Scottish Fiscal Commission

# Fiscal Update

August 2025

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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 tax revenues and devolved social security spending to inform the Scottish Budget. We also publish regular commentary on the Scottish Budget.

This report considers how recent developments in the economic and fiscal outlook have affected the Scottish Budget in 2025-26 and how they may affect the upcoming 2026-27 Budget and the Spending Review. We are publishing this update to support the Scottish Parliament in its pre-Budget scrutiny and the examination of the upcoming Autumn Budget Revision.

We would like to thank once again the hard-working staff of the Commission for their support in the production of this analysis. Our reports represent the collective view of the four Commissioners who take full responsibility for them.


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26 August 2025

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# Summary

## Introduction

1 The Scottish Government plans to present its multi-year Spending Review alongside the 2026-27 Scottish Budget in December 2025. It is facing a tight fiscal settlement and growing pressures on its Budget in the short, medium, and long term. At the same time there is increased short-term economic uncertainty from international trade policies, reflected in weak consumer and business sentiment.

2 This is the context in which the Parliament will undertake pre-Budget scrutiny this autumn and the Scottish Government will develop its spending plans. In its June Medium-Term Financial Strategy (MTFS) the Scottish Government noted substantial gaps between current spending trajectories and available funding. The Scottish Government is required to broadly balance its budget, so the Spending Review will need to set out plans to close the fiscal gaps and place the public finances on a more sustainable footing.

3 In this Fiscal Update, we examine recent developments affecting the Scottish funding outlook, consider broader trends in funding and spending, and look ahead to upcoming fiscal events.

## Recent developments

4 The UK Spending Review in June 2025 set the Scottish Block Grant up to 2028-29 for resource budgets (used for day-to-day spending such as public sector pay) and up to 2029-30 for capital (used for the building of assets, like roads, hospitals and schools). This, along with tax policies, will feed into the Scottish Spending Review (SSR) expected in December 2025.

5 The Scottish Government’s June 2025 MTFS was based on the position after the UK Spending Review on 11 June and set out projections for funding and spending over the next five years. Based on current trajectories, the Scottish Government expects spending to exceed available funding for both resource and capital. Figure 1 shows the resource and capital gaps presented in the MTFS. The gaps for both resource and capital are expected to exceed £2 billion by 2029-30, around 4 per cent of planned spending in 2029-30 for resource, and around 23 per cent for capital.

**Figure 1: Resource and capital gaps in the MTFS**

| £ million (nominal terms) | 2026-27 | 2027-28 | 2028-29 | 2029-30 |
|---|---|---|---|---|
| **Resource** | | | | |
| Funding | 53,975 | 55,235 | 57,100 | 59,099 |
| Spending | 54,938 | 57,132 | 59,453 | 61,723 |
| Gap | -963 | -1,897 | -2,353 | -2,624 |
| **Capital (excluding FTs)** | | | | |
| Funding | 7,109 | 7,004 | 7,059 | 7,067 |
| Spending | 8,180 | 8,501 | 8,962 | 9,213 |
| Gap | -1,070 | -1,497 | -1,903 | -2,146 |

Source: Scottish Fiscal Commission, Scottish Government.

Figures may not sum because of rounding.

6 Since the UK Spending Review the UK Government has made some policy changes which may affect the Scottish Budget either directly or indirectly. While defence was already a priority in the UK Spending Review, an additional commitment has since been made to allocate 5 per cent of Gross Domestic Product to defence spending by 2035. How the Scottish funding position is affected will be determined by whether this is funded through increased borrowing or taxes, or through reductions in spending on other reserved or devolved areas.

7 UK welfare policy has also changed since our last report in June. Previously planned measures to restrict eligibility for Personal Independence Payment (PIP) were removed from the bill passed by the House of Commons on 9 July. The latest social security Block Grant Adjustment forecasts were based on these policies being introduced. This was estimated to reduce the Scottish Government's funding by £0.4 billion by 2029-30. That reduction will likely be reversed when the Office for Budget Responsibility (OBR) produces its next forecasts in the autumn, therefore increasing funding the Scottish Government receives for social security. However, any further UK Government policy changes, including further changes to disability payments, will affect the Scottish Government's funding.

8 Income Tax outturn data for 2023-24 was published in July 2025, showing strong growth in Scottish Income Tax revenues which was faster than in the rest of the UK. This growth contributed to a positive final Income Tax reconciliation of £406 million to be applied in the 2026-27 Scottish Budget.

9 After positive Income Tax reconciliations being applied to the 2025-26 Budget and 2026-27 Budget, the latest SFC and OBR forecasts suggest negative reconciliations applying to the 2027-28 and 2028-29 budgets.[1] The negative reconciliation currently indicated for 2027-28 is £851 million, which would exceed the resource borrowing limit allowed in the fiscal framework.

[1] These reconciliations relate to Income Tax collected in 2022-23, 2023-24, 2024-25 and 2025-26 respectively.

10 Most of the devolved public sector workforce is now covered by agreed pay deals for 2025-26, and most deals agreed also cover 2026-27. The pay deals agreed have all exceeded the Scottish Government's public sector pay policy (PSPP). Under this policy, deals that did not cover three years were to be limited to a 3 per cent increase in 2025-26, and the cumulative increase was to be limited to 9 per cent over the three years from 2025-26 to 2027-28. The deals agreed so far cover only 2025-26 and 2026-27, and some of these also have inflation protection clauses. Unless deals with nominal pay growth of around 1 per cent are accepted for 2027-28, the PSPP of 9 per cent pay increases over three years will be exceeded.

11 As we have set out in previous reports, any pay increases agreed in one year mean that subsequent pay awards are more costly. Pay is also just one part of the Scottish Government's paybill, which also covers employer pension contributions and employer National Insurance contributions (NICs) and is affected by the size and composition of the workforce.

12 In its Fiscal Sustainability Delivery Plan (FSDP), the Scottish Government committed to a gradual reduction in the public sector workforce of an average of 0.5 per cent a year for the next five years, "with frontline services remaining protected".[2] The Scottish Government estimated this will save £100 million in 2026-27 and £700 million by 2029-30. This is intended to contribute to closing the gap between funding and spending which the Scottish Government set out in the MTFS.

13 Achieving a reduction in the workforce would require a significant departure from recent trends. The devolved public sector workforce has grown each year since 2018-19. NHS Scotland is the largest workforce and has been growing steadily since the start of devolution in 1999. There has also been rapid growth in the size of the devolved civil service since 2018-19. This is because of the creation of new executive agencies such as Social Security Scotland to deliver the newly devolved social security payments, the COVID-19 pandemic response, and preparations for the UK's exit from the EU, alongside general growth in the core Scottish Government.[3]

14 The baseline paybill used by the Government to set the workforce reduction targets will increase with any new pay deals above the PSPP agreed since the FSDP in June. Therefore, higher-than-anticipated pay increases would mean the workforce reductions required would be larger than those announced in the FSDP to keep the paybill at the levels intended by 2029-30.

# Looking ahead to the Scottish Spending Review

15 The coming months will see a range of fiscal activity: parliamentary pre-Budget scrutiny, the Scottish Government's Autumn Budget Revision (ABR), a UK Budget, and the 2026-27 Scottish Budget alongside the SSR.

[2] Scottish Government (2025) Fiscal Sustainability Delivery Plan

[3] Institute for Government (2025) Civil service staff numbers

16 The ABR is expected to set out how the Scottish Government intends to allocate Barnett consequentials it received following the UK Government's decision to increase employers' NICs. The 2025-26 Scottish Budget was set without accounting for the increase in employer NICs as the UK Government had not provided details on funding at that stage. It has since confirmed, after compensating its departments for the tax rise, that the Scottish Government will receive £339 million in 2025-26. We expect the upcoming ABR to show how these consequentials are allocated. Since the Scottish Government had estimated its funding needs to be higher than the Barnett consequentials received, we also expect the ABR to show whether the extra cost of higher employer NICs is met from previously unallocated funding, from savings from within existing spending plans, or from a combination of both.

17 The UK Budget is expected in the autumn and will also provide important details for the Scottish funding position. It will confirm any changes in the Block Grant for 2026-27, and new OBR forecasts will determine the Block Grant Adjustments for tax and social security.

18 After the UK Budget, the Scottish Budget and Scottish Spending Review are expected in December. The Scottish Government's June MTFS set out the scale of the challenge the Scottish Government faces in balancing its budget. The fiscal settlement is tight, with a continuation of current spending plans resulting in spending exceeding the available funding. Last year, post-election, the UK Government announced significant in-year changes to spending plans which resulted in a large level of additional funding for the Scottish Government. Such changes should not be expected this year as the UK Spending Review has set out the departmental budgets for the next few years.

19 There are also longer-term challenges for the Scottish Budget because of an ageing population. Our April 2025 report highlighted how the fastest demographic growth in Scotland in the next twenty-five years will be in the older age groups, so funding health-related spending increases will become increasingly challenging.[4] The Scottish Government has also set new climate change targets, and meeting these will require substantial investment. [5]

20 The SSR provides an opportunity for the Scottish Government and the Scottish Parliament to address both immediate budgetary pressures and, crucially, long-term fiscal sustainability challenges. Closing the fiscal gap will require all parties in this parliament and the next to work together to address the fiscal challenges. Any debates around new spending plans, changes to social security policy, or tax changes need to consider the broader public finances.

21 The FSDP identified broad areas of efficiency and reforms in the public sector which the Government plans to use to close the fiscal gaps identified in the MTFS. Except for the commitment to reduce the size of the workforce, the detail of how these efficiencies and reforms would be achieved was not included. The SSR should provide more detail on how the Scottish Government will deliver on the ambitions presented in the FSDP, but it is also likely the Scottish Government will need to continue to work on its programme of reform throughout the spending review period.

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[4] Scottish Fiscal Commission (2025) [Fiscal Sustainability Report – April 2025]

[5] Scottish Government (2025) [New climate targets set]

22 The SSR will take place before the next Scottish Parliament election. Implementing the SSR will mainly be the responsibility of the Scottish Government and Scottish Parliament elected in May 2026. It is important that the SSR provides a meaningful basis for informed debate by all political parties on how the fiscal challenges the Scottish Government faces can be addressed.

# Funding and spending trends

23 Chapter 3 of this report focuses on trends in public funding and spending, which is intended to provide helpful context for parliament and others ahead of the Budget revisions, 2026-27 Budget, and SSR.

24 The Scottish Government is required to broadly balance its budget each year. During the financial year there can be changes in funding through the Block Grant as the UK Government changes its own spending plans in-year, and there can also be volatility from fully devolved taxes or social security spending. The Scottish Government has limited tools to manage any volatility in the budget in-year.

25 The Scottish Government amends the Budget during the financial year, altering spending and funding plans to ensure the budget balances. It can alter borrowing or its planned use of the Scotland Reserve or ScotWind funding. Our analysis suggests in-year spending changes tend to be proportionately larger for capital spending and financial transactions than resource spending, likely because of the nature of the large capital projects being managed.

26 Over the last seven years the only area of resource spending which has grown significantly in real terms is social protection spending. This is because of the devolution of social security payments, and then rapid growth in the cost of those payments. Spending on health peaked during the pandemic and, based on the 2025-26 Budget plans, spending will be broadly the same in real terms as in 2024-25.

# Improving the Scottish Budget

27 We conclude this Fiscal Update by looking at ways in which the presentation of the Scottish Budget might be improved. These are technical but important points if parliament and others are to have the information they require for effective scrutiny.

