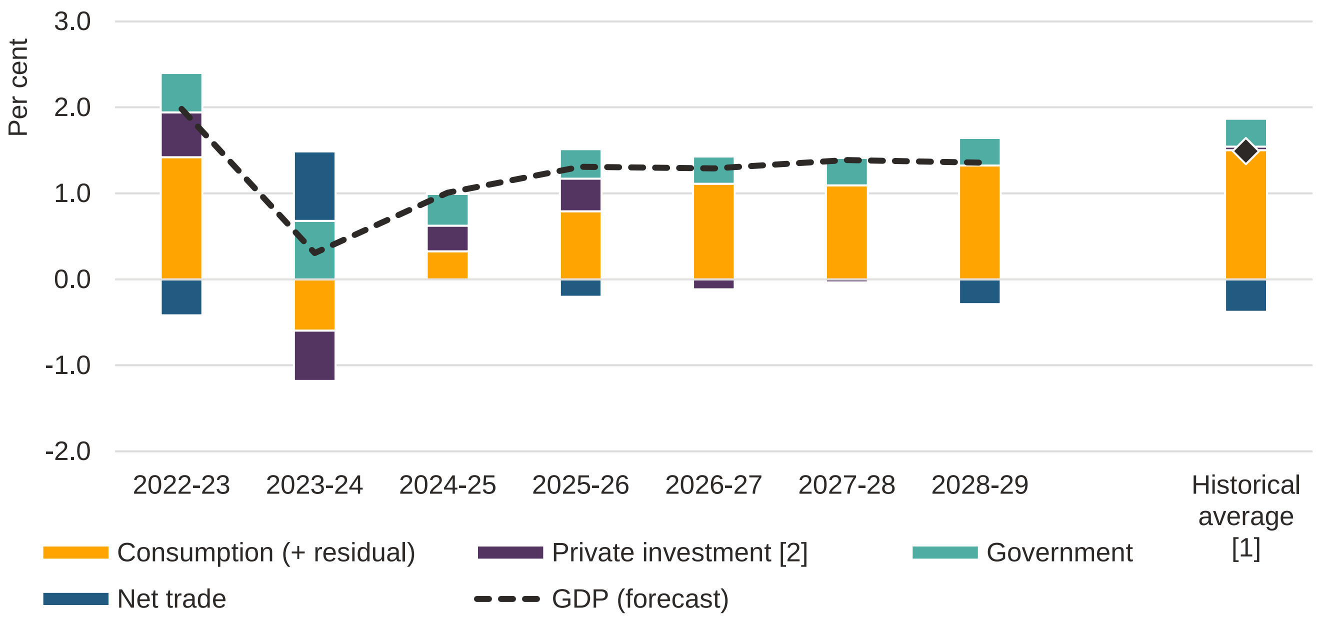
3.17 Higher costs of living and doing business continue to weigh on demand, with GDP expected to remain broadly flat over 2023-24. We forecast GDP growth of 0.3 per cent in 2023-24, picking up to 1.0 per cent in 2024-25 and 1.3 per cent on average from 2025-26 onwards.

3.18 We expect the decline in real disposable incomes will lead to a fall in household expenditure in 2023-24. Consumption is forecast to increase from 2024-25 onwards as living standards gradually recover. The savings ratio has fallen from its pandemic highs over 2022-23 and we expect it to fall further this year, supporting consumption and GDP.

3.19 The pattern of business investment growth reflects the effect of the temporary 100 per cent capital allowance (or ‘full expensing’) measure in place from 2023-24 to 2025-26, as announced in the UK Spring Budget 2023. Despite this, business investment is likely to detract from GDP growth as the weak economic outlook and higher cost of capital weigh on investment decisions in 2023-24. In 2024-25 and 2025-26, we forecast business investment will boost GDP growth as the ‘full expensing’ measure provides an incentive to bring forward planned investment from future years.

3.20 Government expenditure supports the economy throughout the period from 2023-24 to 2028-29, while the contribution of net trade to GDP is broadly neutral on average over the forecast.

Figure 3.10: Contributions to growth in GDP by component of expenditure



Source: Scottish Fiscal Commission, Scottish Government (2023) GDP Quarterly National Accounts: 2022 Quarter 4 (October to December) (link).
[1] Historical average is based on growth from 1999-00 to 2019-20.
[2] Private investment includes business and housing investment.

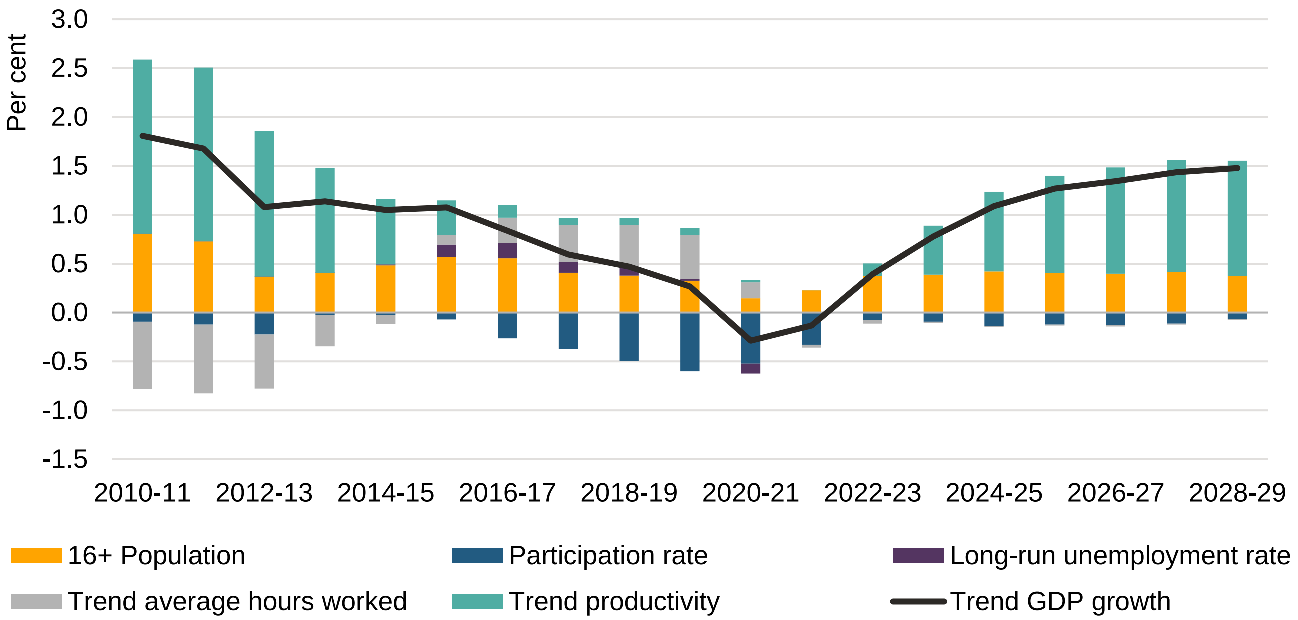
Long-run outlook

2.60 Trend GDP, or potential output, is the estimated amount of goods and services the economy can sustainably produce without inducing excess price inflation in the economy. In the short term, actual output can deviate from potential output, but over the longer term the economy is assumed to be subject to the supply constraint of potential output.

3.21 Trend GDP is based on: the capacity of the economy to supply and efficiently allocate the labour force; the average number of hours worked; and advances in technology, working practices, and human and physical capital that drive trend productivity growth.

3.22 Scotland's trend GDP growth rate has been slowing since the 2008-09 Global Financial Crisis, averaging 1.0 per cent between 2010-11 and 2019-20 compared to 2.0 per cent between 1999-00 and 2009-10. This has been driven by falling productivity growth, slowing population growth, and a declining participation rate. We expect productivity growth to pick up, in line with the expected path at UK level and to be the main driver of trend GDP growth over the medium to long term. Trend GDP growth rises over the forecast period from 0.8 per cent in 2023-24 to 1.5 per cent in 2028-29.

Figure 3.11: Trend GDP growth and contribution of components, 2010-11 to 2028-29



Source: Scottish Fiscal Commission

Figure 3.12: Trend GDP growth and contribution of components, 2023-24 to 2028-29

Year (growth in per cent)	Trend GDP growth	16+ population	16+ participation rate	Long-run unemployment rate	Trend average hours worked	Trend productivity
2023-24	0.8	0.4	-0.1	0.0	0.0	0.5
2024-25	1.1	0.4	-0.1	0.0	0.0	0.8
2025-26	1.3	0.4	-0.1	0.0	0.0	1.0
2026-27	1.3	0.4	-0.1	0.0	0.0	1.1
2027-28	1.4	0.4	-0.1	0.0	0.0	1.1
2028-29	1.5	0.4	-0.1	0.0	0.0	1.2
Average	1.2	0.4	-0.1	0.0	0.0	1.0

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

Trend GDP growth components

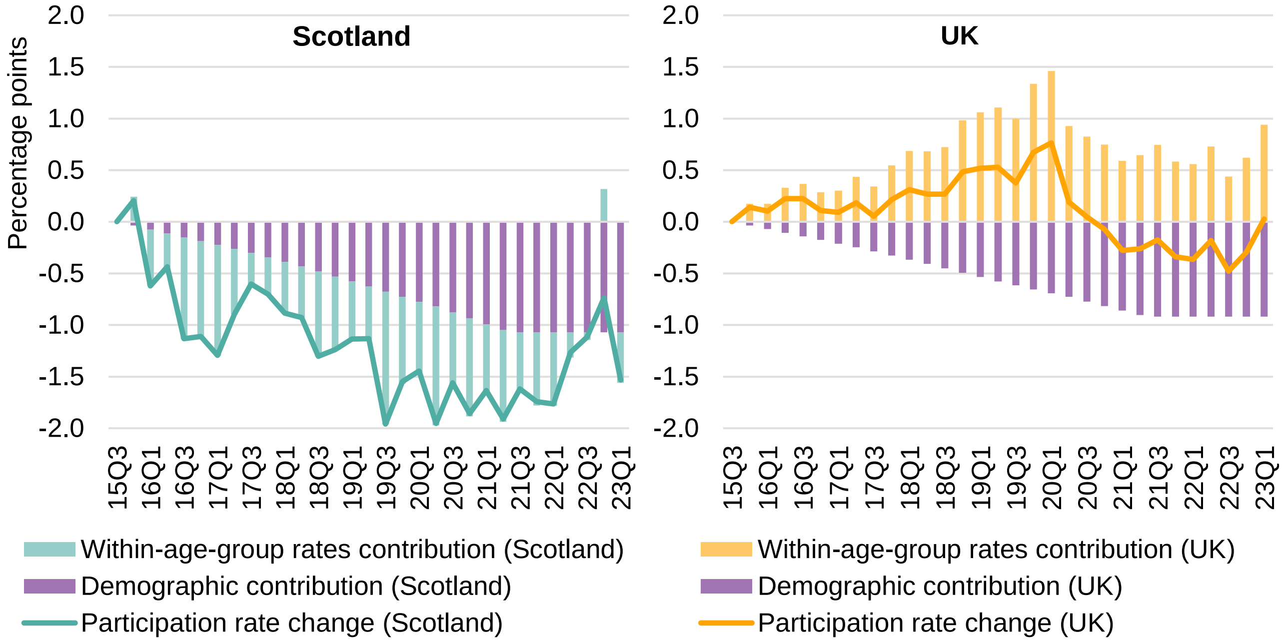
The labour force participation rate

3.23 The labour force is the pool of people aged 16 and over who are in work or actively looking for work. These people are defined as economically active. Those aged 16 and over who are not in the labour force are defined as economically inactive. They could be studying, retired, looking after family, or sick. The labour force participation rate is the percentage of the population aged 16 and over who are economically active.

3.24 Over the five-year horizon, our participation rate projection has the same declining trend as we forecast in December (driven by demographic pressure) but from a higher starting point.[24] Since December, we have made an upward adjustment to the starting point of our projection after reviewing the available participation data for Scotland which show diverging post-pandemic trends. This is discussed further in Box 3.1.

3.25 An ageing population in Scotland and the UK is putting downward pressure on the overall labour force participation rate, as older age groups tend to have lower participation rates. We can disaggregate changes in the participation rate into the effect of changing demographics compared to the effect of varying participation rates within individual age groups. This disaggregation is shown in Figure 3.13 and the demographic contribution is similar for both Scotland and the UK.

Figure 3.13: Contributions to change in historical participation rates since 2015 Q3



Source: Scottish Fiscal Commission, ONS (2023) HI11 Regional labour market: headline indicators for Scotland (link), ONS (2023) A01: Summary of labour market statistics (link).
The starting point for this analysis is 2015 Q3 because this is the quarter after which the Scottish and UK age 16 and over participation rates started to diverge. The 2023 Q1 data point is one month of data for the reporting period December to February 2023.

3.26 At the UK level, upward pressure from within-age-group participation rates, shown as the rates contribution in Figure 3.13, has offset the demographic effect so that the overall UK participation rate has been relatively stable since 2015. In contrast, Scotland's within-age-group participation rates

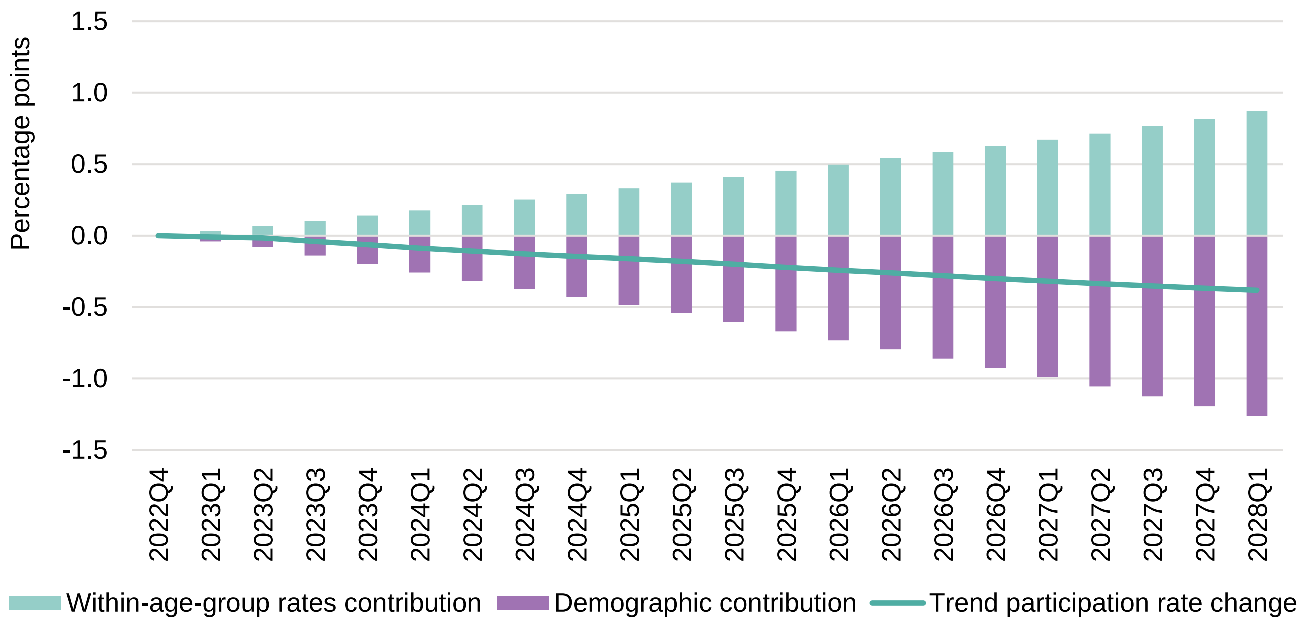
[24] As part of our overall assessment of Scotland's participation rate, we have considered the labour market policies announced in the UK Spring Budget 2023 which apply to Scotland. These are the measures relating to pensions and disability and are relatively small measures. The largest of the announced policies, relating to childcare, does not apply to Scotland.

have put downward pressure on the participation rate, with the overall Scottish participation rate declining relative to 2015.[25] Therefore, to understand why the participation rate in Scotland has been falling compared to the UK, we need to understand why participation rates within individual age groups have performed differently.

3.27 Scottish and UK participation rates have been diverging across most age groups between 2015 and 2022. Those aged 25 to 34 and 35 to 49 are among the age groups with the largest divergence since 2015. These are among the largest segments of the working population and have the highest participation rates. The next section looks at some of the reasons why economic inactivity has changed within individual age groups, with a focus on the post-pandemic period and on ill-health.

3.28 Over the forecast period, on average, we forecast growing within-age-group participation rates, partly reflecting the 2026-28 State Pension age rise. However, demographic change continues to put downward pressure on the participation rate, resulting in our forecast for the trend participation rate declining slightly.

Figure 3.14: Drivers of Scotland's trend participation rate forecast



Source: Scottish Fiscal Commission

Box 3.1: Labour force participation data for Scotland

The Labour Force Survey (LFS) is the source of all headline and disaggregated UK labour force participation estimates. Scotland has both a Scottish portion of the UK LFS as well as the Annual Population Survey (APS) which is a boosted sample of the Scottish portion of the LFS, allowing for more reliable disaggregated analysis. The headline LFS and the APS should show similar trends. However, these two series have diverged in recent years, especially since the start of the COVID-19 pandemic.

This seems to be a particular issue for Scottish data while there is less evidence of such a large and persistent divergence for other regions of the UK. It is unclear why this is the case. It is hoped this will be resolved in the more robust transformed LFS.[26]

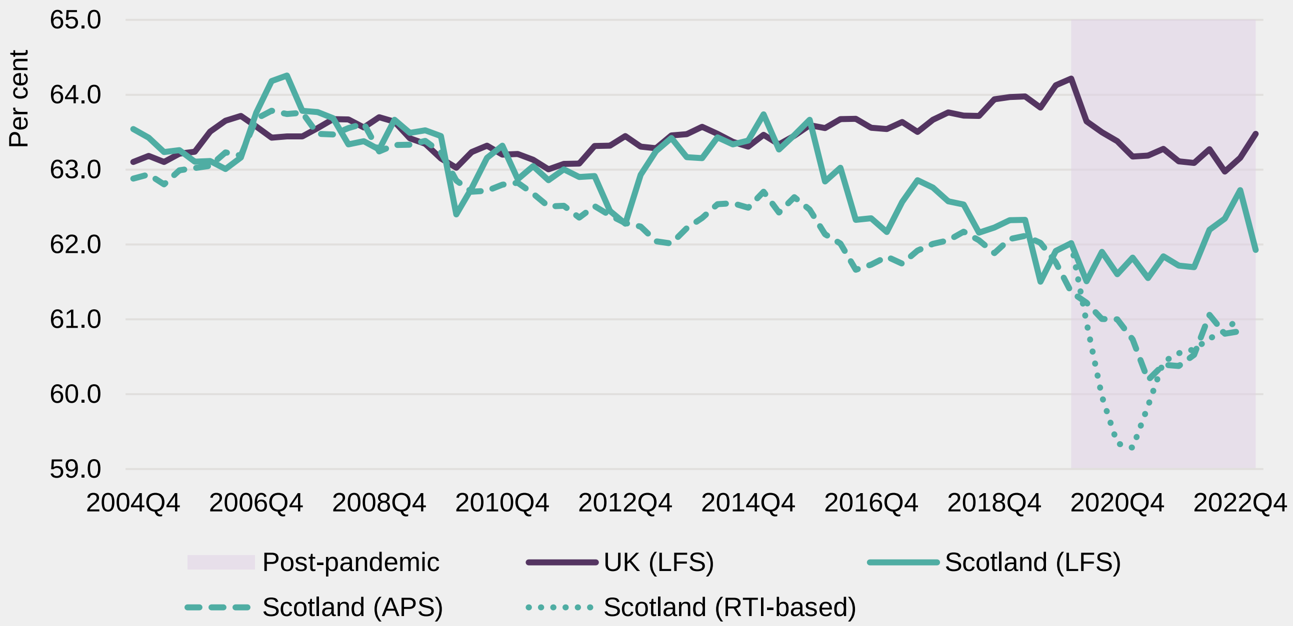
[25] Scottish Fiscal Commission (2022) Trends in Scotland's population and effects on the economy and income tax (link).
[26] ONS (2023) Labour market transformation – update on progress and plans: May 2023 (link).

Confidence intervals around headline LFS participation rates for Scotland and the UK indicate the degree of uncertainty associated with these estimates. Confidence intervals are higher for Scotland because of the smaller sample size. The 95 per cent confidence intervals for the 16 to 64 age group participation rate estimates in January 2023 were 0.5 percentage points for the UK and 2.0 percentage points for Scotland.[27] This means that Scotland's participation rate could be higher or lower than pre-pandemic levels, making it difficult to compare the relative performance of Scotland's and the UK's labour force.

The UK's LFS participation rate has dropped since the pandemic whereas Scotland's LFS participation rate has remained more stable. On the other hand, according to the APS, Scotland's participation rate has dropped by a similar amount to the UK. This drop in labour force participation in Scotland is also supported by Real Time Information (RTI) data, which count employees from Pay As You Earn (PAYE) tax data. Given the intrinsic uncertainty in the measurement of Scotland's labour force, the divergence between the LFS and APS is an added complication.

We are engaging with Scottish Government and Office for National Statistics (ONS) colleagues to understand this more and we will cover this issue in our next Statement of Data Needs.

Figure 3.15: Age 16 and over labour force participation rates



Source: Scottish Fiscal Commission, ONS (2023) HI11 Regional labour market: headline indicators for Scotland (link), ONS (2023) A01: Summary of labour market statistics (link), ONS (2023) Earnings and employment from Pay As You Earn Real Time Information, seasonally adjusted (link).
Scotland's RTI-based labour force participation rate is (RTI-based employment + LFS unemployment)/LFS population.
In this Figure, we broadly match annual APS data to quarterly LFS data for the purpose of showing the respective trends, not to make a direct comparison.

Post-pandemic labour force performance

3.29 There has been much commentary for both Scotland and the UK on: rising inactivity for 50-64-year-olds since the pandemic; and rising ill-health as the main self-reported reason for inactivity across the population aged 16 to 64. In this sub-section, we take a detailed look at these recent trends for Scotland. The analysis broadly supports our view on the participation rate.

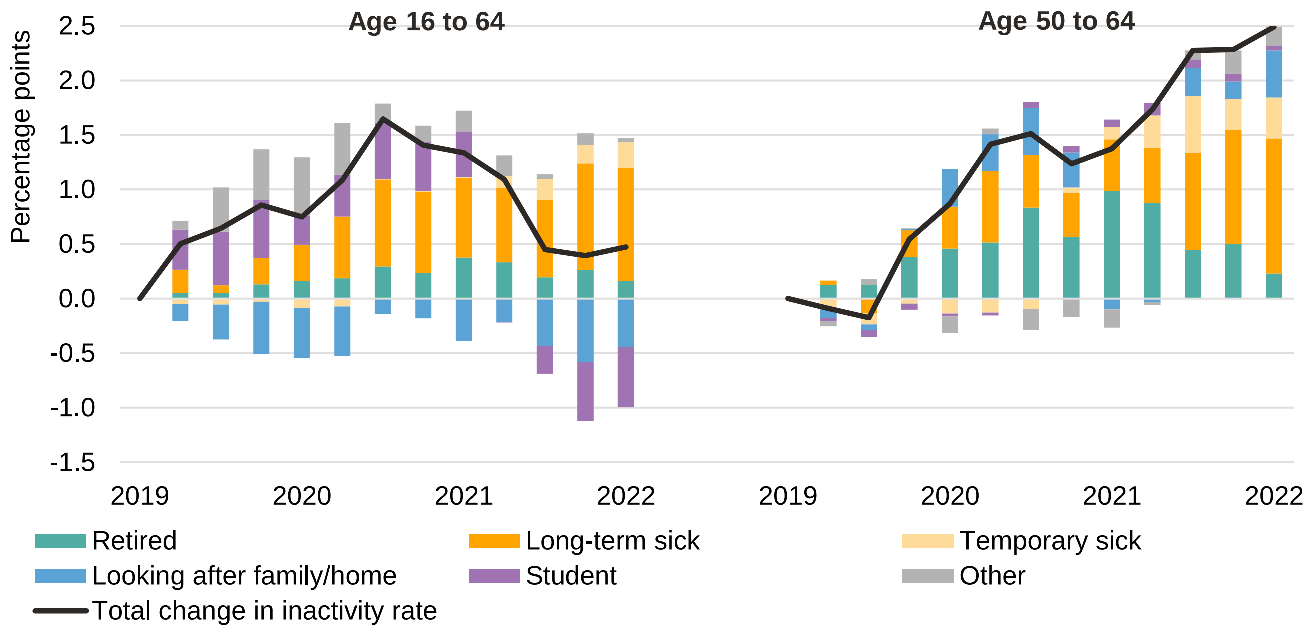
[27] ONS (2023) A11: Labour Force Survey sampling variability (link), ONS (2023) S02 Regional labour market: sampling variability and revisions summary (link).

3.30 Data on reasons for inactivity for Scotland are provided by the APS. In Figures 3.16 and 3.17 we focus on rates rather than levels of inactivity to exclude the effect of changes in demographics. The 50 to 64 age group inactivity rate has seen the largest increase, of 2.5 percentage points between 2019 and 2022. The APS inactivity rate for 16 to 64 age group initially increased during the pandemic but has recently fallen, driven by decreasing inactivity rates for the younger age groups.

3.31 Analysis of longitudinal, or flows, UK LFS data for the 16 to 64 age group show that most of the increase in inactivity due to ill-health has come from people who were already inactive for another reason, including those who had been out for work for five years or longer.[28] Analysis of the longitudinal Scottish APS data show similar findings of recomposition within inactivity for Scotland.[29]

3.32 For people aged 50 to 64, the increase in the inactivity rate since the pandemic was initially due to early retirement during the pandemic. In 2022, ill-health has become the main driver of inactivity in this cohort, while the contribution from retirement has decreased. This probably reflects a combination of two factors: that some retirees would like to return to work but have become unwell, changing their main reason for inactivity to ill-health (recomposition); as well as some active people becoming unwell and leaving the labour market (flows out of activity into ill-health). For retirement, the decrease in its contribution as a reason for inactivity could also reflect post-pandemic retirees re-entering the labour force, in response to the cost of living crisis.[30]

Figure 3.16: Change in 16 to 64 and 50 to 64 age groups inactivity rates since the pandemic in Scotland



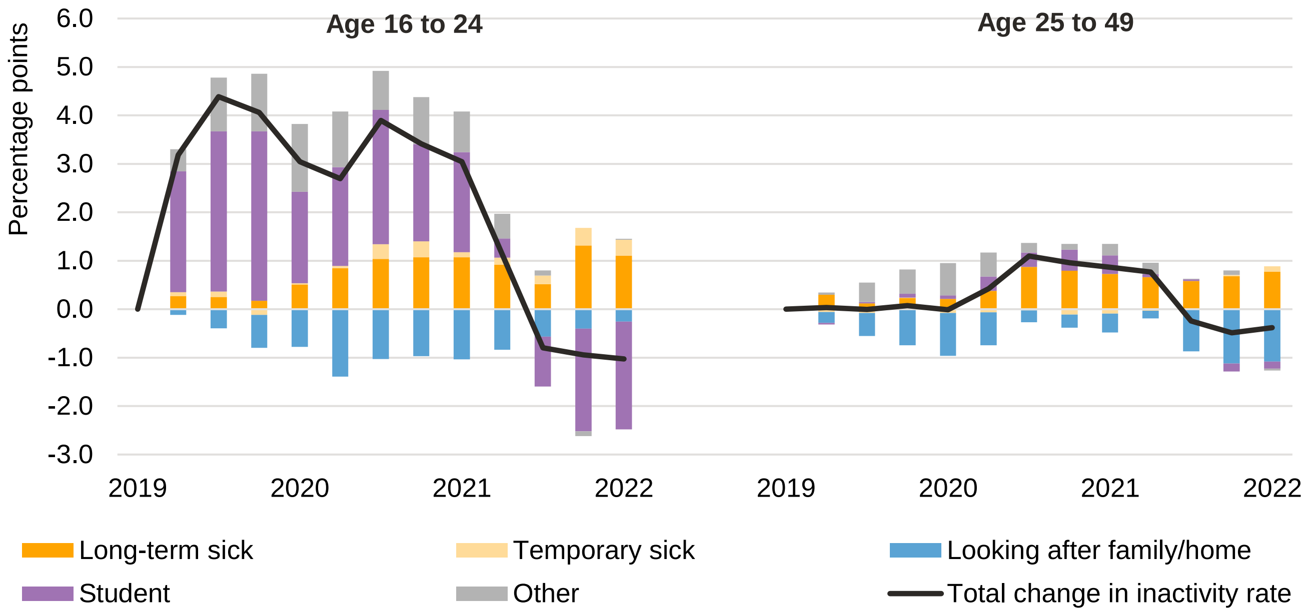
Source: Scottish Fiscal Commission, ONS (2023) APS access via nomisweb (link).
In this Figure, the bars refer to overlapping time periods, as APS data are on a rolling annual basis, but each bar is the change relative to January to December 2019. The comparison in this Figure is to the pre-COVID period, not between overlapping periods.

3.33 Similarly for the younger age groups, ill-health has been on the rise in terms of its contribution to the change in inactivity rates since the pandemic. This could be a mix of people moving from other reasons for inactivity into ill-health (recomposition) as well as active people becoming inactive due to

[28] Institute for Fiscal Studies (2022) Is worsening health leading to more older workers quitting work, driving up rates of economic inactivity? (link), ONS (2022) Half a million more people are out of the labour force because of long-term sickness (link), Resolution Foundation (2023) Post-pandemic participation (link).
[29] Fraser of Allander Institute (2023) Economic inactivity and ill-health in Scotland (link).
[30] Institute for Fiscal Studies (2023) New data show signs of over 50s returning to the workforce (link).

ill-health. For example, relating to recomposition effects, since the COVID-19 pandemic there have been fewer people whose main reason for inactivity is looking after family or home. Some of these people will have entered the labour market while others may have become unwell and changed their main reason for inactivity to ill-health. Overall, since the start of 2022, inactivity rates for the 16 to 24 and 25 to 49 age groups have fallen compared to the pre-pandemic period.

Figure 3.17: Change in 16 to 24 and 25 to 49 age groups inactivity rates since the pandemic in Scotland



Source: Scottish Fiscal Commission, ONS (2023) APS access via nomisweb (link).
In this Figure, the bars refer to overlapping time periods, as APS data are on a rolling annual basis, but each bar is the change relative to January to December 2019. The comparison in this Figure is to the pre-COVID period, not between overlapping periods.

3.34 In December 2022, we said that if rising ill-health continues to be limited mostly to the already inactive population then there is unlikely to be much of an effect on the participation rate. We partly draw on work from the Fraser of Allander Institute (FAI) and the ONS to support our judgement, with both institutions finding that between 50 per cent to 70 per cent of 16-64-year-olds who recently became inactive due to ill-health were already inactive for another reason.[31] However, we acknowledge the complexity of this issue and the evolving nature of the evidence base. For example, someone may have chosen to become inactive due to retirement, but perhaps an element of ill-health spurred that decision to retire early even if it is not recorded as such in the data.

3.35 Widespread inactivity due to ill-health is a downside risk to labour force participation.[32] On the other hand, if NHS waiting lists get smaller faster and the population gets healthier quicker, those too unwell to work could return and labour force participation rates could be higher than expected.

3.36 Rising ill-health measured in the surveys also tallies with higher demand for disability payments in both Scotland and the rest of the UK, as discussed in **Chapter 5**.

[31] Fraser of Allander Institute (2023) Economic inactivity and ill-health in Scotland (link), ONS (2022) Half a million more people are out of the labour force because of long-term sickness (link).
[32] Joseph Rowntree Foundation (2023) Importance of ill-health to the UK's labour market participation challenge (link).

Employment capacity and hours worked

3.37 Since our December 2022 forecast, we have made small changes to the profile of our population forecast but, by 2027-28, the size of the age 16 and over population is roughly unchanged. We have lowered our migration estimates in 2021-22 and 2022-23 in light of new migration data published by the ONS in January 2023. This is offset by slightly higher international migration from mid-2023 onwards of 13,000 per year, up from 10,000, in line with the revised ONS migration projections.

3.38 Despite the age 16 to 64 population shrinking over the forecast, the age 65 and over population is growing by more, with the overall age 16 and over population rising. On average, age 16 and over population growth adds 0.4 percentage points to annual trend GDP growth over the forecast period, as shown in Figure 3.12. Combined with a slightly decreasing trend labour force participation rate, a stable structural rate of unemployment of 4.1 per cent and stable average hours worked, total hours worked growth adds an average of 0.3 percentage points to annual trend GDP growth over the forecast period.

Productivity

3.39 Productivity growth has been slowing globally since just before the 2008-09 Global Financial Crisis in what is known across developed economies as the 'productivity puzzle'.[33] Trend productivity growth averaged 1.2 per cent from 1998-99 to 2007-08 compared to 0.7 per cent from 2008-09 to 2021-22.[34]

3.40 As in December 2022, we forecast trend productivity growth of 0.5 per cent in 2023-24, rising to 1.2 per cent by 2028-29 which is similar to the path of the OBR's forecast of potential productivity growth for the UK.

3.41 Productivity growth contributes an average of 1.0 percentage points to annual trend GDP growth over the forecast period, as shown in Figure 3.12. Combined with total hours worked growth of around 0.3 per cent, annual trend GDP growth is 1.2 per cent on average over the forecast period.

Comparisons to the OBR

3.42 Figure 3.18 shows that Scotland has lower forecast population growth and a slightly weaker projection for the labour force participation rate than the OBR's forecasts for the UK. These differences mean Scottish GDP growth is around 0.3 percentage points lower in 2027-28, the final comparable year of the two forecasts.

[33] Bank of England (2017) Productivity puzzles – speech by Andy Haldane (link).

[34] Figures based on our estimation of the trend using Quarterly National Accounts GDP data and Annual Population Survey total hours worked data.

Figure 3.18: SFC and OBR trend GDP growth and contribution of components in 2027-28

Forecast (growth in per cent)	Trend GDP growth	16+ population	16+ participation rate	Long-run unemployment rate	Trend average hours worked	Trend productivity
SFC May-23	1.4	0.4	-0.1	0.0	0.0	1.1
OBR Mar-23	1.8	0.7	0.0	0.0	0.0	1.1
Gap	-0.3	-0.3	-0.1	0.0	0.0	0.1

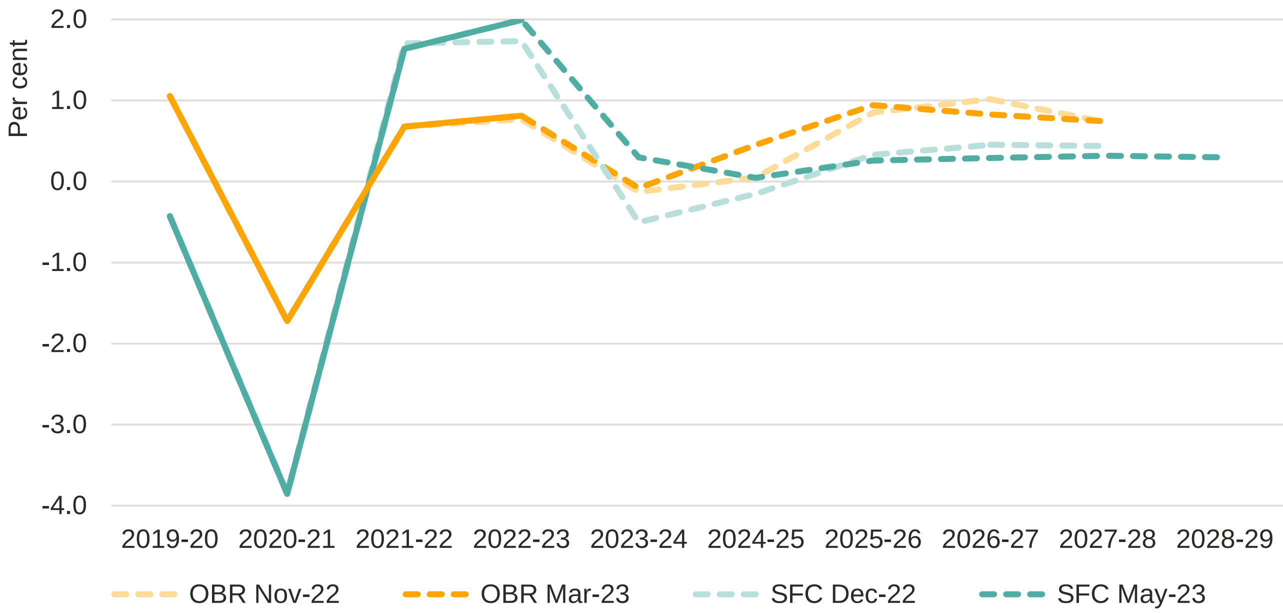
Source: Scottish Fiscal Commission, OBR (2023) Economic and fiscal outlook – March 2023 (link).
Figures may not sum because of rounding.
Potential output growth is approximately equal to the sum of the growth rates of population, employment rate, average hours, and productivity.

Labour market

3.43 The labour market has been more resilient than we forecast in December 2022. The unemployment rate has remained historically low, indicating ongoing tightness in the labour market. We have therefore lowered our near-term outlook for unemployment compared to December. We now forecast that Scotland's unemployment rate rises to its long-run trend of 4.1 per cent by 2024-25 and remains at this rate over the rest of the forecast period. This compares to a peak of 4.7 per cent in 2024-25 in our previous forecast.

3.44 We also expect higher employment growth in the near term. This is the main driver of the positive shift in our income tax revenue forecast for 2023-24 since December. The upward revision to employment growth in 2023-24 is due to relatively stronger outturn data and a higher projection of our participation rate. As discussed in Box 3.1, Scotland's participation data from the LFS and APS have diverged markedly since the pandemic. Therefore, we need to make a judgement about where the trend in Scotland's participation rate sits between these two sources before we can project this trend forward. Since December, we have revised this judgement and made an upward adjustment to our participation rate projection. The starting point of the projection now represents a better balance between the different trends in the LFS and APS data.

Figure 3.19: Employment growth, SFC Scotland and OBR UK



Scottish Fiscal Commission, Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link), OBR (2023) Economic and fiscal outlook – March 2023 (link), OBR (2022) Economic and fiscal outlook – November 2022 (link).
Solid lines refer to outturn available at time of publication and dashed lines refer to forecasts.

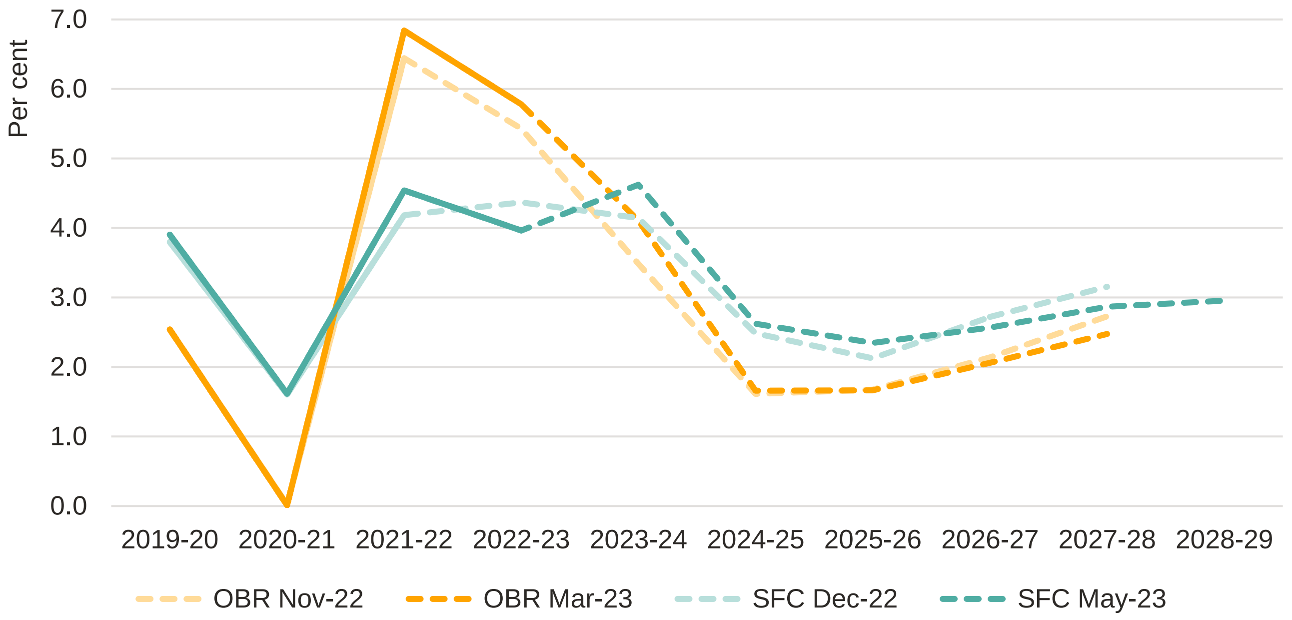
Earnings

3.45 Our overall earnings outlook is broadly similar to what we expected in December 2022. We now forecast slightly higher growth in average earnings in 2023-24, as the ongoing tightness in the labour market and the increased costs of living continue to push up nominal pay growth. This includes higher nominal pay awards in the public sector than we assumed in December. By 2028-29, nominal earnings growth returns to 3.0 per cent in line with productivity growth, unemployment at its trend, and inflation of around 2 per cent. The upward revision in 2023-24 feeds through to higher income tax revenues compared to our December forecast.

3.46 Our forecast of nominal average earnings growth of 4.6 per cent in 2023-24 is slightly above inflation, resulting in a small increase in average earnings in real terms. However, after accounting for taxes and borrowing costs as well as inflation, real disposable incomes are set to fall this year.

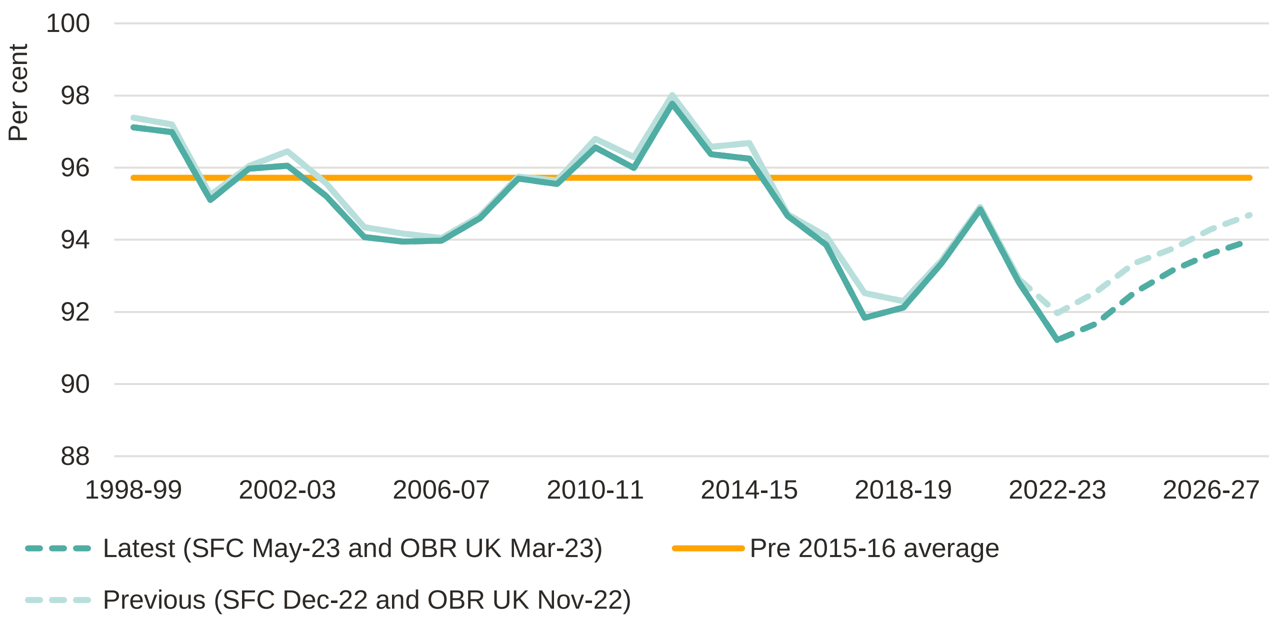
3.47 Figure 3.20 shows our latest May 2023 forecast of nominal average earnings growth, alongside our December 2022 forecast and those of the OBR for the UK. As in December 2022, a divergence in earnings growth between our and the OBR's forecasts continues to be the key driver of the strongly positive projected income tax net position for Scotland. In March 2023, the OBR forecast UK nominal average earnings growth of 2.0 per cent per year between 2024-25 and 2027-28, which is lower than both our forecast for Scotland of 2.6 per cent per year across the same period and the UK average of 2.7 per cent per year between 2011 and 2022.