28 One issue that came up during consideration of the 2025-26 Budget related to the comparator used when presenting spending plans. A large, £1.4 billion increase in 2024-25 funding from the UK Budget 2024 was not included in the 2024-25 comparator. By not doing so, it made the overall 2025-26 Budget increase and portfolio allocations look higher than they were. When the 2024-25 increases were allocated in the Spring Budget Revision (SBR), the difference in the baseline to calculate the changes to portfolios allocations became apparent, as Figure 2 shows.

**Figure 2: Effect of different comparators for changes in resource portfolio allocations**

| Portfolio | Share of budget [1] | Real-terms change from 2024-25 (ABR) | Real-terms change from 2024-25 (SBR) | Percentage point difference |
|---|---|---|---|---|
| Health and Social Care | 39.3 | 3.4 | 0.3 | -3.1 |
| Finance and Local Government | 25.6 | 2.6 | -1.2 | -3.8 |
| Social Justice | 14.6 | 7.9 | 8.1 | 0.2 |
| Justice and Home Affairs | 6.8 | 2.2 | 0.3 | -1.9 |
| Education and Skills | 6.2 | 3.0 | 1.7 | -1.3 |
| Transport | 3.0 | 1.7 | 1.8 | -0.1 |
| Rural Affairs, Land Reform and Islands | 1.8 | -3.1 | -2.7 | +0.3 |
| Deputy First Minister, Economy and Gaelic | 1.2 | 3.7 | 20.7 | +17 |
| Constitution, External Affairs and Culture | 0.6 | 9.3 | 9.9 | +0.6 |
| Crown Office and Procurator Fiscal Service | 0.4 | 7.3 | 7.7 | +0.4 |
| Net Zero and Energy | 0.2 | 11.1 | 61.9 | +50.8 |
| Scottish Parliament and Audit Scotland | 0.3 | 6.4 | 6.2 | -0.2 |
| Total resource spending | 100.0 | 3.7 | 1.4 | -2.3 |

Source: Scottish Fiscal Commission, Scottish Government.

[1] Of the resource part of the 2025-26 Budget as approved by the Parliament after changes through the Budget Bill stages.

Figures may not sum because of rounding.

29 We therefore recommend a threshold be set for in-year funding changes following the ABR and before the Scottish Budget. If exceeded, it should trigger a requirement for the Scottish Government to indicate, as part of the Budget documents for the year ahead, how that additional funding would be spent, with decisions to be confirmed in the SBR. This would mean year-on-year comparisons in spending are more meaningful and would assist parliamentary scrutiny.

30 Similar issues arose with the inclusion of routine transfers between portfolios in the 2024-25 baseline (which was based on the Autumn Budget Revision), but not in the 2025-26 Budget plans. This had a substantial and material effect on the position of portfolios such as Education and Skills, Health, and Local Government which all have routine in-year transfers for certain functions. While the Scottish Government did provide some information on the scale of internal transfers in 2024-25 this did not set out the internal transfers the Scottish Government expected to happen in 2025-26. There are more improvements the Scottish Government could make, including the publication of further information on internal transfers, or presenting the Budget with all spending shown at the outset under the portfolio that will ultimately incur it.

# Chapter 1 Introduction

1.1 This Fiscal Update is intended to inform scrutiny of the upcoming 2025-26 Autumn Budget Revision, the 2026-27 Scottish Budget, and the Scottish Spending Review. It sets out developments since our May 2025 forecast report and our June 2025 update.[6] We intend to establish a Fiscal Update as regular annual publication, published alongside our Forecast Evaluation Report.

1.2 We structure the document as follows.

- In Chapter 2, we look at developments since June, such as UK Government announcements with implications for the Scottish public finances, the final Income Tax reconciliations to be applied to the 2026-27 Budget, and the latest on Scottish public sector pay deals
- In Chapter 3, we discuss recent trends in public funding and spending
- In Chapter 4, we outline what to expect in the upcoming Scottish fiscal events
- In Chapter 5, we consider how the presentation of the Scottish Budget could be improved

1.3 Although this Fiscal Update is forward-looking, we have also restated outturn funding positions for years 2020-21 to 2024-25. This is because our previous reports have not presented final outturn data for these years and because we have made several changes to how we present funding information since we first began reporting the funding position in January 2020. We now present all previous years on a consistent basis in Annex A.

1.4 Finally, in Annex B we provide a costing for the latest Scottish Government policy for Pension Age Winter Heating Payment as announced on 18 June 2025. This is a more detailed costing than the illustrative estimate we included in our June 2025 report.

[6] Scottish Fiscal Commission (2025) Scotland's Economic and Fiscal Forecasts – May 2025 and June 2025 (update)

# Chapter 2
# Developments since June 2025

2.1 In recent months there have been several developments that have altered the Scottish Government's funding and spending position. These include announced changes to UK Government spending, Income Tax outturn data, and several pay deals in Scotland for 2025-26 and beyond.

## UK Government announcements

### Spending Review 2025

2.2 The latest UK Spending Review (UKSR) concluded on 11 June 2025. It set departmental resource budgets up to 2028-29, and to 2029-30 for capital.[7] The Scottish Government's Block Grant was confirmed for the same periods.

2.3 As we outlined in our June 2025 report, the UKSR led to a lower Block Grant than was estimated based on Office for Budget Responsibility (OBR) forecasts of growth in overall departmental budgets. For resource, it was smaller in each year, because, even though the UK Government prioritised devolved areas, it planned for a lot of spending growth to be funded through increases in English Business Rates, for which there is a negative consequential applied to the Scottish Block Grant.[8] For capital, the Block Grant was bigger for 2026-27, but lower thereafter, as the UK Government prioritised reserved areas such as defence. Only the financial transactions (FTs) Block Grant was substantially higher than we expected. As a small part of the Scottish Budget, though, this had a limited effect on total funding.

2.4 The resource Block Grant for 2026-27 is £0.2 billion smaller than previously assumed. While the larger-than-expected capital and FTs Block Grants offset most of that fall, the Scottish Government cannot transfer funding from capital to resource.

2.5 The UKSR also re-stated budgets for 2025-26. Although the UK Government made higher pay offers than Whitehall departments had planned for, the UKSR confirmed that they mostly had to absorb the higher pay deals within existing budgets. Resource departmental budgets in 2025-26 across the UK Government, which were more than £0.5 trillion before the UKSR, increased by only £301 million in 2025-26, generating £10 million in consequentials for the Scottish Government.

2.6 The UKSR provides greater certainty about the level of the Block Grant for the next few years. Experiences from previous Spending Reviews suggest there could still be further changes, but these will not be as significant as the changes announced post-election in 2024 or in the UKSR in June. HM Treasury set aside reserves in each financial year of

[7] HM Treasury (2025) Spending Review 2025

[8] This is because the Scottish Government keeps the revenue of the equivalent tax in Scotland (Non-Domestic Rates), which it distributes among Scottish local authorities. Otherwise, it would have both this revenue and a Barnett share of devolved UK Government spending funded with the equivalent tax in England. For more details, see the 'Non-domestic (business) rates' section in HM Treasury (2025) Statement of Funding Policy.

the UKSR. Over time it is likely to allocate at least part of that funding to departments, with decisions typically made at UK Budgets or Statements. If allocations go to departments that are partly or fully devolved, there will be additional Barnett consequentials.[9] Moreover, as the economic and fiscal context changes, UK Budgets and Statements are opportunities to revisit those departmental budgets beyond what had been set aside as reserves. Again, when these budgets change for departments that are fully or partially devolved, there will be Barnett consequentials, which can be positive or negative.

## Defence Commitments

2.7 The UKSR substantially increased planned capital spending on defence. The Ministry of Defence has the third largest overall budget, after Health and Social Care and Education.[10] Among these three, it is defence spending that the UK Government plans to grow most rapidly (3.8 per cent a year on average in real terms), driven mostly by capital. Following the UKSR, UK Government spending in defence is planned to gradually grow as a share of Gross Domestic Product (GDP), from 2.0 per cent in 2023-24 to 2.3 per cent by 2028-29.[11]

2.8 In the longer term, the UK Government intends to spend substantially more on defence. In June it committed to spending 5 per cent of GDP by 2035, split between core defence spending (3.5 per cent) and broader resilience and security (1.5 per cent).[12]

2.9 Defence is a reserved area. When the UK Government spends on defence, it does so on behalf of the whole of the UK. Therefore, changes to reserved spending do not directly or immediately affect the Scottish Government's funding position.

2.10 If the UK Government borrows to fund this defence commitment, the Scottish Budget would be unaffected. However, it would contribute to the UK Government's future fiscal sustainability challenges. The UK Government may do several things to meet this commitment in a fiscally sustainable way:

- Reducing spending in other reserved areas, as was the case when it announced an overall shift from overseas aid to defence. This does not affect the Scottish Government's funding.
- Reducing spending in devolved areas. This would result in the Scottish Block Grant falling, or at least not growing as rapidly as without the commitment.

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[9] This would formally take place through the Supply Estimates process.

[10] Budget as measured in terms of Departmental Expenditure Limits (DELs), which are set at Spending Reviews. Some departments, such as the Department for Work and Pensions, have much larger budgets. However, most of their spending is classed as annually managed expenditure (AME) because it is demand-led. Therefore, it is not subject to the same controls.

[11] Calculated as the Total DEL for the Ministry of Defence (MoD) and the Single Intelligence Account in 2028-29, divided by forecast GDP in that year in the latest OBR forecasts (March 2025). An allowance has been made for MoD non-defence spending based on outturn spending by COFOG category in 2023-24. This calculation does not include defence-related spending classed as AME. Forecasts of this AME are not produced until the Supply Estimates for each year are published.

[12] UK Government (2025) UK to deliver on 5% NATO pledge as Government drives greater security for working people

- Increasing existing reserved taxes or creating new ones. This would not affect the Scottish Government's funding, although they would also apply to people or businesses in Scotland.

- Increasing devolved taxes, such as Income Tax. In this case, funding for the Scottish Government will fall via the Block Grant Adjustments (BGAs).

2.11 While an increase in defence spending does not immediately or necessarily result in changes to funding for the Scottish Budget, some of that UK Government extra defence spending through procurement or employment for the Ministry of Defence could benefit the Scottish economy directly and indirectly.

## UK Government welfare changes

2.12 In its Spring Statement 2025, the UK Government announced a package of measures to reform welfare spending.[13] The biggest measures were reducing the health-related allowances within Universal Credit (UC) while increasing the standard allowance, and a restriction in eligibility for Personal Independence Payment (PIP). Reducing the number of people receiving PIP was also expected to reduce the number of people eligible for Carer's Allowance (CA). The PIP policy, together with increasing capacity to process award reviews, was expected to save £4.7 billion by 2029-30.

2.13 Universal Credit is a reserved benefit, but PIP and CA are devolved. In Scotland, Adult Disability Payment (ADP) and Carer Support Payment have replaced PIP and CA and it is the Scottish Government setting eligibility criteria and the process for award reviews.

2.14 However, the BGAs for PIP and CA depend on UK Government spending on those benefits. As a result, funding was expected to fall in line with the UK Government savings announced. In May 2025, we noted the BGA for PIP was to be £0.4 billion lower by 2029-30 compared with forecasts in December 2024 largely because of the UK Government policy change.

2.15 Our May 2025 forecast for ADP, which the Scottish Government used in its June Medium-Term Financial Strategy (MTFS), was largely unchanged from December 2024. Therefore, the reduction in BGA funding for PIP led to the shortfall between funding and spending for ADP widening and contributed to the overall resource gap the Government presented in the MTFS.

2.16 The UK Government position on the package of welfare measures on UC and PIP has significantly changed since its Spring Statement 2025. Changes to the PIP eligibility criteria will only be introduced after a review of the PIP assessment process, expected to be completed by autumn 2026. The bill passed by the UK Parliament on 9 July removed the PIP measures and only included the UC measures.