Figure 3.20: Nominal average earnings growth, SFC Scotland and OBR UK



Scottish Fiscal Commission, Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link), OBR (2023) Economic and fiscal outlook – March 2023 (link), OBR (2022) Economic and fiscal outlook – November 2022 (link).
Solid lines refer to outturn available at time of publication and dashed lines refer to forecasts.

Figure 3.21: Scottish nominal average earnings relative to UK



Scottish Fiscal Commission, Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link), OBR (2023) Economic and fiscal outlook – March 2023 (link), OBR (2022) Economic and fiscal outlook – November 2022 (link).
Solid lines refer to outturn available at time of publication and dashed lines refer to forecasts.

Chapter 4
Tax

Overview

4.1 In this chapter we present our tax forecasts and discuss the effect they have on the Scottish Budget. We summarise our forecasts for income tax, Non-Domestic Rates (NDR), Land and Buildings Transaction Tax (LBTT) and Scottish Landfill Tax (SLfT) in Figure 4.1. We also show changes since December 2022 in Figure 4.2.

Figure 4.1: Summary of tax forecasts

£ million	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Income tax	14,764	16,210	17,080	17,808	18,591	19,646	20,799
Non-Domestic Rates	2,848	3,046	3,133	3,158	3,437	3,328	3,374
Land and Buildings Transaction Tax	840	772	733	792	905	992	1,053
Scottish Landfill Tax	112	92	83	58	16	16	16
Total	18,565	20,121	21,029	21,816	22,949	23,982	25,242

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

Figure 4.2: Summary of changes to our tax forecasts since December 2022

£ million	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
Income tax	190	400	448	438	344	209
Non-Domestic Rates	30	-28	54	23	31	42
Land and Buildings Transaction Tax	-10	0	5	-4	-5	-3
Scottish Landfill Tax	12	12	11	1	0	0
Total	222	384	517	457	370	248

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

4.2 We expect devolved Scottish taxes to raise £20.1 billion of revenue in 2023-24, which is £384 million higher than in our December 2022 forecasts. Much of this change can be attributed to income tax. We have seen a slight improvement in the underlying economy forecast as well as higher than expected Real Time Information (RTI) data on Scottish income tax Pay As You Earn (PAYE) receipts.

4.3 Increasing nominal earnings growth combined with tax thresholds that are fixed in nominal terms are driving up income tax revenues. However, for many people these earnings are not keeping pace with inflation, causing their real incomes to fall. In addition, Scottish Government and UK

Government policy changes to freeze tax thresholds and increase tax rates will have increased average tax bills for taxpayers, further reducing disposable income.

4.4 For NDR a new valuation roll was published on 1 April 2023, which we have included in this forecast. We have also reduced our assumption for the amount of revenue that will be lost to appeals.

4.5 For LBTT, we have revised our house price forecast up slightly since December 2022 in light of a slightly more positive outlook for the economy. This leads to an increase in our forecast for residential LBTT. For non-residential LBTT we have reduced our forecast because of lower outturn than expected since December 2022.

4.6 For SLfT, we have revised our estimate of the amount of waste produced in 2022-23 which increases our forecast.

4.7 Our illustrative forecasts of aggregates levy, air departure tax and assigned Value Added Tax (VAT) are in supplementary figures accompanying this report and available on our website.

Tax forecasts and the Scottish Budget

4.8 For income tax, LBTT and SLfT, our tax forecasts should be considered alongside the associated Block Grant Adjustments (BGAs) to understand the net effect on the funding for the Scottish Budget. NDR have a separate funding process to other taxes for which we provide a detailed explanation in our occasional paper.[35]

4.9 As shown in Figure 4.3, the tax net position shows how much funding the Scottish Government is receiving from Scottish tax revenues compared to the BGAs.

[35] Scottish Fiscal Commission (2021) Funding for the Scottish Budget (link).

Figure 4.3: Tax net positions

£ million	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
Income tax								
BGA	11,852	13,624	14,866	15,799	16,239	16,722	17,359	18,092
Scottish revenue	11,948	13,387	14,764	16,210	17,080	17,808	18,591	19,646
Net position	96	-237	-102	411	841	1,086	1,232	1,554
LBTT								
BGA	397	642	722	519	508	612	723	809
Scottish revenue	517	807	840	772	733	792	905	992
Net position	121	164	118	254	225	179	183	183
SLfT								
BGA	87	102	101	96	91	84	87	92
Scottish revenue	107	125	112	92	83	58	16	16
Net position	20	23	12	-5	-8	-26	-71	-76
Total taxes								
Net position	237	-49	28	660	1,058	1,240	1,344	1,661

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding. Shaded cells refer to outturn available at the time of publication. Negative figures for the net position represent a negative funding effect on the Scottish Budget, where the BGA reduces funding by more than the tax revenue.

The income tax net position

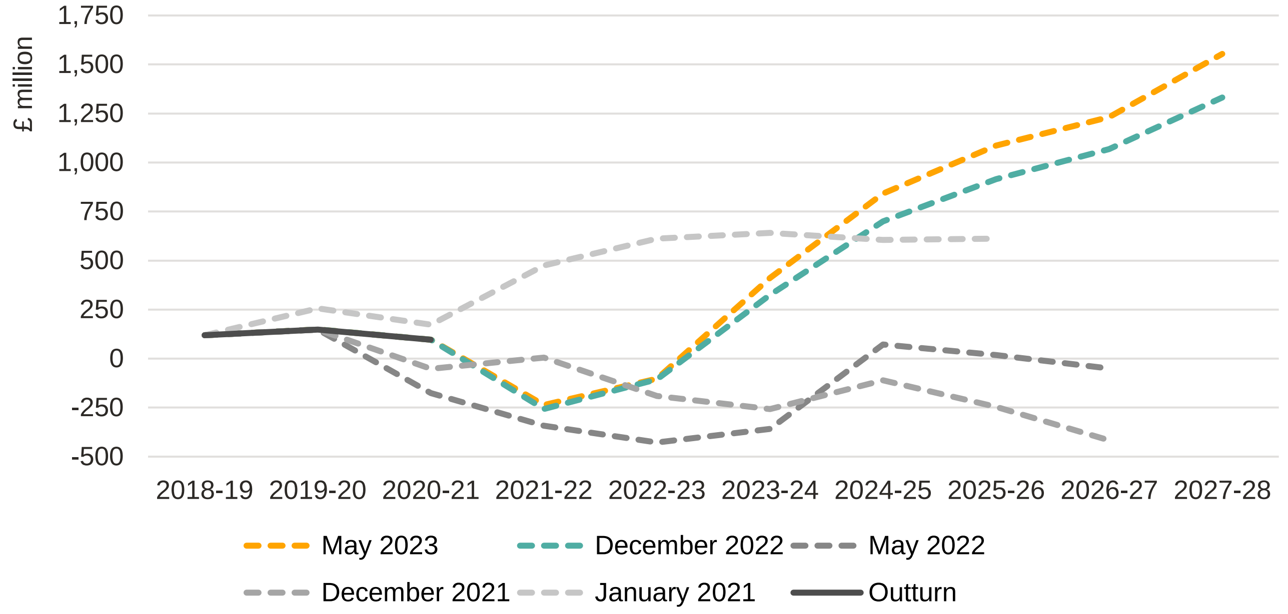
4.10 The income tax net position shows how the funding received from Scottish income tax revenues compares to the reduction in funding from the income tax BGA. Estimates of the income tax net position are calculated by comparing our forecasts to forecasts of the BGA based on forecasts by the OBR.

4.11 In December 2022 our forecasts showed improvements in the net tax position over the five-year horizon compared to previous forecasts. Since then, there have been further, although less significant, improvements in the income tax net position in light of our and the OBR's most recent forecasts. Figure 4.4 shows the different estimates of the income tax position since January 2021.

4.12 As we have stressed in previous reports, we continue to advise caution over the high outlook for the income tax net position. From experience, we can see that revisions to the outlook are quite common. The underlying Scottish and UK income tax forecasts are very large, with the income tax net position driven by the difference between the two. Relatively small changes in either forecast can lead to significant changes in estimates of the net position. In Figure 4.4 we show previous estimates of the net position back to January 2021 to illustrate this variability. Caution over the estimated income tax net position is particularly relevant now as the uncertainty around inflation makes variations in forecasts of income tax revenues in Scotland and the rest of the UK more likely.

4.13 As in December 2022, a divergence in earnings growth between our and the OBR's forecasts continues to be the main driver of the strongly positive estimated income tax net position for Scotland. In March 2023, the OBR forecast UK average nominal earnings growth of 2.0 per cent per year between 2024-25 and 2027-28, the same as in their previous forecast. This is lower than both our forecast of 2.6 per cent per year average nominal earnings growth in Scotland across the same period and the average UK earnings growth of 2.7 per cent per year between 2011 and 2022. If Scottish and UK earnings growth turn out to be closer in the coming years, the net position is likely to be materially lower than currently estimated.

Figure 4.4: The income tax net position comparison



Source: Scottish Fiscal Commission, Scottish Fiscal Commission, Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link), Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – May 2022 (link), Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – December 2021 (link), Scottish Fiscal Commission (2021), Scotland's Economic and Fiscal Forecasts – January 2021 (link).
Solid lines refer to outturn available at time of publication and dashed lines refer to forecasts.

4.14 Focussing on changes to the net position since our December 2022 forecasts, the overall outlook for the Scottish economy is largely unchanged, with slow and fragile economic growth over the short term.

4.15 While the changes we have made to the economic outlook are small, these are larger than those of the OBR for the UK as a whole from 2023-24. This leads to an increased income tax net position relative to that estimated in December 2022. Based on the latest forecasts by us and the OBR, we now expect the net position to be £411 million in 2023-24, while in December 2022 we expected it to be £325 million.

4.16 The employment growth rate is one of the main drivers of the revisions to the income tax net position. We have increased our employment growth rate in 2023-24 to 0.3 per cent, up from -0.5 per cent in December 2022. In contrast, the OBR have maintained their employment growth rate at -0.1 per cent. We estimate that 0.1 per cent extra growth in Scottish employment relative to the rest of the UK would lead to a £13 million increase in the net position.

4.17 Since our previous forecasts, the OBR have revised up their average nominal earnings growth rate in 2023-24 by 0.6 percentage points which is similar to our upwards revision of 0.5 percentage points. We estimate that 0.1 per cent extra growth in Scottish average nominal earnings relative to the rest of the UK would lead to a £25 million increase in the net position.

4.18 RTI data on Scottish PAYE income tax receipts in 2022-23 have been much higher than we expected in our December 2022 report. This has pushed up our income tax forecast and the net position by £190 million.

Income tax reconciliations

4.19 When the Scottish Budget is set, funding from Scottish income tax for the financial year is based on our forecasts and does not change during the year. Only when outturn information on income tax revenues become available is funding brought in line with outturn and a reconciliation applied to the following Scottish Budget.

4.20 We can derive indicative estimates of future income tax reconciliations by comparing our latest forecasts and the latest forecast BGAs to those used in the Budget setting forecasts. We show outturn and indicative estimates of income tax reconciliations in Figure 4.5.

Figure 4.5: Outturn and indicative estimates of income tax reconciliations

Collection year	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24
Applies to Budget for	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
Reconciliation (£ million)	-204	-309	-34	50	-712	88	86

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

4.21 As we have highlighted in recent publications, we continue to expect a large and negative income tax reconciliation for the Budget year 2021-22. Comparing our and the OBR's latest forecasts indicates a large negative reconciliation for 2021-22 of -£712 million. Final outturn data should be available in July 2023, with the resulting reconciliation being applied to the Scottish Budget for 2024-25.

4.22 The forecasts underpinning the Scottish Budget for 2021-22 were made during a time of significant uncertainty around COVID-19. Figure 4.6 shows how forecasts of Scottish income tax revenues and the BGA have been updated since the 2021-22 Scottish Budget was set based on our January 2021 forecasts.

Figure 4.6: Scottish income tax (SIT) revenue forecast and BGA for 2021-22

£ million	Budget setting	Latest	Total Change
SIT	12,263	13,387	1,124
BGA	-11,788	-13,624	-1,836
Net position	475	-237	-712

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

4.23 In January 2021 we stated that the high Budget setting net position of £475 million, largely arose because of the significant uncertainty around COVID-19 and its effects on the data and judgements used in our and the OBR's forecasts, as well as issues with the timing of forecasts.[36] We did not expect Scottish tax revenues to perform significantly differently to the UK in 2021-22. We cautioned that a negative reconciliation was likely, suggesting a value of -£300 million if the net position was closer to the lower 2020-21 value. Given the latest forecasts, the net position is now estimated to be -£237 million in 2021-22, leading to an indicative reconciliation estimate of -£712 million.

[36] Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – January 2021 (link), see paragraphs 2.8 and 2.22 to 2.26

4.24 The reconciliation can still change between the final indicative estimate and the outturn data. For example, for the 2020-21 reconciliation, the final indicative estimate published in May 2022 was out by £221 million, a 1.8 per cent error when compared to the 2020-21 outturn. However, in general, as we get closer to the publication of outturn, we expect indicative reconciliation estimates to become more accurate. Some uncertainty always remains about the precise value of the reconciliation, with potential errors in both our and the OBR's forecasts.

4.25 Despite the uncertainty, we expect the 2021-22 reconciliation will be large, negative, and greater than the Scottish Government's borrowing powers or potential use of the Scotland Reserve. We will discuss the final reconciliation that will be applied to the 2024-25 Scottish Budget in our next Forecast Evaluation Report in August 2023, following the publication of outturn data.

Tax policy changes

4.26 We have estimated the cost of several tax policy changes that have been introduced alongside the Scottish Government's Medium-Term Financial Strategy (MTFS). These are shown in Figure 4.7.

Figure 4.7: Summary of tax policy changes

£ million	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Non-Domestic Rates	-4	-2	0	0	0	0
LBTT	1	5	2	-5	-5	-6
Total	-3	3	2	-5	-5	-6

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

4.27 The Scottish Government has announced two new policies for NDR. There will be a transitional relief for properties located in parks that are new entries on the valuation roll and also reverse vending machines will be removed from the valuation roll rather than receiving NDR relief.

4.28 The Additional Dwelling Supplement (ADS) is an additional charge added to any LBTT which may be due from purchasing additional property. Following a consultation, the Scottish Government intends to implement changes to ADS legislation in 2023-24.

4.29 The first change is that Scottish Government will increase the timelines applying to the ADS, including the repayment timeline from 18 months to 36. We expect this change to be implemented in Autumn 2023. There are other small changes to ADS legislation that fall below our materiality threshold. We provide more detail on these changes in Annex C, but have not produced costings.

Income tax

Forecast

4.30 Our latest forecast is presented in Figure 4.8. Since December 2022, we have increased our forecast for income tax for all years. This is driven mainly by changes in the underlying economy forecasts since December 2022.

Figure 4.8: Forecast revenue for non-savings, non-dividend (NSND) income tax

£ million	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Income tax	11,948	13,387	14,764	16,210	17,080	17,808	18,591	19,646	20,799

Source: Scottish Fiscal Commission, HMRC (2022) Scottish Income Tax Outturn Statistics: 2020 to 2021 (link)
Shaded cells refer to outturn available at time of publication.

Contributions to changes in income tax

4.31 In our economy forecasts we have revised up our outlook for employment growth and nominal earnings growth. In Figure 4.9 we show the effect of those changes between December 2022 and our latest forecast. We expect the change in employment growth rates to increase our income tax forecast by £209 million in 2023-24. This is because of higher recent employment outturn data and a revision to our forecasted participation rates. We discuss participation rates in further detail in Chapter 3.

4.32 Our revision to nominal earnings growth is largely because of an expected increase to the public sector pay award in 2023-24. This revision contributes £71 million towards the change in our forecast for 2023-24 as shown in Figure 4.9. Increasing nominal earnings combined with tax thresholds that are fixed in nominal terms are driving up income tax revenues over the forecast horizon. However, for many people these earnings are not keeping pace with inflation, causing their real incomes to fall.

4.33 Real Time Information (RTI) data on income tax receipts provide timely information on how much PAYE income tax has been collected and is relevant for our 2021-22 and 2022-23 forecast. RTI data have consistently shown levels of PAYE income tax above what we expected in our December 2022 forecast. This adjustment increases our forecast by £190 million in 2022-23.

4.34 We have used the HMRC incorporations forecast, which estimates the income tax lost as a result of incorporations in response to the Scottish and UK tax systems. This decreases our forecast by £100 million in 2023-24 and £280 million decrease in 2027-28. While there are a large number of factors affecting the decision to incorporate, the increases in rates and changes in thresholds in Scotland relative to the UK increase the incentives for those who can manage their tax affairs by setting up a limited company. These effects are largest for taxpayers at the threshold between intermediate and higher rate, but there is also an effect for taxpayers at the top rate threshold.

4.35 The effects of changes in UK tax policy on pensions lifetime and annual allowances announced in the UK Spring Budget 2023 reduce our income tax forecast from 2023-24. We have used provisional data from HMRC on Self Assessment receipts to increase the forecast in 2021-22 by £50 million.

Figure 4.9: Change in NSND income tax forecast since December 2022

Change, £ million	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
December 2022 forecast	11,948	13,337	14,575	15,810	16,633	17,370	18,247	19,437
Employment				209	241	238	225	219
Earnings				71	129	213	186	115
RTI [1]			190	206	217	227	239	254
Incorporations				-61	-100	-153	-214	-280
UK policy effects				-14	-31	-75	-77	-81
Self Assessment receipts		50						
Model updates		0	0	-11	-8	-11	-15	-18
May 2023 forecast	11,948	13,387	14,764	16,210	17,080	17,808	18,591	19,646
Change since December 2022	0	50	190	400	448	438	344	209

Source: Scottish Fiscal Commission, Scottish Government, HMRC (2022) Scottish Income Tax Outturn Statistics: 2020 to 2021 (link).
Shaded cells refer to outturn available at time of publication. Figures may not sum because of rounding.
[1] RTI weighting 0.75.

The effect of fiscal drag

4.36 Tax thresholds in Scotland and the UK have been rising by less than inflation. Over time, this is leading to increased fiscal drag, with the bulk of taxpayers paying a higher average effective tax rate and many taxpayers moving into higher tax bands. While this is happening in both Scotland and the UK, the effect is greater in Scotland.

4.37 The personal allowance, which is set by the UK Government but applies across the whole of the UK, has risen by only £70 since 2019-20 and is set to stay at £12,570 until 2027-28. As peoples' incomes rise with inflation, this means a greater proportion of their earnings will be subject to taxation.

4.38 On top of the freezing of the personal allowance, since 2017-18 the Scottish Government has increased income tax rates and largely frozen thresholds. The introduction of the intermediate rate of 21 pence in 2018-19, the freezing of the higher rate threshold, the increase in the higher rate of tax to 42 pence, and the increase in the top rate of tax to 47 pence have led to higher average effective tax rates for many taxpayers.

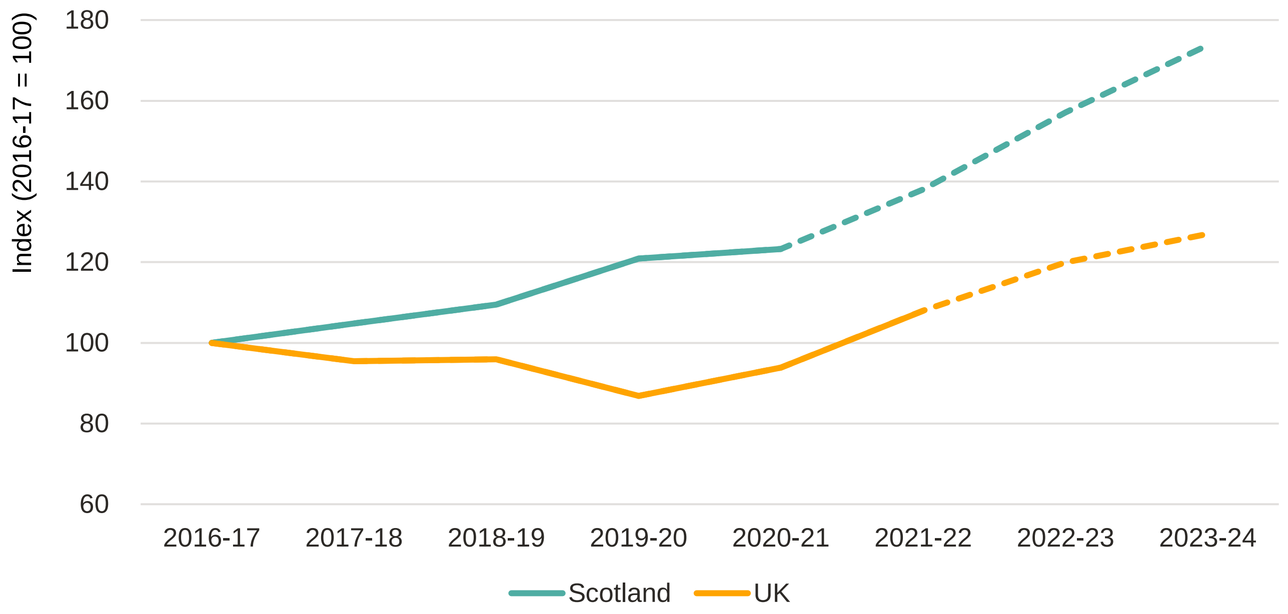
4.39 In 2016-17, prior to the devolution of income tax to Scotland, the higher rate threshold was £43,000 in both Scotland and the rest of the UK. Since income tax was devolved in 2017-18, the Scottish Government has largely kept the higher rate threshold frozen, or limited it to only small increases. In 2023-24, the higher rate threshold in Scotland is £43,662, a £662 increase over seven years. In contrast, the UK Government increased the higher rate threshold in the rest of the UK rapidly from 2016-17, reaching £50,000 by 2019-20. Since 2020-21, the UK higher rate threshold has risen more slowly and is set at £50,270 in 2023-24, then frozen until 2027-28.