2.17 Therefore, the savings the OBR had forecast in March 2025 from PIP reforms will be reduced, as will the fall in the associated BGAs. We expect the OBR to produce a costing of the updated policy alongside the next UK Budget in the autumn.

[13] HM Treasury (2025) Spring Statement 2025

# Income Tax

## Overview

2.18 The latest published outturn shows that Scottish Income Tax (SIT) revenues grew strongly in 2023-24, faster in Scotland than in the rest of the UK. [14] This growth has been generated by ongoing, though easing, inflation and rising nominal earnings while the higher, advanced, and top rate thresholds have been frozen.

2.19 This relatively faster growth in Scotland contributed to a more positive Income Tax net position in 2023-24, so there will be a positive final reconciliation of £406 million applied to the 2026-27 Scottish Budget.[15]

2.20 In both 2022-23 and 2023-24, Real Time Information (RTI) data from HM Revenue and Customs (HMRC) shows that earnings growth in Scotland was faster than across the UK. Income Tax data from RTI shows that SIT revenues continued to grow strongly in 2024-25. However, unlike in 2022-23 and 2023-24, growth in Scotland was more in line with the UK average in 2024-25.

2.21 As a result, while SIT revenues are still forecast to increase, they are now forecast to do so at a similar pace to the rest of the UK in the near-term. In May 2025 the net position was projected to remain steady in nominal terms between 2023-24 and 2025-26. Similar relative earnings growth is one of the main reasons for this.

2.22 We now have a final net position in 2023-24. We will update the projection of the net position from 2024-25 onwards alongside indicative reconciliations in our upcoming forecasts accompanying the 2026-27 Scottish Budget. This will include our latest estimate of the large negative reconciliation to be applied in 2027-28 relating to Income Tax revenue in 2024-25.

## Outturn data, the net position and reconciliations in 2023-24

2.23 The contribution of Income Tax to the Scottish Budget is based on forecasts from both the Scottish Fiscal Commission and the OBR. When outturn data on tax revenues becomes available, the forecast error is calculated, and adjustments are made to a later budget. This process is known as a reconciliation.

2.24 The outturn data published in July 2025 shows that both SIT revenues and the Income Tax BGA were substantially higher than the forecasts used to set the 2023-24 Budget. The underestimation of SIT revenues was more than in the rest of the UK, as shown in Figure 2.1. As a result, there is a positive final reconciliation of £406 million that will be applied in the 2026-27 Scottish Budget.

[14] HM Revenue and Customs (2025) Scottish Income Tax Outturn Statistics: 2023 to 2024

[15] Scottish Government (2025) Income Tax outturn reconciliation 2023-24: joint statement with HM Treasury

**Figure 2.1: SIT and BGA outturn for 2023-24 compared with Budget-setting forecasts**

| £ million | Scottish Income Tax | Block Grant Adjustment | Income Tax net position |
|---|---|---|---|
| December 2022 (Budget-setting) | 15,810 | -15,485 | 325 |
| Outturn | 17,093 | -16,362 | 730 |
| Change | 1,283 | -877 | 406 |

Source: Scottish Fiscal Commission (2022) Scotland's Economic and Fiscal Forecasts – December 2022, HMRC (2025) Scottish Income Tax Outturn Statistics: 2023 to 2024, OBR (2022) Economic and fiscal outlook – November 2022.

Figures may not sum because of rounding.

2.25 The SIT forecast error is mainly because of higher-than-expected nominal wage growth in 2023-24, which subsequently increased the number of taxpayers, particularly in the higher and top rate bands. Our Forecast Evaluation Report, published alongside this Fiscal Update, gives further details on this.[16]

## What to expect in 2024-25 and beyond: earnings growth gap and reconciliations

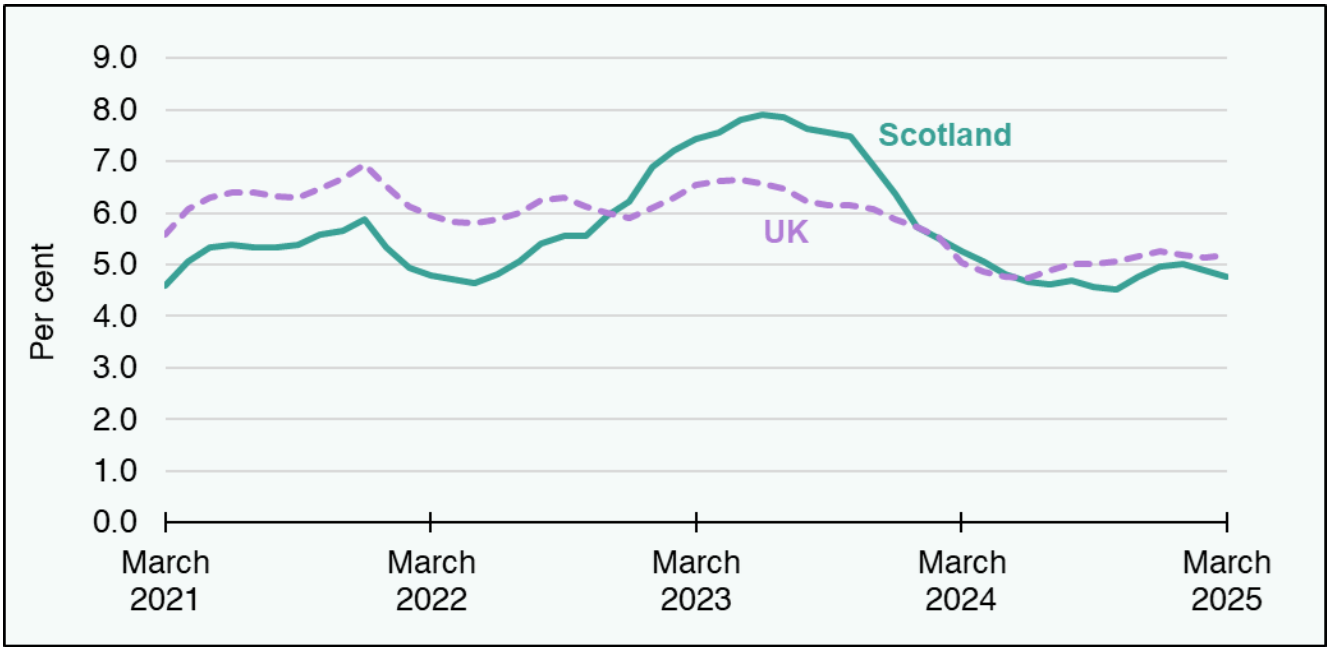
2.26 Following publication of outturn for 2023-24, we can also see the latest outlook for 2024-25 and 2025-26 based on the latest RTI earnings data. This data enables us to assess how accurately the budget-setting forecasts captured earnings growth in both Scotland and the rest of the UK.

2.27 We define the 'earnings growth gap' as the difference between average earnings growth in Scotland and the rest of the UK. Monitoring changes in this indicator over time is crucial, as it affects the Income Tax net position and the scale and sign of subsequent reconciliations. Figure 2.2 shows Scottish and UK earnings growth using RTI data. In 2022-23 and 2023-24, the earnings growth gap was positive. However, for 2024-25, the latest data indicates that the earnings growth gap has narrowed and may actually be slightly negative.

[16] Scottish Fiscal Commission (2025) Forecast Evaluation Report – August 2025

**Figure 2.2: RTI mean earnings rolling annual growth, Scotland and the UK**

**Pay growth in Scotland is now close to the UK average after a period of faster growth**




Description of Figure 2.2: Line chart of RTI data from March 2021 to March 2025 showing that mean pay rolling annual growth in Scotland was slower than in the UK in 2021-22 and 2022-23, faster in 2023-24, and since 2024-25 it has now broadly tracking the UK's.

Source: Scottish Fiscal Commission, Office for National Statistics (2025) [Earnings and employment from Pay As You Earn Real Time Information, seasonally adjusted – August 2025.]

Mean pay growth on a rolling annual basis is the percentage change in mean pay over the latest twelve months compared with the previous twelve months. In March 2023 and March 2024, rolling annual growth is equal to financial-year growth for 2022-23 and 2023-24, respectively.

2.28 For 2022-23 and 2023-24, a comparison of our and the OBR's forecasts had not suggested such a positive earnings growth gap. The positive earnings growth gap that did occur contributed to the positive reconciliations of £451 million and £406 million respectively.

2.29 The OBR's and our budget-setting forecasts from December 2023 and December 2024 had indicated a positive earnings growth gap for both 2024-25 and 2025-26, respectively. However, recent data indicates that this gap has reduced in 2024-25, and this trend may continue into 2025-26. As a result, the projected Income Tax net position has declined for both years, leading to indicative negative reconciliations in the next two Scottish Budgets. This includes a large negative £851 million reconciliation to be applied in the 2027-28 Scottish Budget, which will exceed the borrowing limit if it materialises.

2.30 The projected net positions and reconciliations are based on forecasts from us and the OBR, and will continue to be updated until the final outturn data becomes available. However, RTI earnings data provides a strong indication of how relative earnings growth between Scotland and the UK is changing and what effect this may have on these projections.

## Tax base performance gap

2.31 In our recent reports we have discussed what we termed the 'economic performance gap'. Under the current fiscal framework, the Income Tax net position can move up and down largely because of differences in tax policies and the tax bases in Scotland and the rest of the UK. With the economic performance gap, we try to measure how the performance of the tax base in Scotland compares with that of the rest of the UK. Therefore, we have decided to change the name to 'tax base performance gap'.

2.32 To calculate this, we look at the difference between the Income Tax net position and an illustrative one where we assume Scotland matches the rest of the UK in earnings and employment growth.

2.33 In this illustrative net position, which we refer to as 'policy-only', we show how much more funding the Budget could have received purely from the more progressive Scottish rates and thresholds compared with those in place in the rest of the UK. We last updated it in May 2025 and Figure 2.3 shows this figure is £1,225 million for 2023-24. When compared with the £730 million outturn net position, we can calculate a tax base performance gap of £495 million in 2023-24. This has narrowed by £126 million since May 2025 because of the increase in the outturn net position.

2.34 The tax base performance gap arises because of many factors. The most significant of these are slower aggregate earnings and employment growth in Scotland compared with the rest of the UK, behavioural responses from taxpayers to policy changes, differences in the sectoral make-up of the Scottish economy, and the different distribution of incomes in Scotland and in the rest of the UK.

**Figure 2.3: Tax base performance gap, 2020-21 to 2025-26**

| Collection year | Policy differences only Income Tax net position (£ million) | Income Tax net position (£ million) | Tax base performance gap (£ million) | Tax base performance gap (percentage of SIT revenue) | Income Tax net position status |
|---|---|---|---|---|---|
| 2020-21 | 637 | 96 | -540 | 4.6 | Outturn |
| 2021-22 | 747 | 85 | -662 | 4.9 | Outturn |
| 2022-23 | 877 | 260 | -617 | 4.1 | Outturn |
| 2023-24 | 1,225 | 730 | -495 | 2.9 | Outturn |
| 2024-25 | 1,560 | 562 | -998 | 5.2 | Projected |
| 2025-26 | 1,674 | 616 | -1,058 | 5.2 | Projected |

Source: Scottish Fiscal Commission (2025) Scotland's Economic and Fiscal Forecasts – May 2025

Figures may not sum because of rounding.

2.35 Now that we have final outturn for 2023-24 we can see that the tax base performance gap has remained fairly consistent in the previous four outturn years. It has fallen in nominal terms since 2021-22, coinciding with a period of higher relative earnings growth in Scotland. As a share of SIT revenues, the tax base performance gap became smaller over this period.