4.40 These policies have had a large effect on the number of higher rate taxpayers. Figure 4.10 shows how the number of higher rate taxpayers has changed in Scotland and the UK since 2016-17. The number of higher rate taxpayers in Scotland is expected to have grown by about 74 per cent between 2016-17 and 2023-24. In 2023-24, we expect 17.8 per cent of all Scottish taxpayers to pay the higher rate of tax, compared to 11.6 per cent in 2016-17.

4.41 In contrast, the number of higher rate taxpayers in the UK fell between 2016-17 and 2019-20, when the higher rate threshold was being increased rapidly. With the UK higher rate threshold largely frozen since 2020-21, the number of higher rate taxpayers in the UK is gradually climbing again, though at a slower rate than in Scotland. Overall, we estimate that the number of higher rate taxpayers in the UK will have increased by around 27 per cent since 2016-17.

4.42 The growth in the number of higher rate taxpayers and the differences between Scotland and the UK are almost entirely driven by policies around the higher rate threshold and the general increase in nominal earnings driven by inflation across the whole of the UK. The more rapid growth in the number of higher rate taxpayers in Scotland is not driven by faster earnings growth or shifts in the income distribution relative to the UK.

Figure 4.10: Growth in higher rate income taxpayers in Scotland and UK



Source: Scottish Fiscal Commission
Solid lines show outturn available at time of publication and dashed line shows forecast. Amounts indexed so that 2016-17 is equal to 100.
The Scottish series is from the Scottish Fiscal Commission forecast and is consistent with HMRC income tax outturn data on the number of NSND income taxpayers. UK values are on a different basis, consistent with SPI data and covering all of income tax, not just the NSND element (link).
Forecast UK values are from the OBR (2023) and are for the whole of the UK, including Scotland: OBR (2023) Economic and Fiscal Outlook – March 2023 (link).

Forecast uncertainty

4.43 The uncertainties in our economy forecast are discussed Chapter 3.

4.44 RTI data are gathered from the HMRC PAYE administration system and as a result may not represent the final tax position of individual taxpayers. Most taxpayers who file Self Assessment returns pay some income tax through PAYE and some through Self Assessment. The RTI data will cover the income tax paid through PAYE but not the income tax paid through Self Assessment which is a small but volatile part of Scottish income tax. We have nearly complete RTI data coverage for 2021-22 and 2022-23 which reduces the uncertainty for those years. The outturn data for 2022-23 will not be available until July 2024 so RTI provides useful and timely data for our forecasts.

4.45 Incorporations modelling is carried out by HMRC and attempts to capture a wide range of behavioural changes in the way that the tax affairs of owner managers are arranged. There are no direct measurements of the liabilities that would have been paid by those who chose to incorporate so this part of the forecast has a high level of uncertainty.

4.46 The Survey of Personal Incomes Public Use Tape (PUT) dataset that we use in our simulation model is a sample of the taxpayer population in Scotland in 2019-20. We have income tax outturn data for 2020-21 and we have used this to update the PUT. This means that the population sample for our model is between two and three years out of date. We expect the taxpayer distribution to vary over time and in response to COVID-19 and the UK and Scottish Government measures introduced to reduce the economic impact. This introduces an uncertainty as we may not capture changes in the distribution in response to these economic conditions or policy changes.

Comparison to the OBR

4.47 We and the OBR produce tables that allow key determinants of our forecasts to be compared. In Figure 4.11 we compare the growth rates used by the OBR in their forecasts for the UK Spring Budget in March 2023 to our latest growth rates.[37] In Figure 4.12 we show the changes in the level of income tax revenues and economic determinants for the forecast period, indexed to 2020-21.

4.48 The OBR forecasts for NSND income tax in England and Northern Ireland are used to determine the Scottish Government's BGAs. These BGAs and our forecasts for Scottish income tax affect the funding available to the Scottish government in any given year. In the longer term a process of reconciliation is carried out when the outturn data for both regions are available. The historical reconciliations are shown in Figure 4.5 alongside our indicative examples of forecast reconciliations to be applied from 2024-25.

4.49 Both forecasts share the assumption that the higher rate threshold in Scotland will remain fixed in cash terms over the forecast period. Scottish ministers decide annually what thresholds and rates will apply to Scottish taxpayers as part of the Scottish budget.

[37] Office for Budget Responsibility (2023) Economic and fiscal outlook – March 2023 (link).

Figure 4.11: Comparison of SFC and OBR economic determinants (growth rates)

Source	Per cent change	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
Income tax revenue	OBR[1]	15.4	9.6	6.7	3.2	3.4	4.2	4.7
Income tax revenue	SFC[2]	12.0	10.3	9.9	5.4	4.3	4.4	5.7
Employment	OBR	0.7	0.8	-0.1	0.5	0.9	0.8	0.7
Employment	SFC	1.6	2.0	0.3	0.0	0.3	0.3	0.3
Average nominal earnings	OBR	6.8	5.8	4.1	1.7	1.7	2.1	2.5
Average nominal earnings	SFC	4.5	4.0	4.6	2.6	2.3	2.6	2.9
Total nominal earnings	OBR[3]	8.4	6.6	4.0	2.0	2.4	2.6	3.0
Total nominal earnings	SFC	7.0	6.2	4.9	2.7	2.6	2.9	3.2

Source: Scottish Fiscal Commission, OBR (2023) Economic and fiscal outlook – March 2023 (link).
Shaded cells refer to outturn available at time of publication.
[1] UK NSND excluding SIT and Welsh rate of income tax (WRIT).
[2] Scottish NSND income tax.
[3] This refers to OBR's wages and salaries series.

Figure 4.12: Comparison of SFC and OBR economic determinants (cumulative growth paths)

Source	Index 2020-21 = 100	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
Income tax revenue	OBR [1]	115	126	135	139	144	150	157
Income tax revenue	SFC [2]	112	124	136	143	149	156	165
Employment	OBR	101	102	101	102	103	104	104
Employment	SFC	102	104	104	104	104	105	105
Average nominal earnings	OBR	107	113	118	120	122	124	127
Average nominal earnings	SFC	105	109	114	117	119	122	126
Total nominal earnings	OBR [3]	108	116	120	123	126	129	133
Total nominal earnings	SFC	107	114	119	122	126	129	133

Source: Scottish Fiscal Commission, OBR (2023) Economic and fiscal outlook – March 2023 (link).
Shaded cells refer to outturn available at time of publication.
[1] UK NSND excluding SIT and WRIT.
[2] Scottish NSND income tax.
[3] This refers to the OBR's wages and salaries series.

4.50 The growth rates of UK income tax revenue are lower than ours from 2022-23 onwards which reflect our differing forecasts of employment and earnings and the different policy environment for income tax. The Scottish Government has the power to vary income tax rates and thresholds and has used these powers to freeze tax thresholds and increase tax rates. In 2022.23 and 2023-24 employment growth is higher in our forecast than the OBR's but in the later years of the forecast, the position reverses and our employment growth is lower than the OBR's. For both nominal and average earnings our forecast is for lower growth in 2021-22 and 2022-23, then for later years our forecast is higher.

Non-Domestic Rates

4.51 Non-Domestic Rates, also known as business rates, are payable on non-domestic properties. Our latest forecast is shown in Figure 4.13. In 2023-24 the tax is forecast to raise £3,046 million.

Figure 4.13: Forecast revenue for Non-Domestic Rates

£ million	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
NDR	2,848	3,046	3,133	3,158	3,437	3,328	3,374

Source: Scottish Fiscal Commission.

Changes since December 2022

4.52 Figure 4.14 shows how our Non-Domestic Rates forecast has changed since December 2022.

Figure 4.14: Change in Non-Domestic Rates revenue since December 2022

£ million	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
December 2022	2,818	3,075	3,080	3,135	3,405	3,286
Assumption change	0	26	72	50	13	28
Methodology change	34	-30	-13	-32	-10	-8
Data updates	-4	-18	34	17	13	11
Policy recosting	0	-2	5	4	-3	-2
Inflation update	0	0	-42	-17	19	12
May 2023 forecast pre-measures	2,848	3,051	3,135	3,158	3,437	3,328
Policy costing	0	-4	-2	0	0	0
May 2023 forecast post-measures	2,848	3,046	3,133	3,158	3,437	3,328
Change since December 2022	30	-28	54	23	31	42

Source: Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link).
Figures may not sum because of rounding.

Assumption and methodology changes

4.53 We base rateable value for the next financial year on the valuation roll, with adjustments for appeals losses and rateable value growth during the year. We have used the new valuation roll published 1 April 2023 for this forecast.

4.54 We have reduced our estimate of revenue lost to resolved appeals for the 2017 revaluation cycle from 6.0 per cent to 5.5 per cent in response to current information on the values of resolved and outstanding appeals. This increased our forecast for 2023-24 NDR revenue by £26 million and our forecast for 2024-25 by £72 million.

4.55 We have changed the way we profile revenue lost to appeals in response to new data on the progression of 2017 cycle appeals. This and other small methodology changes decreased our forecast of 2023-24 NDR revenue by £30 million.

4.56 A new two-stage appeals system started on 1 April 2023. We have included the new system in our forecast and described it in detail in our December 2021 and May 2022 publications.[38,39] The effects of the new system on revenue lost to resolved appeals are not yet known and our assumptions around appeals may change as we receive more appeals data.

Data updates

4.57 We now have a full non-domestic property valuation roll for 2023-24, published on 1 April 2023[40]. This replaced the imputed valuation roll we used in our December 2022 forecast, containing a mix of draft and estimated rateable values of all properties for 2023-24. This update increased our forecast of NDR revenue for 2023-24 by £10 million.

4.58 We have also received revaluation appeals data up to Q3 2022-23 and information on 2017 appeals cycle. All data updates combined have decreased our forecast for 2023-24 by £18 million since December 2022.

Inflation update

4.59 The poundage is the percentage of rateable value that non-domestic properties are liable to pay in rates. Rateable value is the taxable value of a property. Reduced inflation forecasts since December 2022 have decreased our forecast of NDR revenue in 2024-25 and 2025-26 before policy decisions on poundage are included.

4.60 We assume for forecasting purposes that in future years the Scottish Government will set the poundage in line with inflation, unless there is a policy decision otherwise. Past poundage is shown in Figure 4.15, comparing our estimates for poundage based on inflation with the actual poundage set by policy decision in past years.

Figure 4.15: Estimated poundage and actual poundage in past years

Poundage (pence)	2019-20	2020-21	2021-22	2022-23	2023-24
Estimated poundage	49.6	49.8	50.1	50.5	54.8
Actual poundage	49.0	49.8	49.0	49.8	49.8

Source: Scottish Fiscal Commission. Poundage projected based on September CPI inflation in the previous year.

4.61 The estimated poundage for 2024-25 is 52.5 pence, which is lower than the 53.2 pence in our December 2022 forecast. This is because inflation is forecast to be lower in 2024-25 than we had previously expected. The change in inflation decreases our baseline forecast of NDR revenue in 2024-25 by £42 million. The poundage for 2023-24 has been frozen so it has not changed in response to inflation. The cost of this policy is discussed in Annex B.

Policy Changes

4.62 Costings for new policies are provided in Figure 4.16. Two have been introduced since the 2023-24 Budget.

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38 Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – December 2021 (link).
39 Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – May 2022 (link).
40 Scottish Government (2023) Non-domestic rates revaluation 2023 in Scotland (link).

- Transitional relief for properties in parks that are new entries on the valuation roll for 2023-24.[41]

- Reverse vending machines have been removed from the 2023 valuation roll rather than receiving NDR relief.[42] This policy does not affect NDR revenue but is included as it slightly changes our methodology.

Figure 4.16: NDR policy costings

£ million	2023-24	2024-25	2025-26	2026-27	2027-28
Baseline	3,051	3,135	3,158	3,437	3,328
New entry parks transitional relief	-4	-2	0	0	0
Reverse vending machine removal	0	0	0	0	0
Forecast with policy changes	3,046	3,133	3,158	3,437	3,328
Difference	-4	-2	0	0	0

Source: Scottish Fiscal Commission

4.63 Our forecast also includes recostings for five policies introduced in the 2023-24 Scottish Budget and described in more detail in our December publication[43]. We provide more detail of these recostings in Annex B. The policies are:

- Transitional relief to cap gross bill increases for some properties that increase in value at revaluation.

- Freezing the 2023-24 poundage at 49.8 pence.

- Changes to the Small Business Bonus Scheme (SBBS) eligibility thresholds.

- A second transitional relief for current SBBS recipients that will cap net NDR bill increases to £600, £1,200 and £1,800 over the next three years.

- Increasing the threshold at which properties are liable to pay the Higher Property Rate from £95,000 to £100,000. This change is below our materiality threshold but is included because it affects other modelling.

Forecast uncertainty

4.64 The creation of two Green Freeports in Scotland has been announced[44]. The possible effect of these freeport sites on NDR revenue has not been costed in this forecast because the provisions and implementation of any associated NDR relief have not yet been confirmed.

4.65 From 2024-25 we use CPI inflation to model the poundage, with increases in inflation contributing to increases in poundage. However, the Scottish Government may choose to set the poundage at a different value.

[41] Scottish Government (2023) The Non-Domestic Rates (Transitional Relief) (Scotland) Regulations 2023 (link).
[42] Scottish Government (2020) The Non-Domestic Rates (Reverse Vending Machine Relief) (Scotland) Regulations 2020 (link).
[43] Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link).
[44] Scottish Government (2023) Green Freeports (link).

Land and Buildings Transaction Tax

Forecast

4.66 Land and Buildings Transaction Tax (LBTT) is payable on transactions of residential and non-residential properties and land. Additional Dwelling Supplement (ADS) is a surcharge on purchases of additional residential properties. Our forecast is shown in Figure 4.17.

4.67 In December 2022 we forecast a drop in LBTT revenue due to higher interest rates and a wider economic downturn. For residential LBTT we are still expecting prices and transactions to fall over the next few years compared to 2022-23. However, we are now forecasting a shallower drop in revenue and have revised our forecast up. We have revised down our forecast of non-residential LBTT based on the latest outturn figures.

Figure 4.17: Forecast revenue for Land and Buildings Transaction Tax

£ million	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Residential [1]	559	627	571	530	579	683	757	805
Non-residential	248	213	202	203	212	223	235	248
Total	807	840	772	733	792	905	992	1053

Source: Scottish Fiscal Commission, Revenue Scotland (2022) Annual Report and Accounts 2021-22 – Devolved Taxes Accounts (link).
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication. LBTT revenue is net of repayments but excludes penalties, interest and revenue losses.
[1] Including Additional Dwelling Supplement (ADS).

Residential LBTT

4.68 We still expect high interest rates and the wider economic downturn to have a negative effect on the housing market. However, we are not expecting as large a drop in house prices as we did in our previous forecast.

4.69 Overall, we are forecasting that demand for properties will decrease from next year and we expect both house prices and transactions to drop over the next few years. This follows a period of strong growth particularly in house prices which have increased by 18 per cent from 2019-20 to 2022-23.

Figure 4.18: Change in total residential LBTT (including ADS) forecast since December 2022

£ million	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
December 2022	621	557	510	566	669	740
Model updates	0	0	0	0	0	0
Data updates	6	5	4	5	6	6
House prices	1	7	9	5	11	15
Property transactions	0	1	1	1	1	1
May 2023 forecast pre-measures	627	570	525	577	687	762
Policy costing	0	1	5	2	-5	-5
May 2023 forecast post-measures	627	571	530	579	683	757
Changes since December 2022	6	14	20	13	14	17

Source: Scottish Fiscal Commission

Figures may not sum because of rounding. LBTT revenue is net of repayments, excludes penalties and interest and also excludes revenue losses.

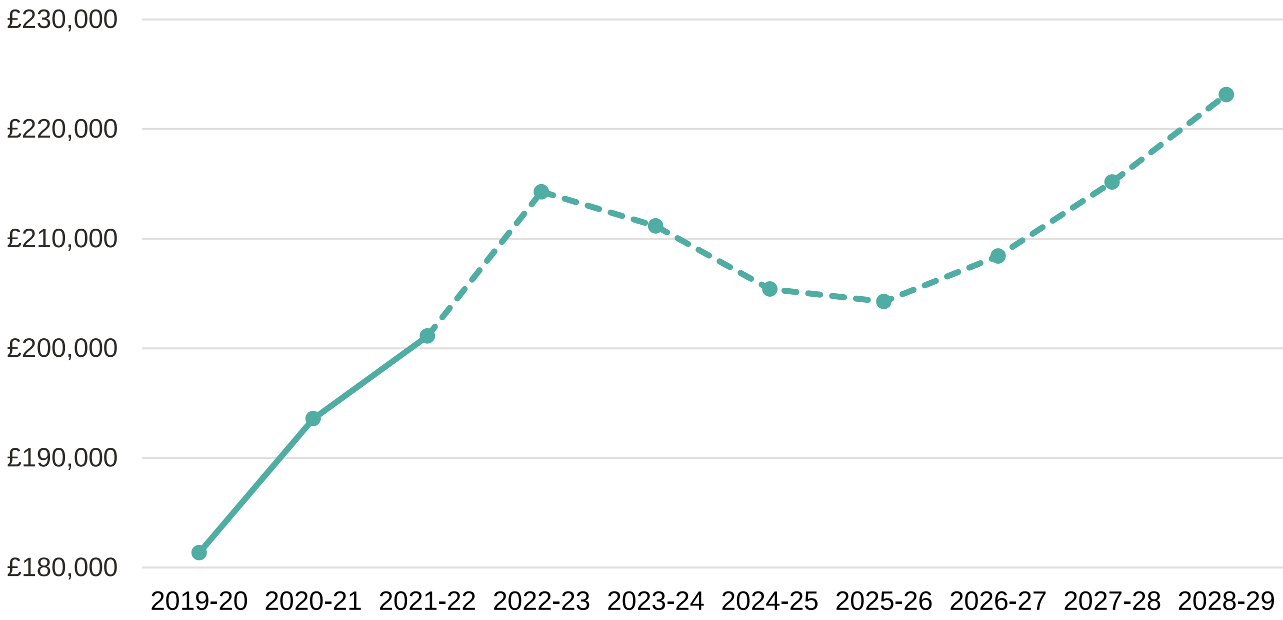
House prices

4.70 In our December 2022 report we expected higher interest rates and lower household disposable income to lead to a fall in house prices. We have now increased our forecast of house prices because of higher outturn than expected in 2022-23 and our expectation that future interest rates will not be as high as those used in our previous forecast.[45] These factors indicate a shallower fall in house prices than we anticipated in December 2022. Our expectations for interest rates are discussed further in Chapter 3.

4.71 We are forecasting a 1.5 per cent fall in average house prices in 2023-24 followed by a further 2.7 per cent fall in 2024-25. We expect house prices to start growing again in 2026-27 and return to the 2022-23 level by 2027-28.

[45] Registers of Scotland (2023) – House price statistics (link).

Figure 4.19: Forecast of average house prices



Source: Scottish Fiscal Commission, Registers of Scotland (2023) – House price statistics (link).
Solid lines refer to outturn available at time of publication and dashed lines refer to forecasts. Note that the vertical axis begins at £180,000.

Property transactions

4.72 Our forecast of transactions has not changed since December 2022. We forecast a 10.6 per cent decrease in 2023-24 and a further 2.8 per cent decrease in 2024-25. We expect transactions to reach 2022-23 levels by 2027-28.

Comparison to the OBR

4.73 The OBR published their UK and devolved house price and transactions forecast in March 2023 Economic and fiscal outlook.[46] Their forecast is similar to ours and they expect house prices to fall in 2023-24 and 2024-25 and begin to rise thereafter.

4.74 We assume that Scotland's housing market is less sensitive to changes in the economy than the wider UK market. The rise in Scotland's house prices has not been as high as in the rest of UK since the pandemic and the average mortgage debt per household is lower in Scotland than in the rest of the UK meaning the Scottish market is less vulnerable to interest rate shocks. We do not expect prices to fall as much as forecast by the OBR in 2023-24 and 2024-25. However, we also expect a slower recovery with prices only rising from 2026-27.

4.75 As with prices, we do not expect Scottish transactions to fall as much as the wider UK market.

[46] Office for Budget Responsibility (2023) Economic and fiscal outlook – March 2023 (link).

Figure 4.20: Comparison of SFC and OBR residential house price and transactions growth rates

Per cent	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
House prices SFC	6.6	-1.5	-2.7	-0.6	2.0	3.2
House prices OBR	7.6	-5.7	-3.9	2.2	3.5	3.6
Transactions SFC	-11.0	-10.6	-2.8	9.6	14.6	5.3
Transactions OBR	-10.5	-15.3	-2.3	11.8	11.5	7.7

Source: Scottish Fiscal Commission, Office for Budget Responsibility (2023) – Economic and fiscal outlook – March 2023 (link).

Policy Costing

Additional Dwelling Supplement

4.76 Additional Dwelling Supplement (ADS) is chargeable where a transaction is for an additional dwelling purchased for over £40,000. You are able to reclaim ADS if you sell one of these properties within a given period of time. Following a consultation, the Scottish Government will increase the timelines applying to the ADS, including the repayment timeline from 18 months to 36 months. We expect this policy will come into effect in Autumn 2023. We have provided further detail in **Annex A**.

4.77 There are other changes to ADS legislation that fall below our materiality threshold. We provide more detail on these changes in **Annex C** but have not provided costings.

Figure 4.21: Impact of changes to the ADS repayment period

£ million	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Total policy costing	1	5	2	-5	-5	-6

Source: Scottish Fiscal Commission

Non-residential LBTT

4.78 The outlook for non-residential property is different than for residential property. Figure 4.22 shows how our non-residential LBTT forecast has changed since December 2022.

4.79 The main changes are driven by data updates. Outturn for 2022-23 non-residential LBTT revenue is lower than we forecast in December 2022 and reduces our forecast in future years.