2.36 RTI data shows that the earnings growth gap closed in 2024-25, which partly explains the projected increase in the tax base performance gap to £1 billion for that year. To understand this further, we need to compare the latest forecasts from the OBR and SFC for 2024-25.

2.37 The latest forecast of the BGA, based on the OBR's March 2025 forecast, is expected to grow by 12.2 per cent in 2024-25. Our May 2025 SIT forecast increases by a lower rate of 11.2 per cent, resulting in a £168 million decrease in the Income Tax net position. This difference could be caused by factors such as faster UK employment and Self Assessment growth. We will explore this in more depth once outturn data is available.

2.38 At the same time, cumulative policy changes in both Scotland and the UK have led to a £335 million increase in the illustrative policy-only net position in 2024-25. With more progressive Income Tax policies in Scotland, we expect this figure to increase each year, but this is the largest one-year increase so far. This can be explained by the policies introduced in the Scottish Budget that year. The Government increased the top rate and brought in the new advanced rate, which we forecast would raise around £200 million before behavioural responses, such as working fewer hours. Even once we have outturn data, we cannot determine exactly how much revenue is lost because of behavioural responses. However, when the policies were introduced, our estimate was that it would be over half of the forecast revenue.

2.39 While the gap has doubled from 2023-24 to 2024-25, SIT revenues have increased a lot since the start of this decade, so it is helpful to consider the tax base performance gap as a percentage of them. Figure 2.3 shows that in 2021-22 the gap was around 5 per cent, falling to 3 per cent by 2023-24. However, in 2024-25 and 2025-26 the percentage is back to 5 per cent. While the gap has widened substantially in nominal terms, relative to SIT revenues it is comparable to levels seen in 2020-21 and 2021-22.

2.40 The tax base performance gap figures for 2024-25 and 2025-26 have not been updated to reflect the latest outturn. We plan to do this alongside a new SIT forecast, which we will publish alongside the Scottish Budget later this year.

# Pay deals in Scotland

2.41 The Scottish Government's December 2024 public sector pay policy (PSPP) provided the framework for pay negotiations for the devolved public sector for 2025-26 to 2027-28. The PSPP set out a 9 per cent increase over these three years, slightly above inflation expectations at the time, with an increase of 3 per cent being used to set the portfolio allocations in the 2025-26 Scottish Budget.[17]

2.42 Figure 2.4 shows that most of the devolved public sector workforce is now covered by agreed pay deals for 2025-26, and most deals agreed also cover 2026-27. Where agreements have been reached, they all have been at levels above the budgeted 3 per cent in 2025-26, and in some instances with inflation protection clauses. While multi-year pay deals provide the Scottish Government with more certainty on pay costs,

[17] Scottish Government (2024) Scottish Government Public Sector Pay Policy 2025-26. These were based on forecast CPI growth from the Bank of England in November 2024.

the inflation clauses mean the Government is still exposed to the risk that higher inflation leads to higher pay deals than currently planned for.

**Figure 2.4: Agreed pay deals in the devolved Scottish public sector**

| Workforce | Deal in 2025-26 (per cent) | Deal in 2026-27 (per cent) | Inflation protection |
|---|---|---|---|
| NHS Scotland, of which: | | | |
| Agenda for Change [1] | 4.25 | 3.75 | Yes [2] |
| Resident doctors | | | |
| Doctors and dentists | 4.00 | | No |
| Scottish Prison Service | 4.25 | 3.75 | Yes [2] |
| Scottish Fire and Resue Service | 3.20 | | No |
| Local Government | 4.00 | 3.50 | No |
| ScotRail and Caledonian Sleeper | 3.60 | 3.00 | Yes [3] |
| Scottish colleges, of which: | | | |
| Lecturers | 4.14 | | No |
| Support staff | | | |

Source: Scottish Government

[1] Agenda for Change covers most NHS staff other than doctors.

[2] Guaranteed to be at least one percentage point above CPI inflation each year.

[3] Pay in 2026-27 will increase by either 3 per cent or the January 2026 Retail Prices Index, whichever is greater.

2.43 These agreed pay deals cover the first two years of the three-year period covered by the PSPP. Unless deals with nominal pay growth of around 1 per cent are accepted for the final year, the policy of 9 per cent pay increases over three years will be exceeded.

2.44 In recent years the Scottish Government has generally increased public sector pay by a higher percentage than was the case in England. This has the consequence that subsequent pay awards are more costly, as each negotiation starts from a higher base. However, we note that the Scottish Government has generally avoided strike action in Scotland, particularly within the NHS.

2.45 Pay is just one part of the paybill. It also includes employer pension contributions, employer National Insurance contributions (NICs), and is affected by the size and composition of the workforce. The Scottish Government's Fiscal Sustainability Delivery Plan (FSDP), which set out measures to address fiscal challenges in the medium term, included a commitment to a gradual reduction in the devolved public sector workforce.[18] However, the baseline paybill used to set the workforce reduction targets will increase with any new pay deals agreed since the FSDP in June which are above the PSPP. Therefore, pay increases above what was anticipated in June would mean larger workforce reductions required than those announced in the FSDP to keep the paybill at the levels intended by 2029-30. In Chapter 3 we discuss how historical trends suggest

[18] Scottish Government (2025) Fiscal Sustainability Delivery Plan

achieving these reductions in the workforce is likely to be challenging. The Scottish Government will need to set out progress against this target and how it plans to measure the size of the workforce, and how that changes over time.

# Chapter 3
# Trends in Funding and Spending

3.1 In this chapter we discuss trends in funding and spending. These, alongside developments since June, provide an indication on what to expect in the 2025-26 Autumn Budget Revision (ABR), the 2026-27 Scottish Budget, and the Scottish Spending Review (SSR).

## Public Funding

3.2 Funding for the Scottish Budget changes over time. In this section we look at trends for three sources: Barnett funding, the Scotland Reserve and borrowing. We also consider the size of Income Tax reconciliations compared with the resource borrowing limits.

### Barnett funding

3.3 The Block Grant is updated every time the UK Government changes its spending plans for departments in devolved areas. The Scottish Government receives a population share of those through the Barnett formula. This is the largest source of funding for the Scottish Budget, and changes to the Block Grant contribute to the volatility in funding which the Scottish Government has to manage both in-year and between years.

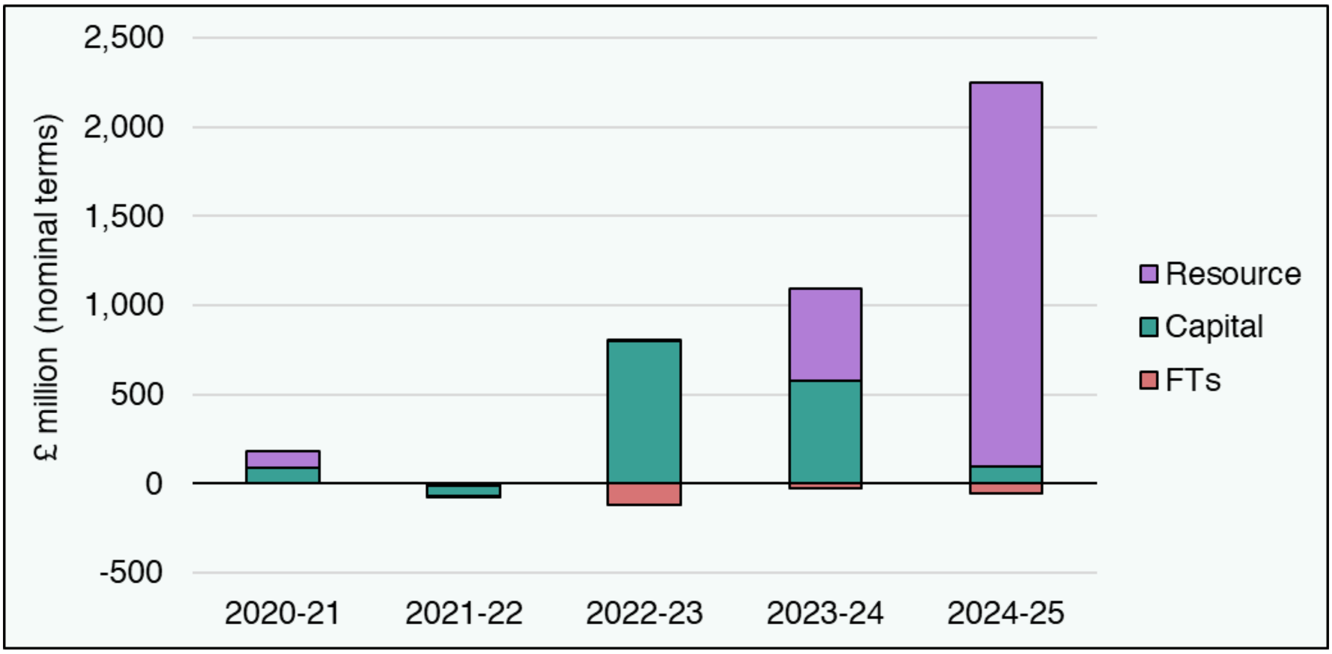
3.4 Figure 3.1 shows how Barnett funding has changed in-year: we compare the position when the Scottish Budget is set with the outturn position, excluding COVID-19 related funding. The in-year changes vary significantly between years, and are different for resource, capital, and financial transactions (FTs). In 2021-22 funding decreased for all three, whereas, in 2022-23, capital funding increased but FTs funding decreased, with resource seeing little to no increase. The most significant in-year changes were in 2024-25, specially in resource, following the UK election.

3.5 These changes all depend on UK Government spending decisions and it is difficult to predict when the UK Government will change its spending plans in-year from those set out in the most recent UKSR. The Scottish Government has limited tools available to manage this volatility. It can change its spending plans during the year, or can alter borrowing or its planned use of the Scotland Reserve or ScotWind funding. There have been occasions in the past when the UK Government has also agreed to flexibilities which effectively allowed the Scottish Government to by-pass the limits of the Reserve, but these are at the discretion of the UK Government and not guaranteed.[19] Overall, the Scottish Government is required to maintain a broadly balanced budget and can transfer a limited level of underspend to the next financial year through the Scotland Reserve.

[19] Scottish Fiscal Commission (2020) Fiscal Update – September 2020. Late consequentials of £148 million in 2018-19 were deferred to 2019-20. In 2019-20 the Scottish Government was allowed to draw down more from the Scotland Reserve than the limit at the time, to manage negative Barnett consequentials which arose in-year. An in-year reconciliation in 2019-20 was deferred until 2020-21 to avoid a late change after the UK Budget in March. An earlier precedent was in 2010-11, when HM Treasury allowed the deferral of in-year reductions to the Block Grant for Devolved Administrations at the Spending Review 2010. See Footnote 9 to Table 1 in HM Treasury (2010) Spending Review 2010.

**Figure 3.1: Changes in Barnett funding in-year**

**The size and source of in-year changes to the Block Grant has grown over time**




Description of Figure 3.1: Stacked column chart showing the in-year changes through the Barnett formula for resource, capital, and financial transactions from 2020-21 to 2024-25. The in-year changes vary significantly between years, and are different for resource, capital and financial transactions (FTs). In 2021-22 funding decreased very slightly for all three. In 2022-23, capital funding increased, but FTs funding decreased, with resource seeing no increase. 2024-25 saw the largest increase in resource funding of all years.

Source: Scottish Fiscal Commission, Scottish Government.

Excludes COVID-19 funding in 2020-21 and 2021-22, which was significantly larger than the changes seen in any other years.