4.80 Our forecast for prices and transactions from 2023-24 onwards is driven by our economy forecast for GDP. We forecast a slight drop in prices and a slight rise in transactions.

Figure 4.22: Change in non-residential LBTT forecast since December 2022

£ million	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
December 2022	229	216	218	228	241	255
Model updates	0	0	0	0	0	0
Data updates	-16	-15	-15	-16	-17	-18
Prices	0	-2	-2	-1	-1	-1
Transactions	0	3	2	1	0	-1
May 2023	213	202	203	212	223	235
Changes since December 2022	-16	-15	-15	-16	-18	-20

Source: Scottish Fiscal Commission

Figures may not sum because of rounding. LBTT revenue is net of repayments, excludes penalties and interest and also excludes revenue losses.

Forecast uncertainty

4.81 There is uncertainty surrounding our price and transactions assumptions. While we are expecting a downturn in the housing market, the scale of this decrease may change as we receive more data. Other risks include further economic shocks and increases in the cost of living more rapidly outpacing the growth in incomes.

4.82 We have not included the latest quarterly house price statistics from Registers of Scotland (RoS) as it was published after our cut-off date for data inclusions.[47] This would have given us house prices and transactions data for the whole of 2022-23. We will discuss this further in our next Forecast Evaluation Report.

4.83 For non-residential LBTT, future tax revenue is influenced by large transactions. Historically, 1 per cent of transactions accounted for 28 per cent of non-residential LBTT revenue, making the variability of a few transactions significant for the annual tax take and difficult to predict.

4.84 Our policy costing is based on an assumed implementation date in Autumn 2023. If the ADS repayment period extension is implemented at a different time this would affect our costing.

Scottish Landfill Tax

Forecast

4.85 We are forecasting Scottish Landfill Tax (SLfT) revenue of £92 million in 2023-24. We expect revenue will fall with the introduction of more incineration from Energy from Waste (EfW) sites and fall further once the Biodegradable Municipal Waste (BMW) ban is introduced in December 2025.

[47] Registers of Scotland (2023) – House Price Statistics (link).

Figure 4.23: Forecast revenue for Scottish Landfill Tax

£ million	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Revenue	125	112	92	83	58	16	16	16

Source: Scottish Fiscal Commission, Revenue Scotland (2022) Annual Report and Accounts 2021-22 – Devolved Taxes Accounts (link).
Shaded cells refer to provisional outturn available at the time of publication.
Scottish Landfill Tax (SLfT) revenue is net of repayments but excludes penalties, interest and revenue losses.

Changes since December 2022

4.86 We have changed our model after concluding we underestimated waste produced in 2022-23. This has increased our forecast up to 2025-26. The effect of this change decreases as the forecast progresses as we expect increasingly more waste to be diverted from landfill and incineration as we move towards the BMW ban.

4.87 We are expecting more incineration to occur sooner in 2025-26. This would mean less waste going into landfill and therefore less SLfT revenue in that year.

Figure 4.24: Change in Scottish Landfill Tax Forecast since December 2022

£ million	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
December 2022	101	79	72	58	16	16
Model Changes	12	11	10	6	0	0
Determinants	0	2	2	1	0	0
Incineration	0	0	0	-6	0	0
Outturn	-1	-1	-1	-1	0	0
May 2023	112	92	83	58	16	16
Change since previous forecast	12	12	11	1	0	0

Source: Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link), Revenue Scotland (2022) Annual Report and Accounts 2021-22 – Devolved Taxes Accounts (link).
Figures may not sum because of rounding.
Scottish Landfill Tax (SLfT) revenue is net of repayments, excludes penalties and interest and also excludes revenue losses.

Forecast uncertainty

4.88 Future incineration capacity is a source of uncertainty. We will revisit our assumption around incineration in future forecasts.

4.89 There is also waste composition uncertainty. Waste composition can affect incineration capacity as different substances burn at different rates. Waste composition will also be the deciding factor of what can be legally landfilled past the BMW ban.

Chapter 5
Social security

Overview

5.1 In this chapter, we present our forecast of devolved social security spending and its changes since the 2023-24 Scottish Budget was published in December 2022.

5.2 We forecast that the spending on social security increases from £5.3 billion in 2023-24 to £7.8 billion in 2028-29. This increase arises because we expect the number of people in receipt of payments to increase, and on average, the amount people receive increases over time, primarily due to most of the payments being uprated with inflation.

5.3 Figure 5.1 shows that since our previous forecast in December 2022, we have increased our forecast by £45 million in 2023-24, increasing to £122 million in 2027-28. The change in the forecast mainly reflects the higher than previously expected demand for disability payments seen across the UK and the higher number of successful applications to Child Disability Payment (CDP). This increase in spending is partly offset by improvements to our Adult Disability Payment (ADP) modelling, a lower inflation forecast, adjustments to the numbers of carers eligible for payment, and a lower caseload forecast for Scottish Child Payment (SCP).

Figure 5.1: Change in social security spending forecast since December 2022

£ million	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
December 2022	3,682	4,187	5,244	6,163	6,554	6,903	7,267	
May 2023	3,682	4,208	5,290	6,192	6,638	7,000	7,389	7,831
Change since December 2022		21	45	30	84	97	122	

Source: Scottish Fiscal Commission

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

5.4 At the end of the chapter, we discuss how social security spending exceeds the funding expected to be received from the UK Government. The Scottish Government receives funding through the Block Grant Adjustments (BGAs) for devolved social security payments. Increases in spending in a devolved payment will be covered by its BGA if spending on the UK equivalent benefit grows by the same amount. In 2027-28, spending forecast on devolved payments is £0.7 billion above the estimated funding through the BGAs. In addition, we forecast that spending on new payments without a UK equivalent is £0.6 billion. We expect a total of £1.3 billion in additional spending in social security payments which must be funded from the Scottish Budget.

Forecasts

5.5 In this section, we provide detail on the trends driving the increase in the number of clients in receipt of devolved social security payments and the value of the payments received.

5.6 We forecast that over the next five years an increasing number of people will receive disability payments. This increase is mainly because of the increasing prevalence of disabilities across the UK and the effect of disability payments policies introduced by the Scottish Government as well as operational changes implemented by Social Security Scotland.

5.7 The Scottish Government plans to complete the transfer of people receiving a devolved disability or carers' payment administered by the Department for Work and Pensions (DWP) to a Scottish payment delivered by Social Security Scotland by the end of 2025. We assume that Winter Fuel Payment will be devolved in 2024-25. In our May 2022 forecast we included a set of indicative forecasts for the replacement of Attendance Allowance, Carer's Allowance, Disability Living Allowance, Industrial Injuries Disablement Scheme, and Winter Fuel Payment.[48] These indicative forecasts reflected the Scottish Government policy intentions. In this May 2023 forecast we continue to include these indicative forecasts.

5.8 We have now produced a formal costing for Carer Support Payment, the Scottish payment for carers, that will replace Carer's Allowance, currently administered in Scotland by the DWP. We have based this formal costing on detail from the draft regulations, its policy note, and the Scottish Government's response to the public consultation on the policy changes to be introduced when the payment is launched nationally in spring 2024.[49]

5.9 Our forecast also includes the Five Family Payments (FFP) introduced by the Scottish Government to support families with children. FFP includes Scottish Child Payment (SCP), the three Best Start Grant payments, and Best Start Foods. The introduction and expansion to children under sixteen of SCP increased spending over 2022-23 and 2023-24. Spending on these payments remains stable beyond 2023-24.

5.10 Inflation is an important factor driving the increase in spending over time. Most of the payments people receive are uprated with inflation each year and, so we revise the payment rates and average payment forecast based on our inflation forecast.

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[48] These payments will be replaced by Pension Age Disability Payment, Carer Support Payment, Scottish Adult DLA, Employment Injury Assistance) and Pension Age Winter Heating Payment.

[49] Scottish Government (2023) The Carer's Assistance (Carer Support Payment) (Scotland) Draft Regulations 2023: policy note (link), Scottish Government (2023) The Carer's Assistance (Carer Support Payment) (Scotland) Draft Regulations 2023 (link), Scottish Government (2023) Scottish Carer's Assistance consultation: Scottish Government Response (link).

Figure 5.2: Social security spending forecast

£ million	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Adult Disability Payment [1]	1,739	2,032	2,713	3,227	3,559	3,852	4,178	4,544
Best Start Foods	14	13	14	16	19	19	19	19
Best Start Grant	14	20	19	19	19	19	19	19
Carer's Allowance Supplement	58	44	49	57	63	67	71	75
Carer Support Payment [2]	294	315	373	429	483	518	544	572
Child Disability Payment [3]	227	278	367	429	467	503	543	583
Child Winter Heating Assistance	5	6	7	7	8	8	9	9
Discretionary Housing Payments	76	82	84	90	94	99	105	111
Employability Services [4]	26	24	21	25	25	25	25	25
Employment Injury Assistance [5]	80	78	84	86	84	83	81	79
Funeral Support Payment	10	10	12	12	12	12	13	13
Pension Age Disability Payment [6]	515	558	643	715	762	790	816	842
Pension Age Winter Heating Payment [7]				180	184	186	185	188
Scottish Adult Disability Living Allowance [8]	464	460	436	407	363	320	284	252
Scottish Child Payment	56	218	405	428	433	435	436	438
Scottish Welfare Fund	36	38	36	36	36	36	36	36
Self-Isolation Support Grant	62	8						
Severe Disablement Allowance	7	6	6	5	5	4	3	3
Winter Heating Payment		20	22	23	23	23	22	22
Total spending	3,682	4,208	5,290	6,192	6,638	7,000	7,389	7,831

Source: Scottish Fiscal Commission, Social Security Scotland, Scottish Government.
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.
[1] Adult Disability Payment has replaced Personal Independence Payment. Figures include spending on Personal Independence Payment until case transfer is complete.
[2] Carer Support Payment will replace Carer's Allowance from spring 2024. Figures include spending on Carer's Allowance until case transfer is complete and Carer's Additional Person Payment which will be introduced after case transfer is complete.
[3] Child Disability Payment spending includes spending on the UK Government Disability Living Allowance for children, while recipients are transferred to the new payment.
[4] Employability Services is an indicative forecast and includes spending on Fair Start Scotland service and additional funding for the replacement of the devolved employability support service.
[5] Employment Injury Assistance is an indicative forecast and includes our estimate of the change in the baseline Industrial Injuries Disablement Scheme and changes arising from the introduction of Employment Injury Assistance policy.
[6] Pension Age Disability Payment is an indicative forecast and includes our estimate of the change in the baseline Attendance Allowance and changes arising from the introduction of Pension Age Disability Payment policy.
[7] Winter Fuel Payment is expected to be devolved in winter 2024 and replaced by Pension Age Winter Heating Payment.
[8] Scottish Adult DLA is an indicative forecast and includes our estimate of the change in the baseline DLA Adult and changes arising from the assumed introduction of Scottish Adult DLA and associated policy.

Changes since December 2022

5.11 Our latest forecast has been updated to reflect the trends emerging in the recent data and our revised assumption and judgements on future spending. Figure 5.3 shows the change in spending forecast for each of the social security payments.

Figure 5.3: Change in social security spending forecast since December 2022, by payment

£ million	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
December 2022	3,682	4,187	5,244	6,163	6,554	6,903	7,267
May 2023	3,682	4,208	5,290	6,192	6,638	7,000	7,389
Change since December 2022, of which:		21	45	30	84	97	122
Adult Disability Payment [1]		-15	24	9	46	57	62
Best Start Foods		-0	-3	-3	-0	-0	-0
Best Start Grant		-0	-0	-0	-0	-0	0
Carer's Allowance Supplement		0	-1	-1	-2	-3	-3
Carer Support Payment [2]		3	1	-9	-15	-31	-37
Child Disability Payment [3]		10	40	55	71	86	116
Child Winter Heating Assistance		1	2	2	3	3	3
Discretionary Housing Payments		-3	0	-1	-0	-0	-0
Employability Services [4]		0	-4	0	0	0	0
Employment Injury Assistance [5]		-2	-0	-1	-1	0	0
Funeral Support Payment		-2	-1	-1	-1	-1	-1
Pension Age Disability Payment [5]		18	29	32	23	21	15
Pension Age Winter Heating Payment [5]				-0	-0	-0	-0
Scottish Adult Disability Living Allowance [5]		20	-2	-10	-8	-9	-10
Scottish Child Payment		-9	-38	-41	-29	-25	-22
Scottish Welfare Fund		3	0	0	0	0	0
Self-Isolation Support Grant		-1					
Severe Disablement Allowance		-0	-0	-0	-0	-0	-0
Winter Heating Payment		-2	-1	-1	-1	-1	-1

Source: Scottish Fiscal Commission
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.
[1] Adult Disability Payment has replaced Personal Independence Payment. Figures include spending on Personal Independence Payment until case transfer is complete.
[2] Carer Support Payment will replace Carer's Allowance from spring 2024. Figures include spending on Carer's Allowance until case transfer is complete and Carer's Additional Person Payment which will be introduced after case transfer is complete.
[3] Child Disability Payment spending includes spending on the UK Government Disability Living Allowance for children, while recipients are transferred to the new payment.
[4] Employability Services is an indicative forecast and includes spending on Fair Start Scotland service and additional funding for the replacement of the devolved employability support service.
[5] Indicative forecasts including costs of assumed social security policy commitments introduced to inform the Scottish Government's Resource Spending Review in May 2022.

5.12 Figure 5.4 shows changes in spending broken down by the main drivers of the change in spending since December 2022.

Figure 5.4: Change in total social security spending forecast since December 2022

£ million	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
December 2022	3,682	4,187	5,244	6,163	6,554	6,903	7,267
Disability Payments – Higher demand		3	60	121	158	188	223
Adult Disability Payment – Reassessed from DLA		-3	-18	-39	-60	-82	-111
Adult Disability Payment – Forecast alignment		7	21	29	35	44	54
Child Disability Payment – Data updates		10	32	40	40	40	41
Carer Payments – Lower proportion of carers		-0	-17	-22	-29	-32	-35
Scottish Child Payment – Lower caseload		-9	-34	-33	-23	-20	-16
Lower inflation forecast		0	0	-78	-47	-49	-65
Population projections		-1	-4	-5	-4	-3	-2
Other changes		14	4	17	15	10	32
May 2023	3,682	4,208	5,290	6,192	6,638	7,000	7,389
Change since December 2022		21	45	30	84	97	122

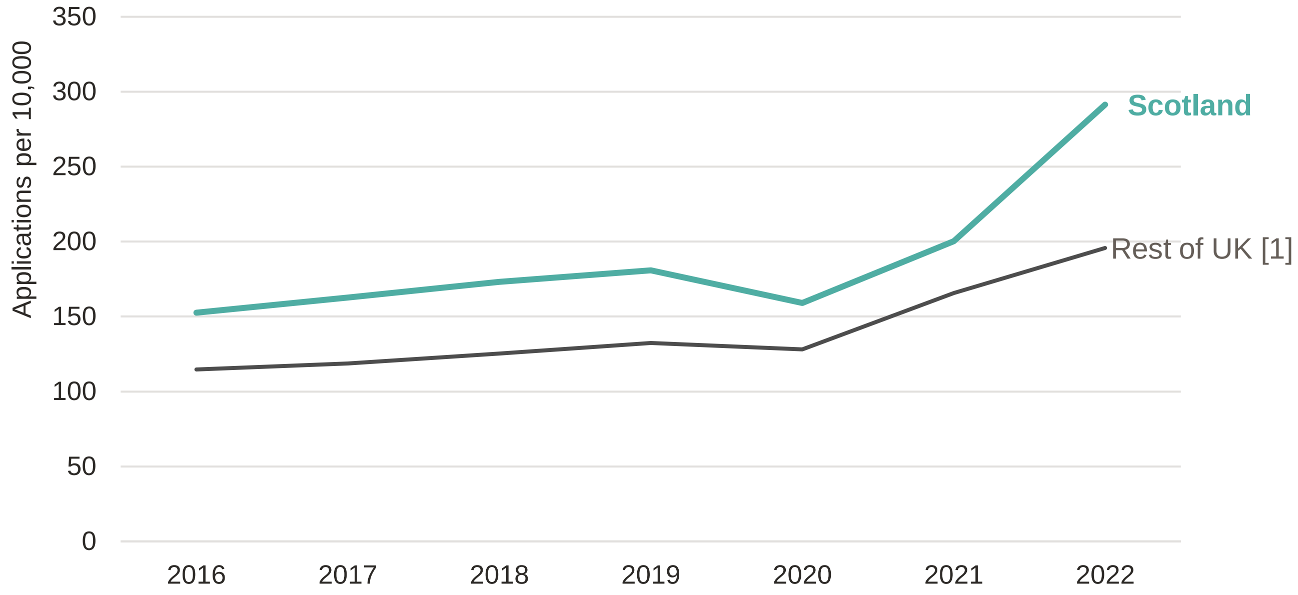
Source: Scottish Fiscal Commission
Figures may not sum because of rounding. Shaded cells refer to outturn available at time of publication.

Disability Payments – Higher demand

5.13 In our December 2022 forecast, we adjusted our Adult Disability Payment (ADP) forecast to reflect the higher number of applications for working age disability payments across the UK.

5.14 Our current assumption is that the increase in demand since 2020, shown in Figure 5.5, is the result of multiple interlinked factors. These include more people on NHS waiting lists for diagnoses and treatment, the increasing number of people economically inactive because of long-term sickness, and the financial pressures because of the current cost of living crisis. However, it is not clear of how much of the increase in demand can be attributed to each of these factors.

Figure 5.5: Applications to PIP and ADP per 10,000 of the working age population



Source: Scottish Fiscal Commission, Social Security Scotland, Office for National Statistics, Department for Communities, Department for Work and Pensions.
[1] Annual applications to PIP in Northern Ireland in 2022 are an estimate. Data are only available up to November 2022.

5.15 In our previous forecast, we adjusted the working age disability payments forecasts to reflect this higher demand. A similar increase in demand has now become clearer for children and pension age payments as well. We have increased our combined forecast for ADP, Child Disability Payment (CDP) and Pension Age Disability Payment (PADP) by £60 million in 2023-24 and £223 million in 2027-28 to reflect the higher demand for disability payments beyond the adjustments in December 2022.

5.16 We also assume that an increase in the number of people receiving disability payments will tend to lead to a higher number of people receiving carer's payments. To receive a carer's payment a person must be providing regular substantial unpaid care for a person who is in a receipt of a specific rate and component of a disability payment. The change in spending discussed in this section does not include any knock-on effect on the Carer Support Payment or Carer's Allowance Supplement.

Adult Disability Payment – Reassessed from Disability Living Allowance revision

5.17 Our ADP forecast shows the total spending expected across Personal Independence Payment (PIP) and ADP. Our ADP caseload forecast is based on our forecast of the number of people accessing the payment and those who stop receiving the payment, also known as exits. Some people in receipt of PIP or ADP have previously been in receipt of Disability Living Allowance (DLA) before moving onto PIP.

5.18 Through our review process, we identified that our forecast was potentially overestimating the number of people in this group in future years. To address this, we increased the number of exits from ADP for this group. This had the effect of reducing our forecast for the ADP caseload.

5.19 This adjustment has reduced the forecast by £18 million in 2023-24 and by £111 million in 2027-28.

Adult Disability Payment – Forecast alignment

5.20 Since the national launch of ADP in August 2022, the DWP stopped accepting Scottish applications for PIP and all new applications from people in Scotland have been made to Social Security Scotland for ADP.

5.21 The latest PIP data for Scotland show a gradual reduction in the number of successful applications to PIP as applications are now submitted to ADP. Data provided by Social Security Scotland show an increasing number of applications to ADP and case transfers from PIP. However, there are currently not enough comparable data on the approval rate of those application or their payment award to be incorporated in our ADP forecast.

5.22 To mitigate the effect of these data constraints and reflect the latest trends on adult disability payments, such as changes to exit rates or average payment award, we have used the OBR's spending forecast of PIP in England and Wales to adjust our spending forecast. This has increased our forecast by £21 million in 2023-24 and by £54 million by 2027-28.

Child Disability Payment – Data updates

5.23 In December 2022, our Child Disability Payment (CDP) forecast was based on data for DLA for children and judgements on the effect of CDP on caseload and payment awards. We were not able to incorporate data on CDP because only limited data on the benefit was available to us at the time.

5.24 Social Security Scotland has now provided the Commission with unpublished management information on the number of children in receipt of the payment and their level of awards. These data show that, compared to our forecasts from December 2022, the initial number of approved applications to CDP is higher. While there has been a relative increase in the number of approved applications receiving the highest award, this has been cancelled out by a larger increase in the number paid at the lowest rate.

5.25 We have revised our forecast to allow for a high number of approved applications with a lower average payment award in the short term to align with the latest data. In the medium term, we forecast that the number of approved applications will return to a lower level. We assume that the high level of approved applications is a temporary effect and the result of clients who may have previously marginally failed the DWP assessment process for DLA for children. Overall, we have increased our caseload forecast by 7,000 clients and our spending forecast by £41 million by 2027-28.

Scottish Child Payment – Lower caseload

5.26 In December 2022, we forecast that the total number of children receiving SCP would reach 338,000 in 2023-24. Our new forecast is around 30,000 lower for 2023-24, at 309,000 children and peaks at 315,000 in 2026-27. This reduction reflects lower assumptions for both the number of children eligible and the take-up rate for children over six.

5.27 We have lowered our estimate of the number of children that will be eligible, in response to a continued fall through late 2022 and a lower forecast for unemployment.

5.28 We have also reduced our assumed take-up rate for children aged six and over in 2023-24 from 86 per cent to 80 per cent. We assume that Social Security Scotland will be able to increase the take-up rate from this lower level, reaching 85 per cent by 2028-29.

5.29 These changes to our view of eligibility and take-up have reduced the forecast by £34 million in 2023-24 and by £16 million in 2027-28.

Carer's Payments – Lower proportion of carers

5.30 To receive a carer's payment, a carer needs to meet certain eligibility criteria, one of those being to provide regular and substantial unpaid care for a person in receipt of specific rate and components of some disability payments. Our forecast for carer's payments is based on the number of people in receipt of disability payments. First, we estimate the proportion of people in receipt of a disability payments with a carer in receipt of Carer's Allowance; then we apply our forecast of this proportion to our disability payment forecast to forecast the number of people in receipt of a carer's payment.