## Scotland Reserve

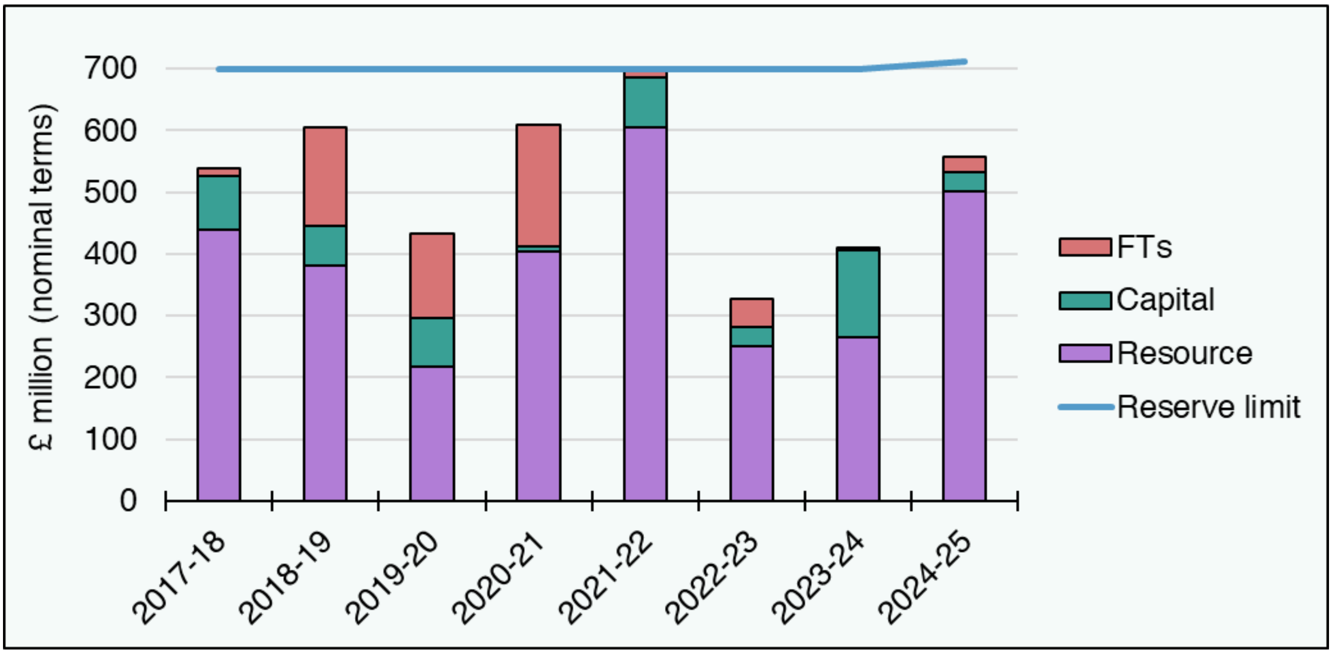
3.6 The Scotland Reserve allows the Scottish Government to move funding between years. It has existed since 2017-18. The cap was £700 million in 2023-24 and since then has risen in line with inflation. While there are three separate accounts (resource, capital, and financial transactions) they do not have separate limits within the total cap.

3.7 The Scottish Government is required to maintain a broadly balanced budget and cannot spend more than it has available in funding for a given year. As a result, the budget management process tends to produce underspends which are carried forward in the Scotland Reserve. In 2025-26 the Scotland Reserve limit of £751 million represents 1.3 per cent of the total discretionary budget.

3.8 Figure 3.2 shows the closing balance for the Scotland Reserve between 2017-18 and 2024-25. The Scottish Budget has grown every year, but the reserve limit only began to increase in 2024-25. The Reserve was almost fully used once in 2021-22. Any Reserve balance over the limit must be returned to the UK Government, meaning the Scottish Government has a very strong incentive to ensure this doesn't happen, and the upper limit of the Reserve is an important constraint when managing the budget. In 2022-23, despite a larger budget, the closing balance of the Reserve was the lowest level since 2017-18.

**Figure 3.2: Scotland Reserve usage trends**

**Use of the Reserve fell from 2022-23 despite growing budgets, coinciding with ScotWind**




Description of Figure 3.2: Stacked column chart showing the closing balance of the resource, capital, and financial transactions accounts in the Scotland Reserve from 2017-18 and 2024-25. A line on top shows the overall reserve limit. The Reserve was almost fully used in 2021-22 with a balance of £699 million. In 2022-23, despite a larger budget, the closing balance of the Reserve was the lowest level since 2017-18.

Source: Scottish Fiscal Commission, Scottish Government.

3.9 ScotWind is another funding source available to the Scottish Government. Since 2022-23 proceeds from the ScotWind leasing programme run by Crown Estate Scotland, ScotWind, and other smaller Crown Estate Scotland programmes, provide a source of revenue which the Scottish Government can use at its discretion and can hold separately to the Scotland Reserve. This provides another tool for the Scottish Government to use to manage its budget. Typically, the Scottish Government has planned to use ScotWind income when the Budget was set and, as there is greater certainty on the final funding and spending position, it has reduced the use of ScotWind income. This strategy has reduced the level of funding, and therefore the level of underspends, which need to be stored in the Reserve. This may partly explain why the level of funds held in the Scotland Reserve has been lower since 2022-23 than in previous years.

3.10 Figure 3.2 also compares the closing balance of the resource, capital, and FTs accounts in the Scotland Reserve. Typically, the Scottish Government uses the Reserve much more for capital and FTs than these components' share of the Scottish Budget. Around 85 per cent of the total Scottish Budget is for resource funding, around 12 per cent for capital, and just about 1 per cent for FTs.

3.11 Resource generally accounts for a lower share of the Reserve than of the Budget. This indicates the Scottish Government generally spends most of its resource budget. In contrast, FTs account for a disproportionate share of the reserve.

## Borrowing

3.12 The Scottish Government has had borrowing powers since 2016. It can borrow to top up resource or capital funding in some circumstances. It sets the Budget each year based on a planned level of borrowing and may revise these plans at Budget Revisions. However, the Scottish Government finalises borrowing plans towards the end of the financial year, when it has a better idea of the latest budgetary position.

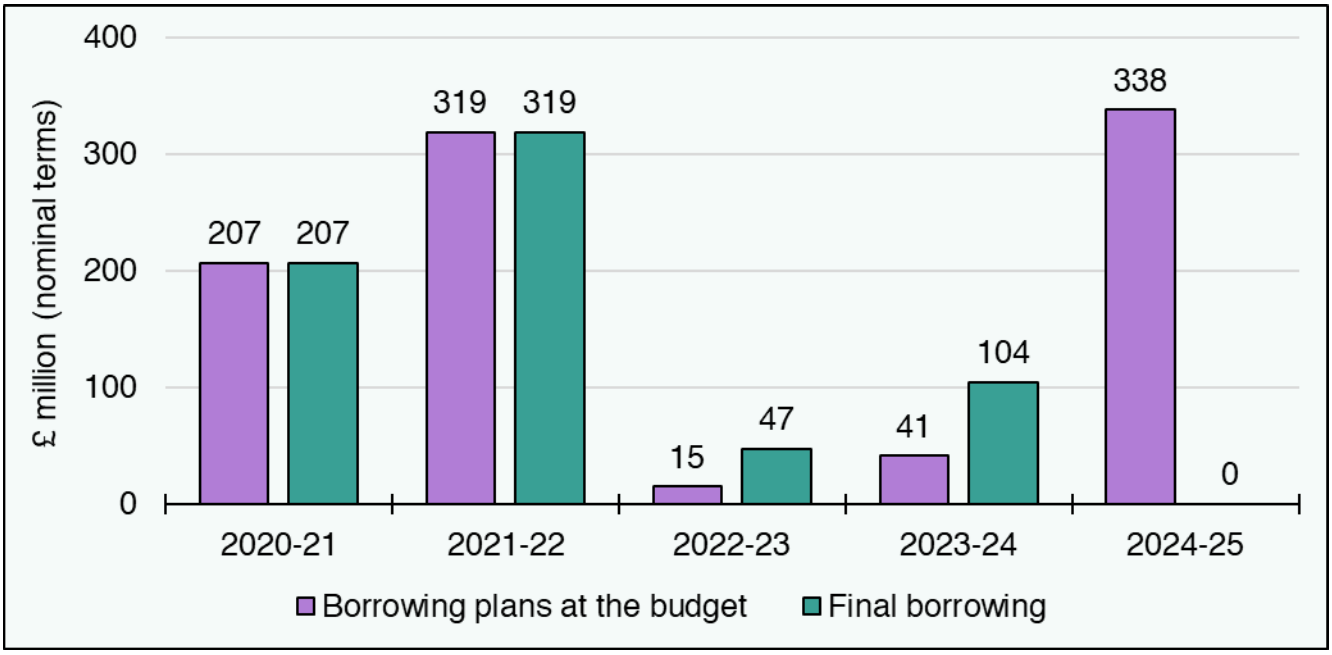
### Resource

3.13 Resource borrowing is only available when there is a forecast error that is unfavourable to the Scottish Budget. This can be because of devolved tax revenues being lower than forecast, social security spending being higher than forecast, a negative Income Tax reconciliation, or unfavourable in-year adjustments to the associated BGAs.

3.14 The annual limit for up until 2023-24 was £600 million, and the overall debt stock was capped to £1.75 billion. Since then, both limits rise in line with inflation.[20]

**Figure 3.3: Scottish Government resource borrowing trends**

**The Government has broadly stuck to initial borrowing plans, except in 2024-25**




Description of Figure 3.3: Column chart showing resource borrowing trends from 2020-21 to 2024-25, comparing borrowing plans when each budget was set with the final level of borrowing in each year. In 2020-21 and 2021-22 the Government borrowed as initially planned. In 2022-23 and 2023-24, the Scottish Government borrowed more than originally planned. In 2024-25 the Scottish Government reduced its borrowing to zero from a planned £338 million.

Source: Scottish Fiscal Commission, Scottish Government.

3.15 The Scottish Government first borrowed for resource in 2020-21. Figure 3.3 compares resource borrowing plans when each Budget was set with the final level of borrowing in each year. The Government has generally planned to borrow to offset the impact of negative Income Tax reconciliations. In 2023-24, despite the first positive Income Tax

[20] As measured by the growth in the GDP deflator, calculated by the Office for National Statistics and forecast by the OBR for future years.

reconciliation, the Budget was set including planned borrowing because of unfavourable final reconciliations relating to the BGAs for fully devolved taxes and social security.

3.16 In 2020-21 and 2021-22 the Government borrowed as initially planned. In 2022-23 and 2023-24, it borrowed more than originally planned by £32 million and £63 million, respectively. In those years, larger-than-expected unfavourable forecast error based on the Office for Budget Responsibility (OBR) forecasts in the autumn meant the Scottish Government was able to borrow more.