5.31 Recent data show that this qualifying benefit proportion has been decreasing for the working age disability population. We assess that this is partly because the new clients to disability payments tend to be less likely to have a carer in receipt of a carer's payment. Our forecast of increasing disability caseload is mainly made up of people who accessed the payments by submitting a new application rather than being transferred from legacy payments such as DLA.

5.32 We have adjusted down our forecast for the qualifying benefits proportion to reflect the increasing number of new applications in the disability payments caseload. These changes to the caseload forecast have reduced our expenditure forecast by £17 million in 2023-24 and by £35 million in 2027-28.

Inflation

5.33 We have updated our inflation assumptions from 2024-25 onwards. These are now consistent with the OBR inflation forecast published in its March 2023 Economic and Fiscal Outlook.

5.34 The largest effect in our forecast is a decrease in the uprating applied at the start of 2024-25; this is now 1.4 percentage points lower than our previous forecast. Our inflation forecast no longer has a prolonged period of deflation, we still expecting a zero uprating in 2026-27.

5.35 This update has led to a decrease of £78 million in 2024-25 and £65 million in 2027-28 through slightly lower uprating of most payments.

Population projections

5.36 Our population projections are slightly lower in the short term, but with a slightly faster growth for 2023 onwards due to using the higher migration assumption published by ONS in January 2023. This has reduced our forecast by £4 million in 2023-24 and by £2 million by 2027-28.

Other changes

5.37 Since our December 2022 publication, our models have been updated with further outturn data. We have adjusted our models to reflect the latest data and to improve the accuracy of our forecast. Together, these changes have increased our forecast by £4 million in 2023-24 and by £32 million by 2027-28.

5.38 The change in spending in 2027-28 includes the correction of an inconsistency in spending on young people in receipt of CDP. Correcting this has increased the forecast by £15 million in 2027-28.

Funding related to social security

5.39 Most social security spending is funded differently to other parts of the Scottish Budget because the Scottish Government receives Block Grant Adjustments (BGAs) from the UK Government for devolved payments. This funding is based on the UK payments they replace and does not include the effect of Scottish Government reforms. Any spending above the level of funding received through the BGAs must be met from the overall Scottish Budget.

5.40 The social security net position is the difference between our forecasts of devolved social security payments and the corresponding BGAs, derived from the OBR's forecasts of spending in England and Wales. This grows to £654 million by 2027-28. The net position reflects the higher spending on Scottish payments, such as Adult Disability Payment (ADP) or Carer Support Payment (CSP), which replace devolved UK Government benefits.

5.41 The Scottish Government has introduced new payments which are only available in Scotland such as Scottish Child Payment (SCP). The spending on these payments is forecast to increase to £620 million by 2027-28.

5.42 Combining the social security payments and the new payments introduced by the Scottish Government, the gap between the level of funding received from the UK Government and total social security spending in Scotland is forecast to widen each year, from £756 million in 2023-24 to £1,274 million in 2027-28.

Figure 5.6: Social security net position and new payments

£ million	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
Social security net position [1]	-19	-210	-369	-495	-581	-654
New social security payments [2]	-353	-546	-584	-598	-611	-620
Total	-372	-756	-953	-1,093	-1,191	-1,274

Source: Scottish Fiscal Commission

Figures may not sum because of rounding.

[1] Social security net position includes Adult Disability Payment (covered by the Personal Independence Payment BGA), Child Disability Payment and Scottish Adult Disability Living Allowance (covered by the Disability Living Allowance BGA), Pension Age Disability Payment (covered by the Attendance Allowance BGA), Carer Support Payment and Carer's Additional Person Payment (covered by the Carer's Allowance BGA), Employment Injury Assistance (covered by the Industrial Injuries Disablement Scheme BGA), Winter Heating Payment (covered by the Cold Weather Payment BGA), Pension Age Winter Heating Payment (covered by the Winter Fuel Payment BGA) and Severe Disablement Allowance (covered by Severe Disablement Allowance BGA).

[2] New social security payments include Scottish Child Payment, Carer's Allowance Supplement, Child Winter Heating Assistance, Best Start Grant Early Learning Payment and Best Start Grant School Age Payment. We also include spending through Discretionary Housing Payments on bedroom tax mitigation and the extra costs of the new commitment to mitigating Benefit Cap deductions.

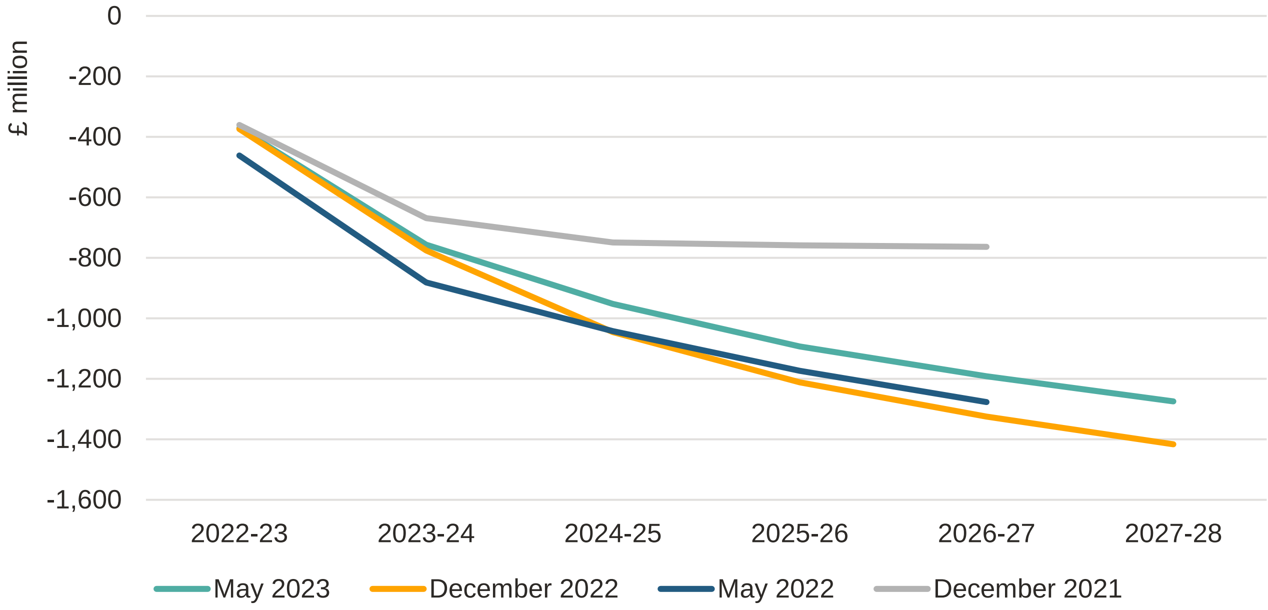
5.43 In December 2022, we reported that the gap between the estimate of the funding to be received from the UK Government and total social security spending in Scotland was forecast to be £1,416 million in 2027-28. In the current forecast, this has narrowed by £142 million to £1,274 million in 2027-28. This is mainly because the current social security net position for 2027-28 has narrowed from £775 million in December 2022 to £654 million in our May 2023 forecast.

5.44 The narrowing of the social security net position by £121 million is only a small proportion of the £7,389 million social security spending forecast in 2027-28. As the net position is calculated from our forecasts of devolved social security spending and the social security BGAs, which are based on the

OBR's forecasts of spending in England and Wales, it is sensitive to changes in both sets of forecasts.

5.45 Figure 5.7 shows the changes on the total social security net position and spending on new payment combined in the last four fiscal events. The funding gap in December 2021 was relatively narrow as it did not include the additional spending for the replacement of payments such as Pension Age Disability Payment or CSP nor the increase of SCP to £25 per week. However, while the funding gap has been variable, it has remained stable in the last three fiscal events.

Figure 5.7: Changes in total social security net position and new payments



Source: Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – December 2021 (link), Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – May 2022 (link), Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link).

Social security net position

5.46 The main drivers of the net position for social security are the changes in eligibility and operational delivery introduced for devolved payments.

Figure 5.8: Comparison of social security spending forecast and BGAs

£ million	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
Block Grant Adjustments [1]	3,343	3,728	4,434	5,132	5,435	5,697	6,003
Spending on social security payments with BGAs [2]	3,326	3,746	4,644	5,501	5,930	6,278	6,657
Net position (BGA less spending), of which:	17	-19	-210	-369	-495	-581	-654
Attendance Allowance	1	-9	3	-1	-34	-57	-72
Carer's Allowance	0	-1	-6	-25	-62	-77	-79
Cold Weather Payment		1	-17	-17	-17	-17	-17
Disability Living Allowance	16	-2	23	64	85	82	94
Industrial Injuries Disablement Scheme	1	2	-1	-2	-3	-6	-7
Personal Independence Payment	-1	-10	-213	-387	-463	-505	-569
Severe Disablement Allowance	0	0	0	0	0	0	0
Winter Fuel Payment				-1	0	-1	-2

Source: Scottish Fiscal Commission, Scottish Government.

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

[1] The latest BGA estimates are based on the OBR's March 2023 Economic and fiscal outlook (link).

[2] Our forecasts of social security spending reflect spending in Scotland on the current payments and additional spending arising from the Scottish Government's policy changes, including our indicative forecasts of future policy commitments.

5.47 The gap between the BGA funding estimate and our spending forecast on the corresponding Scottish payments mainly reflect changes in policy and policy intention for the devolved payment. Spending on social security payment with a BGA is 11 per cent higher than the corresponding funding received through the BGAs in 2027-28.

5.48 The differences for individual payments need to be carefully interpreted. These reflect:

- Our forecast of effect of the policy and operational changes in Scotland. In advance of outturn data being available on the effect of changes after implementation, our forecasts are based on judgements for the scale of the effect. We have been revising our spending forecast and adjusting our judgements as more data become available. For example, we have adjusted our judgement on the initial CDP spike to reflect the latest management information.

- We expect that the spending growth in Scotland would remain broadly consistent with the rest of the UK in the absence of policy changes. However, differences between our modelling and judgements for spending in Scotland and the OBR's forecasts for spending in England and Wales, as well as the data available, can lead to changes in the net position.

5.49 The overall net position has narrowed since the previous forecast. This is mainly because our forecast for ADP has increased by less than corresponding PIP BGA, due to revision of the DLA reassessed group and because our forecast for CSP had decreased while the Carer's Allowance BGA has increased, as we assume a lower proportion of carers since our previous forecast.

Forecast uncertainty

5.50 Our forecasts account for changes in the historical trends in the number of people in receipt of payments, their payment amount, wider changes to the population, and the economic outlook. Access to timely and relevant statistical data, firm details on future policy developments and changes that may affect the access to, or the delivery of, the payments are essential to reduce the uncertainty in our forecasts. The paragraphs below outline some of the challenges we faced in preparing these forecasts for social security spending.

Data access

5.51 Having access to high quality, consistent, and timely data is important to produce accurate forecasts. This is even more relevant in the current transition process from payments administered by the DWP to the payments administered by Social Security Scotland. While we understand that this is a challenging process as multiple operational processes to administer a new payment need to be developed; as highlighted in our Statement of Data Needs 2022, we need detailed data on all the payments administered by Social Security Scotland to produce our forecast.[50]

5.52 Since our previous forecast, the Commission has received more detailed management information from Social Security Scotland on the number of children in receipt of Child Disability Payment (CDP). This has allowed us to increase our CDP caseload and payment award forecasts to reflect the emerging trends.

5.53 At this point, the same level of detail is not available for Adult Disability Payment (ADP). The payment launched nationally in August 2022 and the data available at present are not sufficient for us to identify trends. While we adjusted our forecast to reflect the increase in disability prevalence across the UK, we have not been able to properly capture any Scotland specific change in prevalence. Social Security Scotland has indicated that it aims to provide us with the detailed data we require on ADP in advance of the next fiscal event so we can incorporate these in our forecast.

5.54 The Commission welcomes ongoing engagement with the Scottish Government and Social Security Scotland on development of statistics to support our forecast and the early engagement with the teams developing future replacement payments such as CSP or PADP to capture our forecasting data needs.

Policy developments

5.55 Forecasts for new payments are more uncertain than other parts of our forecasts as they rely more on judgements. These judgements are informed by a systematic process of consultation with policy officials and those responsible for delivery as well as by a comprehensive review of relevant data and evidence, for example, from the introduction of previous social security payments or policy reforms.

5.56 This is particularly relevant for the complex disability payments, such as ADP. Even after the payment has been introduced, the level of judgement attached to these forecasts will be high for several years. We expect spending will increase relative to what would have been spent on PIP in the absence of ADP. Our spending forecast reflects the changes the Scottish Government has made, such as seeking to improve the payment delivery in terms of support available, application process, the types of supporting information used for decision-making and appeal processes; and its

[50] Scottish Fiscal Commission (2022) Statement of Data Needs – August 2022 (link).

ambition to maximise the take-up of the payment by those eligible, whilst reflecting the new Social Security Charter.[51] The PIP BGA net position reflects the scale of the effect of the ADP policies.

5.57 Our forecasts for social security represent a central point within a broad range of possible outcomes which would vary if we altered some of our judgement. We have been refining our judgements on ADP since we produced our initial costing in August 2021. Further adjustments will be introduced to the costing as new data emerge on case transfer and the award determination process. However, it may take several years for the full effect of the reforms to be assessed.

5.58 There are several payments currently administered in Scotland by the DWP that will be transferred to be fully administered by Social Security Scotland by the end of 2025. We produced a set of indicative forecasts for these payments in our May 2022 forecast. These forecasts were developed based on Scottish Government policy intention; there have been no public announcements yet for the introduction of some of the payments and the policy details are still in development for most of them.

5.59 Our forecasts include all the measures announced in last year's Tackling Child Poverty Delivery Plan, but do not include any further measures which the Scottish Government may take to work towards its poverty reduction targets.[52]

Disability trends

5.60 As we discussed in both this chapter and our December 2022 report, there has recently been strong growth in demand for disability payments, both in Scotland and in the rest of the UK. This increase is assumed to be driven by several different factors, including the ongoing impact of the pandemic on people's physical and mental health, NHS waiting times, and cost of living pressures, which relative contribution is uncertain.[53] Furthermore, this is happening at the same time as the rollout of the new Scottish disability payments which make it very difficult to forecast how strongly this trend will continue and to what extent higher spending will be matched by higher BGA funding.

5.61 The CSP eligibility criteria require that the cared for person is in receipt of certain rates of specific components of disability payments, so the characteristics of the people in receipt of disability payment in Scotland will affect the number of clients in receipt of CSP. Because we do not have information on the characteristics of these people yet, there are certain elements of the forecast, such as the proportion of people in receipt of a disability payments with a carer in receipt of a carer's payment, which are based on judgements.

Economic outlook

5.62 As discussed in **Chapter 3**, the main area of uncertainty in our economy forecast is around inflation. Inflation has a direct impact on spending through uprating. If inflation is higher than forecast then social security spending for 2024-25 onwards would be proportionally higher and if inflation is lower spending will be lower, but the risk to the overall Scottish Budget is relatively small. Most of the change in spending would be matched by a corresponding change in the funding received through Block Grant Adjustments.

5.63 Continued high inflation could indirectly affect the social security spending if the higher cost of living drives higher take-up rates for devolved social security payments. High inflation could also lead to

[51] Scottish Government (2019) Social Security Scotland: our charter (link).
[52] Scottish Government (2022) Best Start, Bright Futures: tackling child poverty delivery plan 2022 to 2026 (link).
[53] In **Chapter 3**, we discuss how there is uncertainty in the survey-based measurement of levels of economic inactivity and ill-health in Scotland relative to the rest of the UK.

higher numbers of people becoming eligible for low-income payments through increased receipt of qualifying benefits like Universal Credit.

5.64 We have reduced our forecasts for spending on the Five Family Payments to reflect a lower unemployment forecast, but there is still significant uncertainty. Higher unemployment or a weaker economy could also lead to higher social security spending than we currently forecast.

Annex A
Policy Costings

Policy Costings

Introduction

A.1 This annex sets out the steps and judgments taken to arrive at our costings of changes in Scottish Government policy since our December 2022 forecasts were published.[54]

New Policy Costings

A.2 Figure A.1 shows a summary of new policy costings included in our forecasts. Negative values represent lower tax revenues or higher social security spending. Positive values represent higher tax revenues or lower social security spending. In the later sections covering the individual policy measures, social security changes are shown as positive if they increase spending.

Figure A.1: Policy costings summary

£ million	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Non-Domestic Rates: New entry parks transitional relief	-4	-2	0	0	0	0
Land and Buildings Transaction Tax: Increase in ADS repayment period	1	5	2	-5	-5	-6
Social Security: Introduction of Carer Support Payment		-15	-52	-70	-73	-76

Source: Scottish Fiscal Commission

[54] Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link).

Taxes

Title of measure

Non-domestic rates – New entry parks transitional relief

A.3 A transitional relief has been created for properties in parks that are new entries on the 2023 valuation roll[55]. These properties located within parks or parts of parks were previously exempt from rating, but have been added to the 1 April 2023 valuation roll. They will receive a transitional relief that reduces their gross bill by 67 per cent in 2023-24 and 33 per cent in 2024-25.

A.4 The relief amount was calculated by finding the eligible properties on the 2023 valuation roll and using the rateable values of those properties and the relief terms to calculate the amount of relief those properties were eligible for.

Figure A.2: Cost of transitional relief for new entry parks properties

£ million	2023-24	2024-25	2025-26	2026-27	2027-28
New entry parks transitional relief	-4	-2	0	0	0

Source: Scottish Fiscal Commission

Title of measure

Increase in the Additional Dwelling Supplement repayment period

Measure Description

A.5 Additional Dwelling Supplement (ADS) is chargeable when a residential property is bought for over £40,000 when the buyer already owns other residential property and the main residence has not been replaced. The buyer can reclaim the ADS if a previous main residence is sold within a given period of time.

A.6 The Scottish Government will increase the timelines applying to the ADS, including the repayment timelines from 18 months to 36 months. We expect that this will be implemented in Autumn 2023.

The costing

A.7 Our costing in Figure A.3 shows that an increase in the timelines applying to the ADS, including the repayment timelines will mean a short-term reduction in ADS repayments, leading to more ADS revenue between 2023-24 and 2025-26.

Figure A.3: Impact of increase in timelines applying to the Additional Dwelling Supplement (ADS), including repayment timelines from 18 months to 36 months

£ million	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Change in LBTT revenue	1	5	2	-5	-5	-6

Source: Scottish Fiscal Commission

[55] The Non-Domestic Rates (Transitional Relief) (Scotland) Regulations 2023 (link).

A.8 The expected decrease of repayments of the ADS towards the beginning of the repayment timeline is based on an assumption that people will take longer to sell additional properties now they have a longer period in which to do so.

A.9 We are costing an increase in overall ADS repayments as we expect more people will reclaim the ADS over a 36-month timeline than we do over an 18-month timeline. This increase in repayments takes a few years to take effect in our forecast and we expect LBTT revenue to fall from 2026-27 onwards.

Social Security

Title of measure

Introduction of Carer Support Payment

Measure Description

A.10 Carer Support Payment (CSP) will replace Carer's Allowance (CA) in Scotland, as a pilot at the end of 2023 and nationally from spring 2024. The new payment will continue to provide financial assistance to people who provide regular and substantial unpaid care for people with disabilities.

A.11 In our previous forecasts, we published indicative forecasts to support the Scottish Government's multi-year Resource Spending Review, which included Carer Support Payment forecast.[56,57] This policy costing is an update to the indicative forecasts and is produced using confirmed policy details such as launch dates for CSP and timings for some of the proposed policy changes. The policy costing also updates some of the assumptions using recently published outturn data.

A.12 Currently, carers who meet the eligibility criteria can apply and receive CA, delivered by the Department for Work and Pensions (DWP).[58] Additionally, carers who receive CA in Scotland are entitled to and receive Carers Allowance Supplement (CAS). CAS is paid biannually by Social Security Scotland using information on people living in Scotland and receiving CA on a specific qualifying date, with no need to apply separately.

A.13 From launch, eligibility for CSP will broadly be aligned with CA to allow the transfer of the awards for people in Scotland receiving Carer's Allowance onto Carer Support Payment. The introduction of CSP will include policy changes that will broaden eligibility to receive a payment. From the national launch of CSP, the Scottish Government will introduce changes to eligibility for carers who study full-time. Also introduced at the national launch will be changes to the past presence test to align with that for disability payments in Scotland which allows people moving to Scotland from outside the Common Travel Area to access support quicker.

A.14 Transferring awards for people receiving CA in Scotland from the DWP to Social Security Scotland and onto CSP is a joint programme with the DWP aimed at ensuring that improvements are available to everyone at the same time, avoiding a 'two-tier' system of entitlement. Timings for the completion of case transfer are still being finalised, but from discussions between the Scottish Government and the DWP, the current intention is that case transfer will begin at national launch and be completed by the end of 2024.

A.15 The Scottish Government has stated that once the case transfer is completed and as soon as practicable, additional changes that broaden eligibility for payment will be introduced. These changes include:

- increase of the earnings limit;

[56] Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – May 2022 (link), Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link).
[57] We published our indicative forecast for carer's payments under the working title of 'Scottish Carer's Assistance'. The Scottish Government announced in February 2023 that the name for the replacement carer's payments would be Carer Support Payment: Scottish Government (2023) Carer Support Payment to be piloted by the end of this year (link).
[58] UK Government, Carer's Allowance (link).

- extending period of payment after the death of a cared for person;
- extending period of payment if a cared for person is admitted to a hospital or care home;
- allowing carers to add together hours spent caring for more than one person;
- providing Short-term Assistance (STA) for carers.

A.16 The Scottish Government also plans to introduce Carer's Additional Person Payment (CAPP) which will provide additional support for carers who receive CSP and are caring for more than one person who receives a qualifying disability payment. CAPP will also be introduced as soon as practicable after the completion of case transfer.

A.17 Initially Carers Allowance Supplement (CAS) will continue to be paid separately from the main CSP, however following the public consultation, the Scottish Government plans to change this in future and to pay CAS alongside regular payments of CSP. Timing for the changes to CAS are being considered as part of wider work on future changes to CSP and the delivery of CAPP. In this report, we treat CAS as a separate payment to CSP.