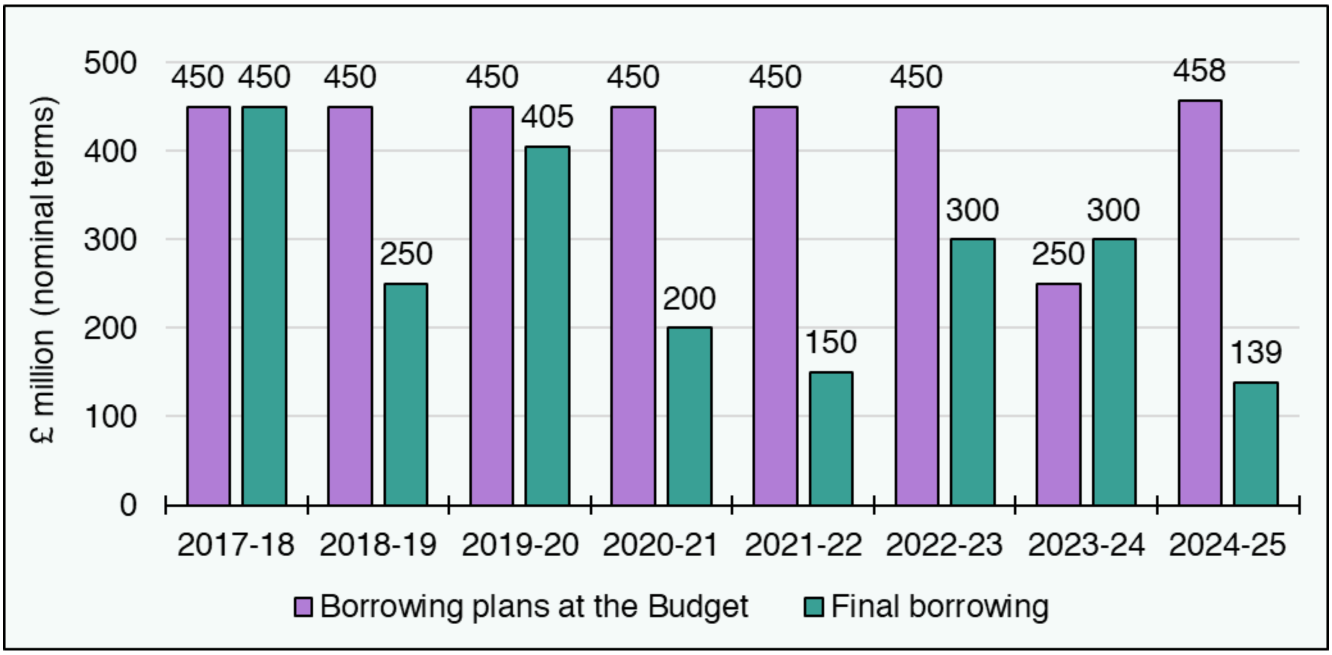
3.17 In 2024-25 the Government reduced its borrowing to zero from a planned £338 million, even though a negative reconciliation of that magnitude applied to the 2024-25 Budget. This was because large in-year Barnett consequentials from the UK Budget 2024 made the spending plans deliverable without borrowing. By not borrowing, the Government reduced future repayments, increasing how much is available to spend in future years.

## Capital

3.18 The Scottish Government can increase capital spending through borrowing, within the limits of the fiscal framework. The annual limit for up until 2023-24 was £450 million, and the overall debt stock was capped at £3 billion. Since then, both limits rise with inflation.

**Figure 3.4: Scottish Government capital borrowing trends**

**The Government generally reduces its capital borrowing plans during the year**




Description of Figure 3.4: Column chart showing capital borrowing trends from 2017-18 to 2024-25, comparing borrowing plans when each Budget was set with the final level of borrowing in each year. In 2017-18 the Government borrowed as initially planned. In years 2018-19 to 2022-23, the Scottish Government initially planned to borrow £450 million but reduced the borrowing. In 2023-24, the borrowing was increased by £50 million. In 2024-25, the Scottish Government reduced the borrowing down to £139 million from £458 million.

Source: Scottish Fiscal Commission, Scottish Government.

3.19 Figure 3.4 compares the capital borrowing plans at each Budget with final Scottish Government borrowing decisions. The Scottish Budget has generally been set based on plans to borrow the maximum allowed, but borrowing has then reduced as the financial year progresses. The exceptions are 2017-18, when the final borrowing stayed the same as the original plan, and 2023-24 when borrowing increased during the year.

3.20 This trend reflects the Scottish Government's approach to managing the capital budget. By basing spending plans on the maximum borrowing possible, the Government gives itself greater flexibility. It can then reduce that borrowing during the year to avoid large underspends which might arise from managing a large number of complex capital projects, and ensure any unanticipated capital Barnett consequentials arising late in the financial year can be managed within the limits of the Scotland Reserve.

## Probability of Income Tax reconciliations

3.21 In January 2021 we considered how Income Tax reconciliations might vary over time and compared this with the resource borrowing limits at the time.[21] That analysis estimated a 12 per cent chance of Income Tax reconciliations exceeding £600 million.[22]

3.22 We have now repeated the analysis based on the latest outturn data and the historical forecast errors for both Scottish Income Tax (SIT) revenues and UK Government Income Tax revenues. Both SIT revenues and the BGA have grown from around £12 billion in 2021 to around £20 billion today. This nominal increase alone is likely to significantly increase the nominal value of forecast errors and therefore of reconciliations. We now estimate a 24 per cent chance of a negative reconciliation exceeding £600 million, or approximately one year in four. This suggests the volatility to which the Scottish Budget is exposed from Income Tax reconciliations has increased over the last four years.

### Changes since January 2021

3.23 We have updated this analysis based on outturn data from 2017-18 to 2023-24. We now assume an average absolute forecast error of 6.6 per cent.[23] This is higher than we had assumed in January 2021.

3.24 When we did the analysis in January 2021 the resource borrowing limit was fixed at £300 million a year, doubled to £600 million a year when certain conditions were met. From 2024-25, it has been £600 million and grown by inflation each year. However, in this analysis we have considered both SIT revenues and the borrowing limits fixed.

3.25 Figure 3.5 shows the results of our simulations. In our central case, a negative reconciliation exceeding £600 million could occur 24 per cent of the time, or approximately once in every four years. As we assume the distribution of reconciliations

[21] See Annex D of Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – January 2021. We simulated 100,000 forecasts of Scottish Income Tax (SIT) and the Block Grant Adjustment (BGA) and combined these to generate a distribution of potential reconciliations.

[22] In our central case we assumed SIT and BGA errors followed a normal distribution. Both SIT and BGA had an assumed average absolute forecast error of 5.7 per cent, which we took as the variance of the distribution. We assumed a 50 per cent correlation between SIT and BGA forecast errors.

[23] We now assume the correlation between the SIT and BGA forecast errors is 80 per cent as we have observed a high correlation in the forecast errors.

is symmetrical, the likelihood of the positive reconciliations is the same as the likelihood of negative ones.

**Figure 3.5: Probability of reconciliations exceeding borrowing limit, per cent**

| Forecast error | Correlation | Probability of a reconciliation larger than negative £600 million | Probability of a reconciliation larger than £600 million |
|---|---|---|---|
| **Central case** | | | |
| 6.6 | 80.0 | 24.0 | 24.0 |
| **Varying average absolute forecast error** | | | |
| 2.0 | 80.0 | 1.0 | 1.0 |
| 11.0 | 80.0 | 33.0 | 33.0 |
| **Varying correlation** | | | |
| 6.6 | 40.0 | 34.0 | 34.0 |

Source: Scottish Fiscal Commission, Scottish Government.

3.26 We also tested the sensitivity of our results to changes in the underlying assumptions. The larger the average absolute forecast error, the greater the chances of a reconciliation exceeding £600 million. We varied our assumed forecast error between 2 per cent and 11 per cent. The lower scenario reduces the probability of reconciliations exceeding the borrowing limits to be around 1 per cent. On the other hand, in the higher scenario reconciliations exceeding negative £600 million could occur as often as once every three years.

3.27 Varying the correlation of SFC and OBR forecast errors also has an important effect on how often the borrowing limits are exceeded. If forecast errors were less correlated, the chances of reconciliations exceeding £600 million would increase. The size of the reconciliation is very sensitive to the correlation, or similarity, of our and the OBR's forecast errors. This highlights a feature of the fiscal framework. Reconciliations will tend to be smaller if we and the OBR make similar forecast errors, and larger when our forecast errors go in a different direction to the OBR.

# Public Spending

3.28 This section considers devolved public spending trends using the UN's Classification of the Functions of Government (COFOG).

3.29 We presented similar analysis in December 2024, which took account of the 2025-26 Budget plans at that time and the Autumn Budget Revision (ABR) position for 2024-25. We now repeat this analysis, using the 2025-26 plans which were amended as the Budget Bill progressed through the Parliament, and the provisional outturn position for 2024-25.

## Reallocation of funds

3.30 Budget Revisions usually take place twice a year: once in autumn around September, and once in spring around February. Each allocates new funding and redistributes funding already allocated. New funding could be Barnett consequentials or increases to other sources of funding that were not anticipated, or funding that had been held centrally for contingencies.

3.31 For at least a decade there has been no instance of overall discretionary funding levels going down in-year, and the Scottish Budget has grown with each revision. Therefore, spending reductions in any one area are made to increase spending either in another area or in another financial year.

3.32 Within a financial year there can be two reasons for a reallocation. One is when an underspend arises in one area which the Scottish Government transfers to another area. The other is when the Scottish Government requires savings to be made within an area either because it expects greater spending pressures in another area or because savings are harder to make elsewhere.

3.33 The data we work with does not allow us to distinguish between mandated savings or the surrendering of underspends. The Scottish Government decides any required reallocations in each financial year. Figure 3.6 provides a breakdown of changes in in-year spending.

3.34 Up to 2023-24, there was little reassignment of resource spending in-year. In 2020-21 and 2021-22, unanticipated COVID-19-related Barnett consequentials allowed increases in spending without needing to reallocate funding. However, from 2023-24, some areas have seen their budget reduce in-year to increase spending elsewhere. This happened at the same time as the Scottish Government introducing spending controls.[24] In 2023-24, a substantial share of the in-year spending reductions came from Education, mostly from the Scottish Funding Council and higher education student support.

3.35 Spending on social protection has never been reduced in-year other than in 2024-25. In summer 2024, the Scottish Government decided to replicate for its Pension Age Winter Heating Payment the immediate means-testing of Winter Fuel Payments the UK Government had announced.[25] It implemented the saving in the ABR, alongside a reduction in the corresponding BGA.[26]

3.36 Redeployments of capital and FTs spending tend to be large relative to how much is spent on them overall. For capital, there have been large in-year reductions for Environmental Protection in three of the last six years, relating to grants for energy efficiency and decarbonisation. For Transport, the only significant in-year reduction was in 2023-24, and it lowered the financial support to CalMac, the public corporation in charge of ferry services in Scotland. Similarly, for Housing (which also covers water supply) the in-year spending reduction was notable only in 2022-23, mostly because

[24] See Scottish Government (2025) Correspondence regarding emergency spending controls: FOI release for 2023-24 and Scottish Government (2024) Urgent action to balance Budget for 2024-25

[25] Scottish Government (2024) UK Government decision ends universal fuel payments