A.18 Details of the policy changes and how we have forecast spending are set out below. Full details on CSP can be found in the Scottish Government's Scottish Carer's Assistance consultation response, policy note and draft legislation.[59]

The cost base

A.19 The cost base is the number of people that will be affected by the proposed changes to be introduced through CSP policy. We show the number of people receiving carer's payments in Scotland and how this will change with the introduction of the CSP from 2024-25.

A.20 The baseline caseload is calculated using historical data of the proportion of people receiving a specific rate and component of the qualifying disability payments that have an eligible carer in receipt of Carer's Allowance.[60] Our baseline caseload is the number of people receiving Carer's Allowance (CA) and Carer's Allowance Supplement (CAS), in the absence of CSP.

A.21 The introduction of the new payment with broader eligibility might lead to an increased number of additional applications from new clients or clients who were previously not eligible for CA and CAS.

A.22 To calculate the effect of the new policy on the caseload, we estimate the additional number of people who would receive CSP when the policy and operational changes are introduced. The combined caseload in turn will determine the spending forecast for CSP. We consider the effects of the policy changes on eligibility from reducing restrictions on carers in full-time education, extending period of support after the death of a cared for person or if they are admitted into a hospital or care home, changing the earnings limit, and allowing carers to add together hours of care for more than one person.

A.23 We have used data on number of students by age band from Scotland's Census 2011 and information on carers from Family Resources Survey (FRS) to estimate the number of students who

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[59] Scottish Government (2023) The Carer's Assistance (Carer Support Payment) (Scotland) Draft Regulations 2023: policy note (link), Scottish Government (2023) The Carer's Assistance (Carer Support Payment) (Scotland) Draft Regulations 2023 (link), Scottish Government (2022) Scottish Carer's Assistance consultation: Scottish Government Response (link).
[60] Scottish Fiscal Commission (2021) How we forecast social security: disability and carer's payments (link).

are eligible for CSP. We estimate that on average this change to the eligibility will result in an increase in the overall caseload by an average of 1,500 people.

A.24 We also have used FRS estimates to inform our assumptions about the number of people who become eligible for the payment when the earnings limit is changed and the number of people who provide care for more than one person to estimate the number of people eligible for Carer's Additional Person Payment (CAPP).

A.25 Figure A.4 shows the estimated number of people to receive CSP and CAPP as an addition to the baseline caseload from CA and CAS.

Figure A.4: **Number of people forecast to receive Carer Support Payment (CSP) and Carer's Additional Person Payment (CAPP)**

Thousands	2024-25	2025-26	2026-27	2027-28	2028-29
Baseline CA (and CAS) caseload [1]	100	105	109	114	118
Additional CSP caseload, of which:	4	8	12	12	12
Reduction of restrictions for carers in full-time education	2	2	2	2	2
Higher earnings limit		2	4	5	5
Additional applications	2	4	6	6	6
CAPP caseload [2]		17	18	19	20

Source: Scottish Fiscal Commission
Figures may not sum due to rounding.
[1] Everyone who receives Carer's Allowance (CA) in Scotland also receives Carer's Allowance Supplement (CAS). We assume that all the additional caseload from Carer Support Payment (CSP) changes will also receive CAS.
[2] To receive CAPP the applicant must already be receiving CSP so the CAPP caseload is already included in the additional CSP total.

The costing

A.26 This section presents our estimate of how spending on carer's payments will change when Carer Support Payment (CSP) is introduced. We start from our forecast of the baseline Carer's Allowance (CA) and Carer's Allowance Supplement (CAS) spending and caseload estimate.

A.27 As discussed in the section on the cost base, we assume that the changes introduced through the CSP policy will increase the number of people who apply and receive the payment. This increase in the caseload will result in additional spend on CSP and CAS of £15 million in 2024-25 and £76 million by the end of the forecast period in 2028-29. Further, the introduction of Carer's Additional Person Payment (CAPP) to support carers who already receive CSP and provide care to more than one person will lead to an additional increase in spending, but not the caseload. Figure A.5 shows a summary of the estimated cost of the introduction of CSP and CAPP.

Figure A.5: **Overall policy costing for Carer Support Payment (CSP)**

£ million	2024-25	2025-26	2026-27	2027-28	2028-29
Baseline spending, of which:	471	494	515	542	571
CSP Baseline (CA)	415	436	454	478	503
CAS Baseline	56	58	61	64	68
Additional CSP, of which:	15	52	70	73	76
Additional CSP	13	38	54	56	59
Additional CAS	2	5	7	7	7
CAPP		9	9	10	10
Total carer's payments spending	486	546	585	615	647

Source: Scottish Fiscal Commission
Figures may not sum due to rounding.

A.28 The Scottish Government will run a pilot for CSP from winter 2023. This has not been included in our costing as the scale of the pilot is currently unclear. However, we assume it will focus on operational delivery and not have a material effect on our forecast as it will likely to be implemented at a small scale and only cover the last quarter of the year.

A.29 The Scottish Government has committed to launch CSP nationally in spring 2024, so in preparing this costing we assume that CSP is fully launched from April 2024 when new CA claims will stop being accepted by the DWP and clients will instead be directed to apply to Social Security Scotland for CSP.

A.30 Once CSP has fully launched, the payments for people receiving CA will gradually be transferred from the DWP systems to Social Security Scotland. This is referred to as the case transfer process. Timings for the completing of case transfer are still being finalised, but following discussions with the Scottish Government we assume that case transfer will begin at national launch in April 2024 and be completed by the end of 2024.

A.31 Figure A.6 shows the breakdown of the policy costing for CSP by additional spending for carer's payments from each of the policy changes we have considered, as well as the introduction of CAPP. These policy changes will be implemented after the case transfer is completed, except for the reduction of restrictions for carers in full-time education which will be introduced at the national launch.

Figure A.6: Breakdown of the additional CSP policy costing

£ million	2024-25	2025-26	2026-27	2027-28	2028-29
Additional CSP policy costing, of which:	15	52	70	73	76
Reduction of restrictions for carers in full-time education	5	7	7	7	7
Higher earnings limit		10	21	22	23
Other eligibility changes [1]		5	5	5	5
Additional applications	10	21	28	29	30
Carer's Additional Person Payment		9	9	10	10

Source: Scottish Fiscal Commission

Figures may not sum due to rounding.

[1] Other eligibility changes include extension of period of support after the death of a cared for person or if the cared for person is admitted to a hospital or care home from eight to 12 weeks; allowing carers to add together hours spent caring for more than one person and adding Short-term Assistance (STA) to CSP qualifying payments.

Reduction of restrictions for carers in full-time education

A.32 The Scottish Government plans to reduce restrictions for carers studying more than 21 hours a week who are currently not eligible for Carers Allowance (CA) on the basis that financial support for full-time students is separate from the current benefits system. The Scottish Government plans to introduce this change when CSP is launched nationally in spring 2024. This change will bring eligibility in line with that for carers who study for less than 21 hours.

A.33 We have used Scotland's Census 2011 data to calculate students providing care for at least 35 hours and Family Resource Survey (FRS) data on care recipients receiving the relevant qualifying disability payments to estimate the proportion of the population that are students eligible for CA. We have applied this proportion to our population projections to estimate the number of people in full-time education that are eligible for CA.

A.34 We estimate that, on average, this change to the eligibility will increase the overall caseload and would increase spending by £5 million in 2024-25 and £7 million by the end of forecast period in 2028-29.

Higher earnings limit

A.35 To receive Carer's Allowance, a carer who meets the other eligibility criteria should also not be earning more than £139 per week (in 2022-23) after tax, National Insurance and expenses from employment. Following the Scottish Carer's Assistance consultation, the Scottish Government is considering changing the earnings limit for carers receiving CSP and for it to be linked to a specific rate, such as the Real Living Wage.[61]

A.36 Using the 2021-22 level of the Real Living Wage (RLW), which is £9.90 an hour, working 16 hours per week would increase the earning limit to £158 per week, compared to the 2021-22 earnings limit of £132 per week.[62] Policy for changes to the earnings limit is still being finalised, so we assume that the earnings limit will change as the RLW changes. The RLW rate is not determined by Scottish

[61] Scottish Government (2022) Scottish Carer's Assistance consultation: Scottish Government response (link).

[62] The CSP policy proposals are based on the 2021-22 RLW and earnings limits. The current applicable rates in 2022-23 are £10.90 for the RLW and the earnings limit is £139 per week.

Ministers, but we assume that it is changed to reflect inflation, so in turn we assume that the earnings limit for CSP will be uprated in line with inflation.[63]

A.37 Based on Family Resources Survey (FRS) data we estimate that spending on CSP would increase by about £10 million in 2025-26 up to £23 million by 2028-29 if the earnings limit is linked to the Real Living Wage.

Other eligibility changes

A.38 Once the transfer of cases from Carer's Allowance (CA) to CSP is complete and as soon as practicable, the Scottish Government has indicated plans to introduce further changes to eligibility for CSP. We have grouped these proposed changes and assess their impact together. These changes include:

- extending period of support after the death of a cared for person from 8 to 12 weeks;
- extending period of support if the cared for person is admitted to a hospital or care home from 4 weeks to 12 weeks;
- allowing carers to add together hours spent caring for more than one person who receives the qualifying disability payments and claim CSP if their total hours of care meet the eligibility criteria;
- adding Short-term Assistance (STA) as a qualifying benefit for Carer Support Payment;[64]
- introducing changes to past presence test for carers to align with that for disability payments in Scotland which allows people moving to Scotland from outside the Common Travel Area to access support quicker. Note that the change to past presence test will be introduced at the national launch in spring 2024, while other eligibility changes will be implemented after the completion of case transfer.

A.39 We estimate that these changes will individually have a non-material effect on the caseload and expenditure forecasts. Based on the limited evidence available, we have made a judgement to increase our spending forecast by £5 million annually from 2025-26 to account for the total effect of these changes.[65]

Additional applications

A.40 The Scottish Government is committed to maximising the take-up of Scottish social security payments, as set out in a series of Benefit Take-up Strategies, the latest of which was published in October 2021.[66] There are also changes in the delivery of CSP in terms of the support available to people to encourage applications and how the payment is advertised and promoted. Through these changes the Scottish Government intends to encourage more people who are eligible for support to

[63] Real Living Wage for 2022-23 was announced in September 2022 which increased the rate to £10.90 per hour: Living Wage Scotland – The real Living Wage for the real cost of living (link). We have used the 2021-22 RLW rate to align with the current CSP policy proposal, see Scottish Government (2022) Scottish Carer's Assistance consultation: Scottish Government response (link).

[64] In the Scottish social care system, Short-term Assistance (STA) provides financial support for people while they challenge a decision to reduce or stop ongoing payment of certain devolved payments. For CSP, STA will be paid in situations where a CSP decision is being challenged and also when the cared for person is challenging a decision and receiving STA on the disability payment they receive.

[65] Currently we do not have sufficient data on number of deaths of cared for person, or admissions to a hospital or care home of cared for person, or data on hours of care for carers who are not currently eligible for the CA but may become eligible for CSP if they add together hours of care for multiple people.

[66] Scottish Government (2021) Social Security (Scotland) Act 2018: benefit take-up strategy – October 2021 (link).

apply for the payment. We expect the proposed changes will increase the number of people receiving payment.

A.41 We also expect that the introduction of the changes under CSP may involve some degree of behavioural change. For example, the option to work 16 hours at the Real Living Wage might lead people who do not meet the eligibility criteria at the current earnings limit to change their working arrangements so that they are able to provide unpaid care and apply for payment at the higher earnings limit.

A.42 We estimate that these factors will result in more people applying for and receiving CSP and subsequently we have adjusted the caseload to account for this. We assume the increase in caseload will grow gradually after the introduction of CSP. We have increased the caseload forecast by 2 per cent in 2024-25 at the launch of the payment and rising to 5 per cent by the end of forecasting period in 2028-29. This increases our spending forecast by £10 million in 2024-25 to £30 million by the end of the forecasting period in 2028-29.

Carer's Additional Person Payment

A.43 The Scottish Government plans to introduce Carer's Additional Person Payment (CAPP) to support carers providing care to more than one person receiving disability payments.

A.44 To receive CAPP, carers must be in receipt of CSP and provide care for at least another person who is in receipt of a qualifying disability payments and should be providing at least 20 hours of care a week for each additional person they are applying for CAPP for.

A.45 The payment amount for CAPP will be the equivalent of £10 per week for each additional person cared for and will be uprated each year using the same measure of increases in costs used for other Scottish payments. CAPP will be launched after the case transfer process is completed.

Uncertainty in the costing

A.46 Modelling new payments is challenging and especially when it involves a process of transition between different systems such as the case transfer process from the DWP to Social Security Scotland. Inevitably this costing is largely based on a number of judgements and has a degree of uncertainty. The main source of uncertainty comes from the absence of historical data on some of the aspects being introduced under CSP, how the policy changes will be implemented, and the potential behavioural response to the changes introduced. We have drawn on the evidence of the higher number of approved applications from other replacement payments in Scotland such as Child Disability Payment and Adult Disability Payment, though these are not fully comparable to CSP. We have also consulted with officials from the Scottish Government and Social Security Scotland involved with introducing the new payment to inform these judgements.

A.47 Should any of the judgements and assumptions that we have based the costing on turn out to not be correct, then there is a risk that the costing may be too high or too low. Once CSP has launched and we start to receive data from its operation, we will be able to base the forecasts on information on how the policy is operating in practice and so our future forecasts will become less dependent on judgements.

A.48 The Scottish Government has confirmed that CSP will be launched nationally in spring 2024. Without details of a specific date, for the purpose of our forecast we have assumed that CSP will launch on 1 April 2024. Any variation from the assumed start date will affect spending and the scale of the effect depends on the length of variation. Additionally, a number of the eligibility changes, as well as the introduction of Carer's Additional Person Payment (CAPP), are planned to be implemented after the case transfer process has completed. We have assumed that case transfer will be completed by end of 2024 and that the proposed policy changes are implemented from 2025-26. Delays to introducing these changes will also affect our estimate of the associated additional spending.

A.49 Our estimation of the impact on spending of the proposed change to earnings limit is based on the 2021-22 Real Living Wage (RLW) rate of £9.90 per hour in line with CSP policy proposal. In September 2022 the Living Wage for 2022-23 was announced, increasing by 10.1 per cent to £10.90 per hour in line with the September 2022 CPI inflation rate. We have assumed that the RLW and the earnings limit for CSP will be uprated in line with inflation for rest of the forecast. If there was a policy to uprate the earnings limit by a factor different from inflation, this would affect our costing of the additional cost to CSP from this change.

Annex B
Policy Recostings

Introduction

B.1 In this section we present updated versions of previous policy costings for which we do not yet have outturn data that include the effects of the policy. For example, changes made to income tax in 2023-24 will not be present in the data until summer 2025.

B.2 We may also sometimes present updated costings for older policies if we have revised key judgements or assumptions, particularly in response to new evidence.

Policy recostings

B.3 Figure B.1 shows the latest recostings. Tax measures are shown as a positive figure where they generate additional revenue and negative if they reduce revenue. Social security costings are shown as positive if they reduce spending and negative if they increase spending.

Figure B.1: Latest policy recostings

£ million	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Income tax: Changes in AR threshold and rate, HR threshold freeze and rate, Basic and Starter rate band freeze	4	133	147	157	168	181	195
Income tax: Higher rate threshold freeze in 2022-23 [1]	109	105	148	131	98	115	137
NDR: Raising Higher Property Rate	0	-1	-2	-2	-1	-1	-1
NDR: Poundage freeze	0	-305	-307	-305	-328	-322	-326
NDR: Transitional relief (universal)	0	-69	-17	-4	0	0	0
NDR: SBBS changes	0	56	60	59	59	60	61
NDR: Transitional relief (SBBS)	0	-38	-37	-32	0	0	0
LBTT: Increase of ADS from 4 per cent to 6 per cent	12	35	28	34	38	38	34
Scottish Child Payment increase to £20 per week	-96	-181	-192	-195	-196	-195	-196
Scottish Child Payment increase to £25 per week [2]	-30	-49	-51	-51	-52	-52	-52
Benefit Cap mitigation	-1	-3	-7	-8	-9	-10	-13
Remove Best Start Foods income thresholds [3]		0	-3	-6	-6	-6	-6
Changes to Self-Isolation Support Grant in May 2022	16						

Source: Scottish Fiscal Commission

[1] The higher rate threshold freeze in 2022-23 was costed against a baseline of thresholds increasing with inflation. This recosting uses the same baseline but updated with the latest inflation figures. New policies are costed against a baseline with the higher rate threshold frozen at the 2021-22 level.

[2] Costing for increasing Scottish Child Payment to £25 now includes the full cost of increasing the rate in November 2022 rather than April 2023, some of which was originally included in the costing of the £20 rate.

[3] Best Start Foods income thresholds are now expected to be removed from February 2024.

B.4 Figure B.2 then shows the change since the versions which were presented in either Annex A or Annex B of our December 2022 forecast publication.[67]

Figure B.2: Change since last costing

£ million	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
Income tax: Changes in AR threshold and rate, HR threshold freeze and rate, Basic and Starter rate band freeze	0	4	5	6	6	6
Income tax: Higher rate threshold freeze in 2022-23 [1]	2	4	52	28	-16	-10
NDR: Raising Higher Property Rate	0	0	0	0	0	0
NDR: Poundage freeze	0	3	3	2	-4	-5
NDR: Transitional relief (universal)	0	-9	-2	-2	0	0
NDR: SBBS changes	0	2	3	3	0	3
NDR: Transitional relief (SBBS)	0	2	1	1	0	0
LBTT: Increase of ADS from 4 per cent to 6 per cent	0	0	0	0	-1	-2
Scottish Child Payment increase to £20 per week	3	16	17	12	10	9
Scottish Child Payment increase to £25 per week [2]	2	5	5	4	3	3
Benefit Cap mitigation	0	1	2	1	1	2
Remove Best Start Foods income thresholds [3]		3	2	0	0	0
Changes to Self-Isolation Support Grant in May 2022	0					

Source: Scottish Fiscal Commission

[1] The higher rate threshold freeze in 2022-23 was costed against a baseline of thresholds increasing with inflation. This recosting uses the same baseline but updated with the latest inflation figures. New policies are costed against a baseline with the higher rate threshold frozen at the 2021-22 level.

[2] Costing for increasing Scottish Child Payment to £25 now includes the full cost of increasing the rate in November 2022 rather than April 2023, some of which was originally included in the costing of the £20 rate.

[3] Best Start Foods income thresholds are now expected to be removed from February 2024.

[67] Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link).

Annex C
Materiality and Policy Costings

Introduction

C.1 Some policies announced by the Scottish Government will have a very small effect relative to the Scottish Budget. The Commission publishes detailed information on policies which have a material effect on the Scottish Budget in **Annex A**. This annex covers the policies which do not have a detailed costing, some of which are still included in our forecasts. We explain the approach for each policy below.

C.2 Our approach to materiality was introduced in our December 2018 Scotland's Economic and Fiscal Forecasts publication. We reviewed our materiality policy and set out increased materiality thresholds in Annex C of our January 2021 Scotland's Economic and Fiscal Forecasts report.[68] In February 2023 we reviewed our materiality policy again and decided to keep the current thresholds unchanged. We plan on reviewing our materiality policy every two years.

C.3 We also consider materiality in our approach to error correction, published in our statement of compliance with the Code of Practice for Statistics.[69] We categorise errors based on materiality and then use this to help us decide on an appropriate response.

Materiality policy

Negligible policies

C.4 The Commission has set thresholds under which policies will not be costed. The threshold for negligible policies is £2 million.

Small policies

C.5 For policies over £2 million but under a threshold of £5 million a decision will be made whether to cost the policy or not.

C.6 Our criteria for when not to cost a small policy require some, or all, of the following:

- a high degree of confidence that the cost of the policy is low, even if there is a high degree of relative 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 We also consider the level of political and media interest in our decision whether to cost a policy.

[68] Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – January 2021 (link).
[69] Scottish Fiscal Commission (2022) Statement of Voluntary Compliance with the Code of Practice for Statistics and Error Policy (link).

Materiality decisions for May 2023

C.8 Since we published our December 2022 forecasts, the Commission has decided not to produce costings for the following policy changes.

C.9 Firstly, some small policies are judged not to be material and are not shown in **Annex A** but are still included in our forecasts. This is typically because they are simple to model. For example, the decision to uprate some of the smaller Social Security Scotland payments by 10.1 per cent from April 2023. The small measures included in this forecast are as follows:

- Removal of Reverse Vending Machines from the NDR valuation roll. These were previously eligible for NDR relief, so the change has no impact on the overall forecast.

C.10 The second category is changes which we judge to be materially small or negligible and for which there is no estimate included in our forecast. These are:

- Amendments to the LBTT Additional Dwelling Supplement (ADS) which will have a negligible effect on overall ADS revenue:
    - Relief from residential LBTT, including ADS for local authority purchases for affordable housing purposes. As the maximum cost of relief would not be more than total residential LBTT liabilities by local authorities and that figure has historically been below our materiality threshold we have not costed this amendment.
    - Provisions in ADS to address potential unfair outcomes in existing legislation where there are joint buyers.
    - ADS relief in the event a property is inherited after missives have been signed on a new property.
    - AN exemption for ADS where a taxpayer acquires or holds an interest in a property valued at less than £40,000.
    - Relief from ADS where a new property is purchased and an interest in a previous main residence is required to be retained by court order or separation agreement.
- Introduction of a LBTT Green Freeports relief, applying to non-residential LBTT. We expect that transactions in new green freeports will mostly involve leases which only represents a small fraction of non-residential LBTT revenues with any land potentially available for sale being of minimal value. As the majority of non-residential LBTT revenue is collected from the higher end of conveyances we have assumed this policy will be below our materiality threshold and we have made no formal costing.
- In May 2023 the Scottish Government laid emergency legislation relating to the Sudan conflict to ensure that affected arriving individuals could access devolved social security assistance without having to meet the habitual residence or past presence test requirements.[70] We have not produced a policy costing as based on an initial review of the information available the effect of the change is likely to fall below our materiality threshold of £5 million in annual expenditure.