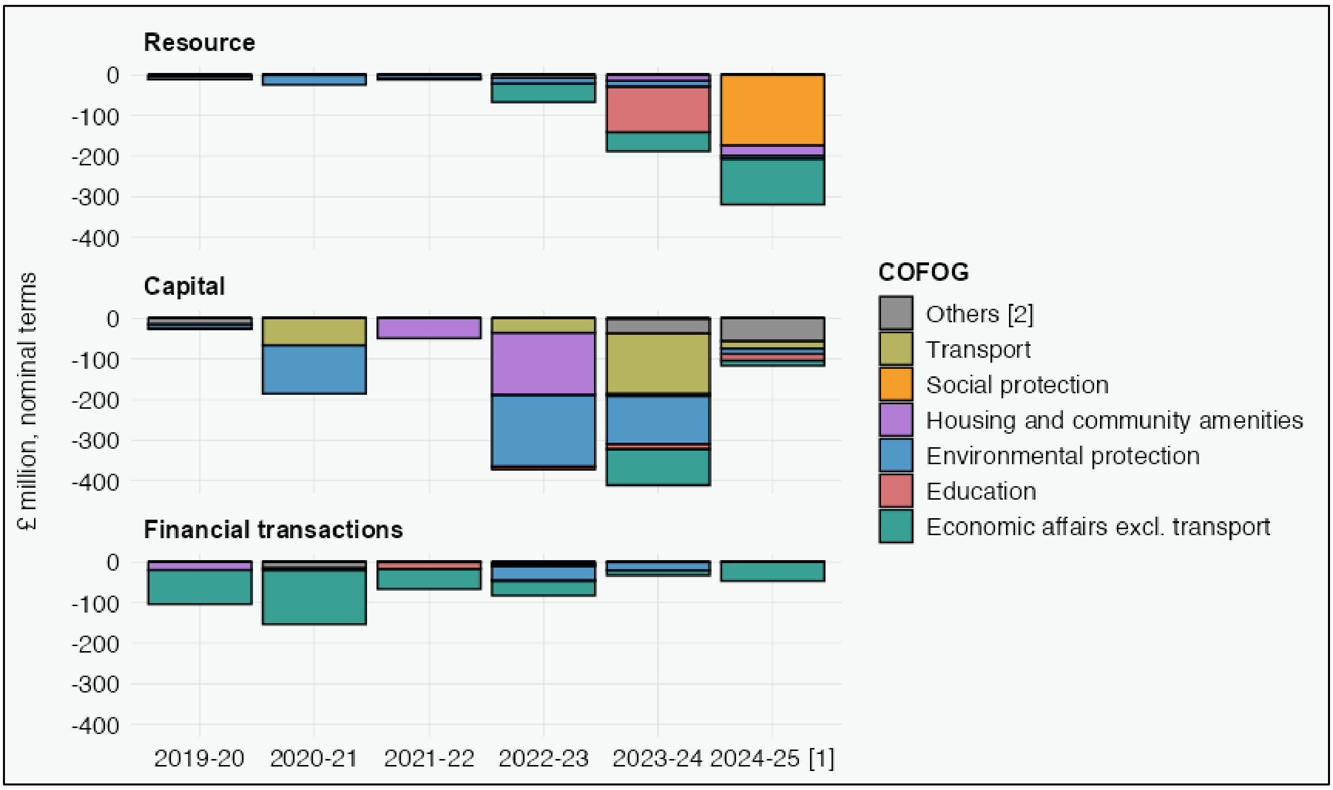
[26] See Schedule 3.7. Scottish Government (2024) Autumn Budget Revision 2024-25.

less money was provided to Scottish Water, another public corporation, and because less was spent on the More Homes programme.

3.37 For FTs, spending on Economic affairs other than transport is the area that regularly sees reductions in spending in-year. This relates to lending by the Scottish National Investment Bank (SNIB).[27] In all these cases, in-year spending reductions are more likely to be because, as the year evolves, underspends have emerged.

**Figure 3.6: In-year spending reductions by COFOG and control aggregate**

**Capital sees the largest in-year spending reductions, but they are becoming more important for resource since 2023-24**




Description of Figure 3.6: Three stacked column charts showing in-year spending reductions in resource, capital and financial transactions by COFOG category between 2019-20 to 2024-25. Capital has seen the biggest in-year reductions in spending, especially in 2022-23 and 2023-24 in environmental protection. Resource in-year spending reductions have increased over the years with 2024-25 seeing the highest reductions. Financial transactions saw the highest reduction in 2020-21, with most of it being in Economic affairs excluding transport.

Source: Scottish Fiscal Commission, Scottish Government.

[1] Provisional outturn. Final outturn will be confirmed with the Scottish Budget final outturn report in spring 2026.

[2] Groups together General public services, Health, Public order and safety, and Recreation, culture and religion.

[27] Scottish Government (2022) Consolidated Accounts: year ended 31 March 2022. The SNIB underspent 26.5 per cent of its capital allocation and the document states it 'invested less than its ambitious forecast' in the context of it being the bank's first year in operation.

## Spending trends

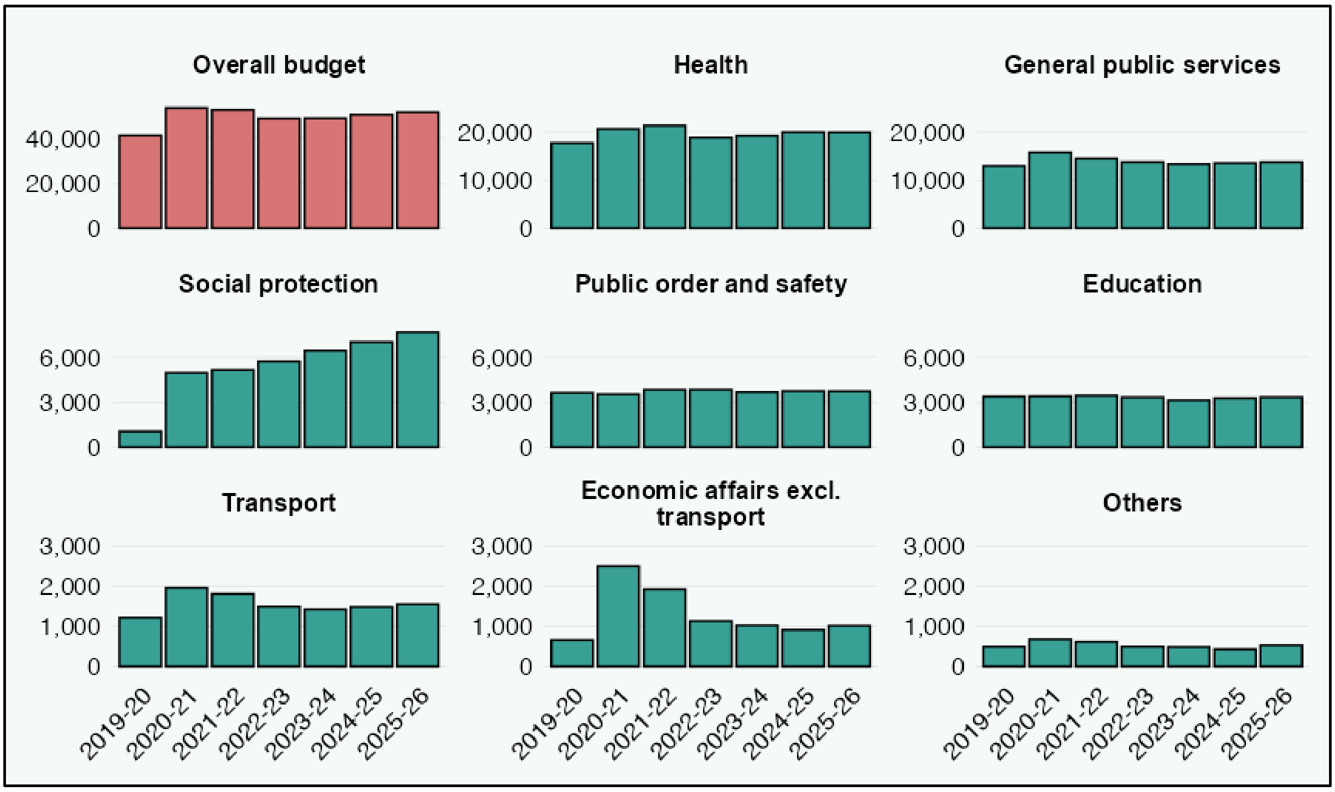
### Resource

3.38 Figure 3.7 shows trends in resource spending, which is used for day-to-day running costs, such as buying services and paying staff.

3.39 The UK Government's response to the COVID-19 pandemic meant resource spending grew significantly in 2020-21. Spending fell to more normal levels within a couple of years as pandemic-related funding tailed off and has grown more gradually since 2022-23.

**Figure 3.7: Resource spending trends by COFOG category, £ million (2025-26 prices)**

**Only social protection spending has grown rapidly within a resource budget that has risen modestly since the pandemic**




Description of Figure 3.7: Nine column charts showing how resource spending levels by COFOG category have changed in real terms from 2019-20 to 2025-26. Overall resource spending grew rapidly during 2020-21 and 2021-22, but fell in 2022-23 and has grown more modestly since then. Health spending followed a similar trend but is flat between 2024-25 and 2025-26. Social protection spending sees a step-change in 2020-21 and grows rapidly thereafter. Public order and safety, and general public services, are broadly flat over the seven-year period.

Source: Scottish Fiscal Commission, Scottish Government.

Figures exclude in-year budget-neutral transfers, except those which have been baselined in 2025-26. See Box 2.1 of the December 2024 SEFF for more details.

Figures have presentational adjustments made for the Verity House Agreement in 2022-23 and 2023-24. Prior to 2022-23, we have made a manual adjustment to Early Learning and Childcare grants to local government to ensure numbers are more consistent with the later presentational adjustments. See 'COFOG and presentational adjustments' in Annex A of Spending trends in the 2024-25 Scottish Budget for more details.

3.40 Figure 3.7 also shows the Scottish Government's choices. The largest area of resource spending, health, grew rapidly in 2020-21 and 2021-22 because of the pandemic. Health spending fell in real terms in 2022-23 but remained above pre-pandemic levels, and has grown gradually since. However, based on the 2025-26 Budget plans, spending will be broadly the same in real terms as in 2024-25. With a growing resource budget, it means that the share of the budget spent on health will fall slightly relative to 2024-25.[28]

3.41 'General public services' includes the main funding provided by the Scottish Government to local government, and saw spending grow in 2020-21. In 2020-21 extra support was given to local authorities because of public health restrictions; this support included funding to counter a loss in revenue from temporary reliefs for Non-Domestic Rates. Spending in this category fell in 2021-22, although it remained above pre-pandemic levels. It then fell in real terms until 2023-24, but has grown since. Based on the 2025-26 Budget plans, spending in this area will be 9 per cent above 2019-20 levels in real terms.

3.42 Social protection covers social security payments and saw a jump in spending in 2020-21, when responsibility for most devolved social security payments was transferred to the Scottish Government and the Scottish Child Payment was launched.[29] Social protection has seen the fastest growth among the major areas of resource spending since then, partly because Scottish Child Payment was extended to cover all children in 2022-23. Based on 2025-26 Budget plans, spending on social protection will be 55 per cent above 2020-21 levels in real terms. This increase is because of the Scottish Government's expanded policies on social security and rising numbers of people receiving disability payments in Scotland as well as across the UK.

3.43 Spending on public order and safety, and on education, has remained stable in real terms over the seven-year period analysed.

3.44 Transport and economic affairs were the two areas with the largest proportional increase in resource spending during the pandemic. Grants were made to public transport operators and widespread business support was rolled out to accompany the Scottish Government's public health restrictions. Post-pandemic, spending on economic affairs other than transport fell back to almost pre-pandemic levels. In contrast, spending on transport remained significantly higher, because greater support is required as rail passenger numbers have not recovered to pre-pandemic levels.[30]

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[28] See the 'Comparator at Budget time' section in Chapter 5 to understand why this differs from the presentation of year-on-year growth rates in the 2025-26 Budget documents.

[29] Scottish Child Payment was launched in 2020-21, and the main disability and carer payments were devolved in 2020-21, transferring the legal and financial responsibility for those then. Two other payments were devolved later: Cold Weather Payments in 2022-23 and Winter Fuel Payments in 2024-25.

[30] Transport Scotland (2024) Summary Transport Statistics. In 2023-24 rail passenger numbers were still 16 per cent below 2019-20 levels.