70 Scottish Government (2023) – The Social Security (Residence Requirements) (Sudan) (Scotland) Regulations 2023 (link).

Assessing cumulative materiality

C.11 One of the criteria for deciding whether or not to cost small policies is to check if the cumulative changes would be above our materiality threshold. We also keep under review the policies we have previously not costed to ensure that none of these are now above the thresholds.

C.12 In Figure C.1 we show all of the materiality decisions we have made since we introduced our original materiality policy in December 2018.

Figure C.1: Policies not costed since December 2018

Policy	Description and reason not to cost	Timing of original decision
NDR relief for day nurseries	Indefinite extension of the Non-Domestic Rates relief for day nurseries beyond June 2023. Our baseline assumption was that the relief would continue, so this did not change our forecast.	Scotland's Economic and Fiscal Forecasts December 2022
NDR relief for Enterprise Areas	Non-Domestic Rates Enterprise Areas relief was extended by one year to the end of March 2024. Our baseline assumption was that the relief would continue, so this did not change our forecast.	Scotland's Economic and Fiscal Forecasts December 2022
NDR changes to Business Growth Accelerator and Fresh Start Relief	There were small changes to Business Growth Accelerator Relief and Fresh Start Relief in Non-Domestic Rates (including an increase in the rateable value upper threshold to be eligible for this relief, from £95,000 to £100,000), which will allow relief to continue while taking into account revaluation.	Scotland's Economic and Fiscal Forecasts December 2022
Self-Isolation Support Grant increase	The Self-Isolation Support Grant was increased from £225 to £250 in October 2022 and continued to be available beyond the October 2022 end date we had assumed in earlier forecasts. This slightly increased spending in 2022-23.	Scotland's Economic and Fiscal Forecasts December 2022
Change in eligibility Winter Heating Payment	There is a small change in Winter Heating Payment, from removing restrictions on eligibility for people who live in alternative accommodation such as care homes. This change was introduced in regulations laid on 16 November 2022 and we forecast that it would increase our caseload forecast, however the value would be below our materiality threshold.	Scotland's Economic and Fiscal Forecasts December 2022
CPI uprating for BSF, BSG, CWHA and WHP	From Apri 2023, Best Start Foods, Best Start Grant, Child Winter Heating Assistance and Winter Heating Payment were all uprated in line with CPI inflation of 10.1 per cent. In isolation each of these upratings was below our materiality threshold.	Scotland's Economic and Fiscal Forecasts December 2022
NDR exemptions for onsite renewable energy generation	Non-Domestic Rates rating exemptions introduced for prescribed plant and machinery used in onsite renewable energy generation and storage in Scotland from April 2023.	Scotland's Economic and Fiscal Forecasts December 2022

Figure C.1 (continued): Policies not costed since December 2018

Policy	Description and reason not to cost	Timing of original decision
End of Self-Isolation Support Grant	The Scottish Government announced on 7 December 2022 that the payment would stop in January 2023. This announcement came after we had finalised our December 2022 forecasts and slightly reduced spending in 2022-23.	Scotland's Economic and Fiscal Forecasts December 2022
6 per cent uprating	Our May 2022 forecasts included the small costs associated with the March 2022 decision to uprate several social security payments by 6 per cent from April 2022.	Scotland's Economic and Fiscal Forecasts May 2022
Voluntary DLA transfers	In May 2022 the Scottish Government introduced regulations which included provision to enable people receiving Disability Living Allowance who were under 65 when Personal Independence Payment was introduced to voluntarily request a transfer to Adult Disability Payment. The costs were included in our forecast and were estimated to be less than £5 million.	Scotland's Economic and Fiscal Forecasts May 2022
Automation of Best Start Grant	Our May 2022 forecasts included the small costs of automating some Best Start Grant payments to families already receiving Scottish Child Payment.	Scotland's Economic and Fiscal Forecasts May 2022
Child Winter Heating Assistance eligibility for ADP recipients	Child Winter Heating Assistance eligibility was extended to some younger Adult Disability Payment recipients. The small costs were included in our forecast.	Scotland's Economic and Fiscal Forecasts May 2022
Changes to Self-Isolation Support Grant eligibility in late 2021 and early 2022	There were several changes to eligibility criteria in response to the Omicron wave of the pandemic. It is possible that some of these individually had a material impact, but they were all superseded by the new system introduced in May 2022 and we did not attempt to produce costings.	Scotland's Economic and Fiscal Forecasts May 2022
Ukraine regulations	Emergency legislation in March 2022 allowed people fleeing Ukraine to access benefits without meeting all the usual residence requirements. We now think it is possible that this will have a material effect given the large numbers of people who have arrived under the Ukraine visa schemes.	Scotland's Economic and Fiscal Forecasts May 2022
Miscellaneous changes to the Five Family Payments	Regulations laid in September 2022 included various changes to eligibility criteria. We assessed these as having negligible costs, based on draft regulations.	Scotland's Economic and Fiscal Forecasts May 2022
Best Start Foods eligibility during pregnancy	Regulations clarified the eligibility criteria for Best Start Foods during pregnancy in cases where a partner or appointee makes the claim. We estimate that this has negligible costs.	Scotland's Economic and Fiscal Forecasts May 2022

Figure C.1 (continued): Policies not costed since December 2018

Policy	Description and reason not to cost	Timing of original decision
Non-Domestic Rates solar panel relief	Business Growth Accelerator relief was extended to give full relief to any rise in rateable value from installing solar panels. We estimated that the value of this relief would be negligible.	Scotland's Economic and Fiscal Forecasts December 2021
Child Winter Heating Assistance eligibility for PIP recipients	Eligibility was extended to include some Personal Independence Payment recipients. We included the costs in our forecast, but they were below our negligibility threshold.	Scotland's Economic and Fiscal Forecasts December 2021
Best Start Foods thresholds uprated	The income thresholds for Best Start Foods eligibility rose in line with the National Living Wage. We estimated the costs were negligible.	Scotland's Economic and Fiscal Forecasts December 2021
Child Winter Heating Assistance uprating	An uprating of 6 per cent was announced for April 2022. We included the higher rate in our forecast, but the cost is negligible.	Scotland's Economic and Fiscal Forecasts December 2021
Afghan residence requirements	Residence requirements were changed so people evacuated from Afghanistan could access devolved social security assistance. We estimated that this would not have material costs.	September 2021
Best Start Foods – increase to £4.50	The weekly value was increased from August 2021 and the income thresholds were uprated. We included the small costs in our August 2021 forecast.	May 2021
Non-Domestic Rates – Local Authority Discretionary Sports Club Relief	A costing of £3 million was included in the Barclay Review of Non-Domestic Rates. We estimated that this policy change fell below our £5 million threshold for small policies.	Scotland's Economic and Fiscal Forecasts January 2021
Non-Domestic Rates – RV threshold for Fresh Start relief	The rateable value threshold for Fresh Start relief from Non-Domestic Rates was increased from £65,000 to £95,000. We estimated that the change fell under our £2 million threshold.	Scotland's Economic and Fiscal Forecasts January 2021
District Heating Networks relief	District heating networks installed on or after 1 April 2021 and powered by renewables, energy from waste, or waste heat will receive 90 per cent relief, rather than 50 per cent. We estimated that this change was negligible.	Scotland's Economic and Fiscal Forecasts January 2021
Child Disability Payment – Pilot	The CDP pilot ran from the July 2021 to November 2021. We estimated that the additional spending was negligible.	Scotland's Economic and Fiscal Forecasts January 2021
Social Security Administration and Tribunal Membership (Scotland) Bill	This is a series of administrative changes which we believe will have no material effect on spending.	In advance of the bill being introduced in April 2020

Figure C.1 (continued): Policies not costed since December 2018

Policy	Description and reason not to cost	Timing of original decision
Non-Domestic Rates – Reverse Vending Machine Relief	All Reverse Vending Machines will be eligible for 100 per cent relief so adding them to the valuation roll had no effect on NDR income.	Scotland's Economic and Fiscal Forecasts February 2020
The Revenue Scotland Tax Powers Act 2014 (Amendment) Regulations 2020	This is an administrative change which we believe has no financial implications.	Scotland's Economic and Fiscal Forecasts February 2020
Young Carer Grant	An annual payment for young carers with an estimated cost of less than £1 million.	Scotland's Economic and Fiscal Forecasts December 2018

Annex D
Fiscal Update

Overview

D.1 Due to the way the Scottish Budget is funded, the amount of money available during the year can change substantially.

D.2 For example, new UK Government spending announcements on devolved areas, new OBR forecasts of devolved taxes or devolved social security spending in the rest of the UK, or revised SFC forecasts of either devolved tax revenues or devolved social security spending in Scotland can all affect funding available to the Scottish Government.

D.3 This is why we track funding levels throughout the year. Sometimes we publish a standalone Fiscal Update paper. On this occasion, we have reported changes in funding in this annex.

2022-23

Introduction

D.4 The Scottish Budget for 2022-23 was laid before the Scottish Parliament on 9 December 2021.[71] After some minor changes during the debates at Stage 2 and 3, it was passed on 10 February 2022 and became law on 23 March 2022.[72]

D.5 We have given updates on the funding position for 2022-23 throughout the financial year. The latest update was reflected in Annex D of our December 2022 report, which tracked changes up to that point with almost three months of the financial year still left.[73]

D.6 The 2022-23 financial year has now ended. Between our December 2022 forecasts and the end of the financial year there has been only one UK fiscal event that affects the 2022-23 Scottish Budget's funding position: the approval of the UK Supplementary Estimates 2022-23 in March 2023.[74]

D.7 In addition, this report includes our latest forecast for 2022-23 fully devolved tax revenue. Later this year we will know how much was collected with the publication of outturn data by Revenue Scotland. We will publish a final Fiscal Update on the 2022-23 Budget alongside our Forecast Evaluation Report in the Autumn.

D.6 With the financial year ended, no more spending in 2022-23 is taking place. Changes to the 2022-23 funding position will be limited to the change arising from the publication of devolved taxes outturn data. Once final accounts are published later in 2023 any differences from Budget spending plans will be identified. Any underspends will be managed through the Scotland Reserve.

71 Scottish Government (2021) Scottish Budget 2022 to 2023 (link).
72 UK Government (2022) Budget (Scotland) Act 2022 – March 2022 (link).
73 Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022 (link).
74 UK Government (2023) Supplementary Estimates 2022-23 – February 2023 (link).

Resource

D.7 Figure D.1 shows changes to the resource funding position since 15 December 2022. Overall, resource funding for 2022-23 has gone up by an additional £86 million since then. The changes since the last fiscal update are:

- £105 million of additional Barnett consequentials. These were all generated with the UK Supplementary Estimates 2022-23, which granted some extra spending to UK Government departments. They cover areas devolved to the Scottish Government, so any changes to their spending plans affects the Scottish Block Grant via the Barnett formula.

- £2 million of extra forecast revenues from fully devolved taxes. Our forecast for Land and Buildings Transactions Tax (LBTT) has been revised down by £10 million, but this has been offset by an upward revision of the forecast for Scottish Landfill Tax (SLfT) of £12 million.

- £50 million less resource borrowing than previously planned, in line with the budget management process and the confirmation of additional Barnett consequentials.

- £27 million of additional 'other' funding. This is made up of an extra £5 million from the Scottish share of the Migrant Surcharge, £2 million less from the King's Lord Treasurer and Remembrancer (KLTR), and £6 million less from Machinery of Government transfers. There are an additional £30 million which consist of a correction of a historical error on the comparability factor of the Home Office in the UK Spending Review 2021, and some compensation for the costs relating to Her Late Majesty's death (Operation Unicorn).

Figure D.1: 2022-23 Budget – resource funding position over time

£ million	2022-23 Budget (9 Dec 2021)	Changes up to 15 Dec 2022	Annex D SEFF (Dec 2022)	Changes since 15 Dec 2022	Current position (May 2023)
Barnett baseline	34,322		34,322		34,322
Barnett consequentials		+447	447	+105	553
Non-Barnett funding	704		704		704
Forecast devolved revenues	14,546	+101	14,646	+2	14,648
of which: taxes	14,521	+101	14,621	+2	14,623
of which: non-tax revenues	25		25		25
Tax and non-tax BGAs	-14,639	-74	-14,713		-14,713
Social security BGAs	3,587	+116	3,703		3,703
Adjustment for past forecast error	0	+82	82	-50	32
Reconciliations	-15	+0	-15		-15
Resource borrowing	15	+82	97	-50	47
Scotland Reserve drawdown	0	+605	605		605
Other funding	742	+159	901	+27	928
of which: assumed	620	-600	20		20
of which: confirmed	122	+759	881	+27	908
NDR distributable amount	2,766		2,766		2,766
less: resource borrowing costs		-77	-77		-77
less: capital borrowing costs		-83	-83		-83
Resource funding available for discretionary spend	42,027	+1,276	43,303	+84	43,388

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

Capital

D.8 Figure D.2 shows changes to the capital funding position since 15 December 2022. Overall, capital funding for 2022-23 has gone down by £353 million since then. Rather than requiring spending cuts, the fall in capital funding levels has been balanced through slippages in planned investment projects. The changes are:

- £73 million less capital Block Grant funding and £117 million less FTs Block Grant funding because of negative Barnett consequentials. The lower capital budgets for UK Government departments were confirmed at the UK 2022-23 Supplementary Estimates. Including FTs, these consequentials leave the 2022-23 Barnett capital settlement £177 million below the UK Spending Review 2021 plans.

- £150 million less capital borrowing than initially planned, despite lower overall capital funding levels. This has been feasible, as explained above, due to delays in planned investment projects in 2022-23.

- A reduction of £12 million in other capital funding. This consists of £0.6 million of additional capital city deals, and -£13 million on Machinery of Government Transfers (MoGs). With this reduction, the MoGs align with the UK 2022-23 Supplementary Estimates.

Figure D.2: 2022-23 Budget – capital funding position over time

£ million	2022-23 Budget (9 Dec 2021)	Changes up to 15 Dec 2022	Annex D SEFF (Dec 2022)	Changes since 15 Dec 2022	Current position (May 2023)
Capital (Excluding FTs)					
Barnett baseline	4,469		4,469		4,469
Barnett consequentials		+13	13	-73	-60
Non-Barnett funding	643	+75	718		718
Capital borrowing	450		450	-150	300
Scotland Reserve drawdown	118	-37	81		81
Other funding	144	-12	132	-12	120
of which: assumed	0	+20	20		20
of which: confirmed	144	-32	112	-12	100
Total capital funding (excluding FTs)	5,824	+39	5,863	-235	5,627
Financial transactions (FTs)					
Barnett baseline	466		466		466
Barnett consequentials				-117	-117
Scotland Reserve drawdown	61	-47	14	-1	14
Total financial transactions	527	-47	480	-118	362
Total capital funding	6,351	-8	6,343	-353	5,990

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

2023-24

Introduction

D.9 The 2023-24 funding position was first estimated on 15 December 2022, when the draft 2023-24 Scottish Budget was laid before the Scottish Parliament.[75]

D.10 The 2023-24 financial year began in April 2023. This is the first time we report changes to the funding position for this year since the 2023-24 Budget was published. We will do this again alongside the 2024-25 Scottish Budget.

D.11 The main event that has affected the funding position for this year since the draft 2023-24 Budget is the UK Spring Budget 2023, which has generated Barnett consequentials.[76] The policies outlined in the Spring Budget 2023 for 2023-24 have formally been translated into revised spending plans at

[75] Scottish Government (2022) Scottish Budget: 2023-24 (link).
[76] UK Government (2023) Spring Budget 2023 (link).

the Main Supply Estimates 2023-24.[77] These, along with some other adjustments to spending allocations for UK Government departments, have generated some extra Barnett consequentials.

D.12 In addition, we have revised our forecasts of devolved tax revenues for 2023-24, as presented in this report. Finally, with 2022-23 over, any underspends in 2022-23 will be saved in the Scotland Reserve and be available to support additional spending in 2023-24. At the time of writing this report, the Scottish Government plans to draw down £50 million from the Scotland Reserve for FTs.

D.13 Any extra funding in 2023-24 will be available for deployment at the upcoming Autumn Budget Revision.

Resource

D.14 Figure D.3 shows changes to the 2023-24 funding position since December 2022. Resource funding has gone up by £269 million since then.

D.15 The main changes are:

- An increase of £95 million in Block Grant funding due to additional Barnett consequentials. £43 million were generated from policies the UK Government announced in its Spring Budget 2023. The other £52 million have been generated from additional departmental spending as presented in the draft UK 2023-24 Main Supply Estimates.
- An additional £11 million following our latest forecast of devolved tax revenues, which we publish in this report. Most of the additional revenue is Scottish Landfill Tax.
- An additional £73 million of other resource funding. This consists of an additional £40 million of the Scottish share of the Migrant Surcharge, £13 million of extra Machinery of Government (MoG) transfers, and a further £20 million to correct a historical error made on the comparability factors for the Home Office at the UK Spending Review 2021.
- A small reduction in the projected borrowing costs, given the final decisions to borrow less for resource and capital in 2022-23 than previously planned.

[77] UK Government (2023) Main Supply Estimates 2023 to 24 (link).

Figure D.3: 2023-24 Budget – resource funding position over time

£ million	2023-24 Budget (15 Dec 2022)	Changes since 15 Dec 2022	Current position (May 2023)
Barnett baseline	34,942		34,942
Barnett consequentials	1,081	+95	1,176
Non-Barnett funding	715		715
Forecast devolved revenues	16,688	+11	16,699
of which: taxes	16,663	+11	16,674
of which: non-tax revenues	25		25
Tax and non-tax BGAs [1]	-16,131	+0	-16,130
Social security BGAs [1]	4,360	+73	4,434
Adjustment for past forecast error	87		87
Reconciliations	46		46
Resource borrowing	41		41
Scotland Reserve drawdown	0		0
Other funding	435	+73	508
of which: assumed	120	+73	193
of which: confirmed	315		315
NDR distributable amount	3,047		3,047
less: resource borrowing costs	-120	+6	-114
less: capital borrowing costs	-112	+10	-103
Resource funding available for discretionary spend	44,991	+269	45,260

Source: Scottish Fiscal Commission, Scottish Government.
Figures may not sum because of rounding.
[1] The BGAs have been updated with the March 2023 OBR forecasts (link). However, these only provide an indication of where the in-year adjustment may land. Funding levels are not adjusted until Autumn 2023 and will be based on a later set of the OBR's forecasts.

Capital

D.16 Figure D.4 shows changes to the capital funding position for 2023-24 since December 2022. Overall, capital funding for this year has increased by £51 million.

D.17 The only change of significance to the capital budget position is an increase of £50 million in the Block Grant, resulting from extra Barnett consequentials. These have been generated from the policies the UK Government announced in the Spring Budget 2023 and in the UK Main Estimates 2023-24.

Figure D.4: 2023-24 Budget – capital funding position over time

£ million	2023-24 Budget (15 Dec 2022)	Changes since 15 Dec 2022	Current position (May 2023)
Capital (Excluding financial transactions)			
Barnett baseline	4,757		4,757
Barnett consequentials	0	+63	63
Non-Barnett funding	632		632
Capital borrowing	250		250
Scotland Reserve drawdown	0		0
Other funding	300	+2	302
of which: assumed	300		300
of which: confirmed	0	+2	2
Total capital funding (excluding financial transactions)	5,939	+65	6,004
Financial transactions			
Barnett baseline	186		186
Barnett consequentials	blank	-13	-13
Scotland Reserve drawdown	50		50
Other funding	188		188
of which: assumed	188		188
of which: confirmed	0		0
Total financial transactions	424	-13	410
Total capital funding	6,363	+51	6,414

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

Additional Information

Abbreviations

ADP	Adult Disavility Payment
ADS	Additional Dwelling Supplement
APS	Annual Population Survey
BGA	Block Grant Adjustment
BGAs	Block Grant Adjustments
BMW	Biodegradable Municipal Waste
BoE	Bank of England
CA	Carer's Allowance
CAPP	Carer's Additional Person Payment
CAS	Carer's Allowance Supplement
CDP	Child Disavility Payment
CPI	Consumer Price Index
CSP	Carer Support Payment
CWHA	Child Winter Heating Assistance
DLA	Disability Living Allowance
DWP	Department for Work and Pensions
EfW	Energy from Waste
EU	European Union
FAI	Fraser of Allander Institute
FFFPs	Fines, Forfeitures, and Fixed Penalties
FFP	Five Family Payments
FRS	Family Resources Survey
GDP	Gross Domestic Product
HMRC	His Majesty's Revenue and Customs
HMT	His Majesty's Treasury
IPR	Intermediate Property Rate
KLTR	King's Lord Treasurer and Remembrancer
LBTT	Land and Buildings Transaction Tax
LFS	Labour Force Survey
MoG	Machinery of Government
MTFS	Medium-Term Financial Strategy
NDR	Non-Domestic Rates
NHS	National Health Service
NIESR	National Institute of Economic and Social Research
NSND	Non-savings, non-dividend
OBR	Office for Budget Responsibility
OECD	Organisation for Economic Cooperation and Development
ONS	Office for National Statistics
PADP	Pension Age Disability Payment
PAYE	Pay As You Earn
PIP	Personal Independence Payment
POC	Proceeds of Crime
PUT	Public Use Tape
RLW	Real Living Wage
RTI	Real Time Information
SBBS	Small Business Bonus Scheme
SCP	Scottish Child Payment
SEFF	Scotland's Economic and Fiscal Forecasts
SFC	Scottish Fiscal Commission

SG	The Scottish Government
SIT	Scottish income tax
SLfT	Scottish Landfill Tax
SPI	Survey of Personal Incomes
SSS	Social Security Scotland
STA	Short-term Assistance
VAT	Value Added Tax
WRIT	Welsh rate of income tax

A full glossary of terms is available on our website:

https://www.fiscalcommission.scot/explainers/glossary/

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The Commission is committed to fulfilling our role as an Independent Fiscal Institution, in line with the principles set out by the Organisation for Economic Cooperation and Development (OECD).[78]

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All figures in this publication have also been made available in spreadsheet form on our website. For technical enquiries about the analysis and data presented in this report please contact the responsible analyst:

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[78] OECD (2014) Recommendation on Principles for Independent Fiscal Institutions (link).
[79] Scottish Fiscal Commission (2018) Compliance with the Code of Practice for Statistics and Error Policy (link).

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