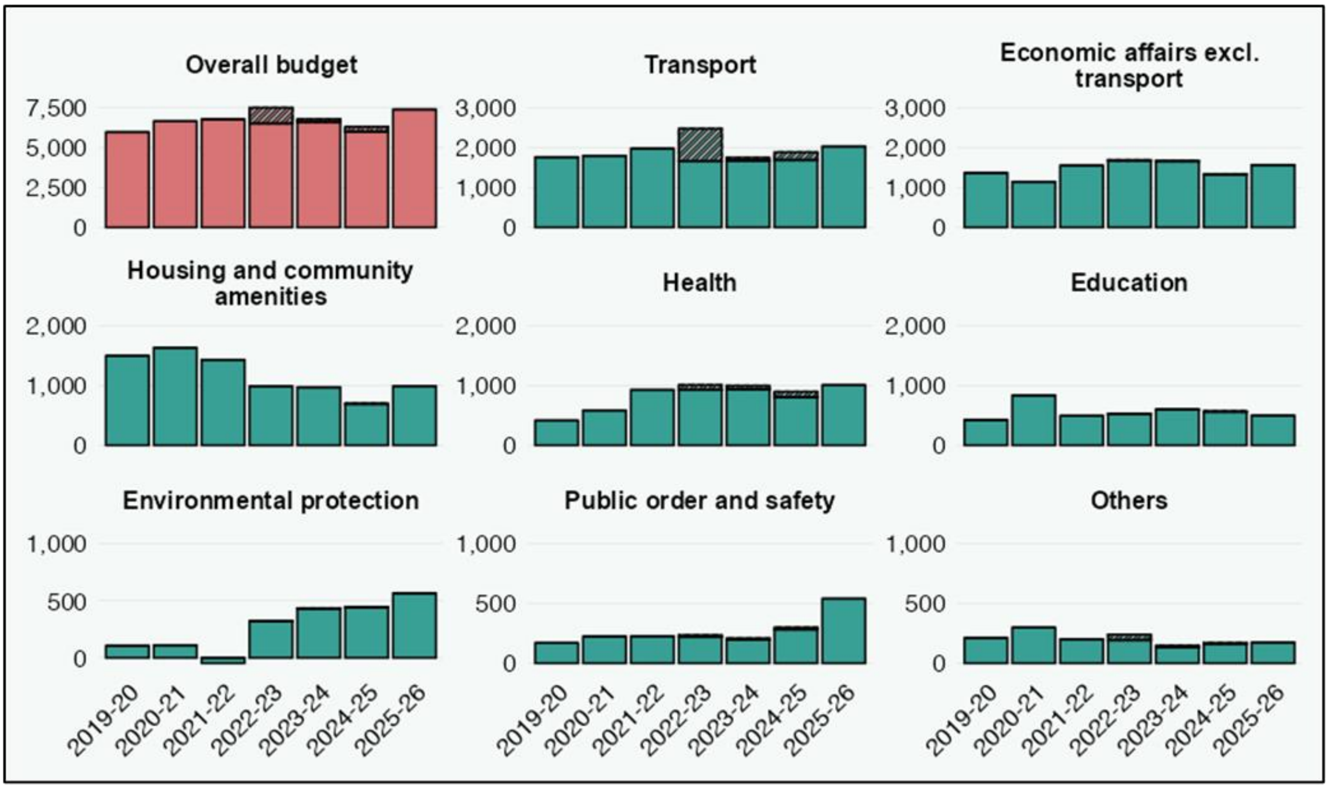
## Capital

3.45 Capital relates to investments in physical assets, such as roads and hospitals, or in financial assets such as loans from the Scottish National Investment Bank (SNIB).[31]

3.46 As for resource, Figure 3.8 shows that trends in capital spending vary for different areas, reflecting the Scottish Government's choices. Overall spending grew from 2019-20 to 2021-22 in real terms but flattened after and fell in 2024-25.[32] After the General Election in 2024, the UK Government increased in capital spending sharply. This boosted the Scottish Government's capital spending, returning the capital budget to 2022-23 levels.

**Figure 3.8: Capital spending trends by COFOG category (£ million, 2025-26 prices)**

**Health prioritised within a broadly flat capital budget, but public order and safety benefits the most from the uplift in 2025-26**




Description of Figure 3.8: Nine column charts showing capital spending levels by COFOG in real terms from 2019-20 to 2025-26. Overall capital spending would have been broadly flat from 2020-21 to 2024-25 had it not been for IFRS16-related adjustments. Capital spending on health grew rapidly up to 2022-23 and has remained at that level since. Meanwhile, spending on housing and community amenities has declined over time. All COFOG categories other than education see an increase in spending in 2025-26, coinciding with the uplift to the overall capital budget, but public order and safety sees the greatest relative rise.

Source: Scottish Fiscal Commission, Scottish Government.

The striped part relates to IFRS16 spending, which was fully funded by the UK Government.

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[31] Spending through financial assets such as loans is classified as FTs and is a subset of capital spending. For the purposes of this analysis, we are including FTs within capital spending.

[32] Ignoring spending related to the implementation of IFRS16, which the UK Government fully funded, and is shown striped in Figure 3.8.

3.47 The largest area of capital spending is Transport which has broadly followed a similar trend to the overall capital budget. The exception is 2024-25 when it was protected in real terms despite falls in the overall capital budget. However, it then grew by less than the overall capital budget in 2025-26.

3.48 Economic affairs (other than transport) fell in 2020-21 despite a slightly larger budget overall. Since then, the category has broadly followed the general trend.

3.49 Housing and community amenities declined steadily even in the context of flat levels of capital spending overall until 2024-25. In 2025-26 capital spending in this area has recovered but remains below pre-pandemic levels.

3.50 Health and Environmental protection increased rapidly, albeit from low bases, and stabilised in 2022-23. Both areas benefited from the increase in overall capital spending in 2025-26.

3.51 Environmental protection is negative in 2021-22 because, even though outturn data shows some capital spending in this area (£106 million), it was less than the in-year internal transfers made to this category in Budget Revisions (£145 million). We must remove these from the outturn data to meaningfully compare to spending plans for 2025-26, because the Budget-setting plans showed only some of the recurrent in-year internal transfers in the portfolio actually incurring the spending. Chapter 5 discusses this issue in more detail.

3.52 Education had particularly high capital spend in 2020-21, but this was a one-off and spending has been at lower levels since then.

3.53 Public order and safety, which saw flat capital spending for six years, has higher spending in 2025-26 because of the planned building of new prisons.

3.54 It is important to note that trends for capital spending can be less informative over a short period because of the inherent lumpiness of investment. Some portfolios may see a large project every few years, with peaks of investment, rather than a regular stream of capital spending. For example, the higher capital spending on public order and safety in 2025-26 is to build two new prisons, and so we might expect capital spending in this area to fall back in future years as the projects are completed.33

## Public sector workforce

3.55 We presented developments on public sector pay in Chapter 2. Other than pay, the size of the workforce is the other main variable in managing the paybill. In its Fiscal Sustainability Delivery Plan (FSDP), the Scottish Government committed to a gradual reduction in the public sector workforce of an average of 0.5 per cent a year for the next five years, “with frontline services remaining protected”.[34]

3.56 The Government stated that this will be achieved by letting the workforce shrink as staff leave and retire without hiring replacements, known as ‘natural attrition’. Voluntary

[33] Scottish Government (2025) Scottish Budget 2025-26: Finance Secretary’s statement

[34] Scottish Government (2025) Fiscal Sustainability Delivery Plan

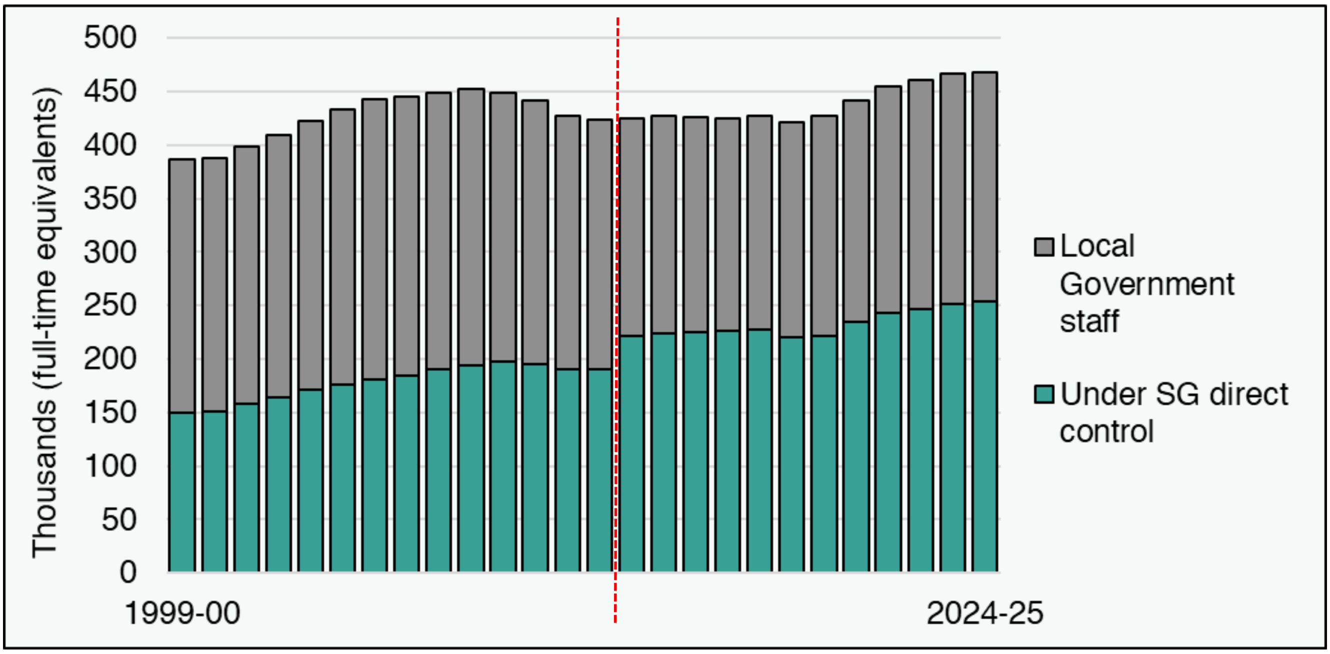
redundancies may also be used. The Government also stated that compulsory redundancies would be considered only in extreme cases.[35]

3.57 'Frontline services' is not a well-defined term, and it is not yet clear exactly which parts of the public sector will be protected. In addition, frontline services often rely on a range of support from back-office staff. Protecting one group of public sector workers means that the other categories must face greater than a 0.5 per cent average annual reduction.

3.58 Moreover, achieving a reduction would be a significant departure from recent trends. Figure 3.9 shows that the devolved public sector workforce has grown each year since 2018-19. Prior to that, it was broadly constant compared with the beginning of devolution in 1999 only because of falls in the number of local government employees in the decade since 2007-08. Although police and fire services were centralised in 2013-14, decisions on local government staffing levels are still mainly taken by Scottish local authorities. In contrast, the workforce under the Scottish Government's direct control has risen almost every year since the beginning of devolution.

**Figure 3.9: Devolved public sector workforce, by layer of government**

**The workforce under the Government's direct control grew each year since devolution**




Description of Figure 3.9: Stacked bar chart showing the size of the devolved public sector workforce in full-time equivalent from 1999-00 to 2024-25. The part that is under the Scottish Government's direct control has grown every year except 2018-19. Local Governments' workforce grew before 2007-08, then shrank for a decade, and grew again from 2018-19.

Source: Scottish Government (2025) Public Sector Employment Statistics

Quarterly levels have been averaged by financial year.

Dashed line represents the point at which police and fire services were centralised (2013-14), so were no longer part of local government staff.

3.59 Figure 3.10 breaks down the workforce under the Scottish Government's direct control. NHS Scotland is the largest workforce and has been growing steadily since 1999,

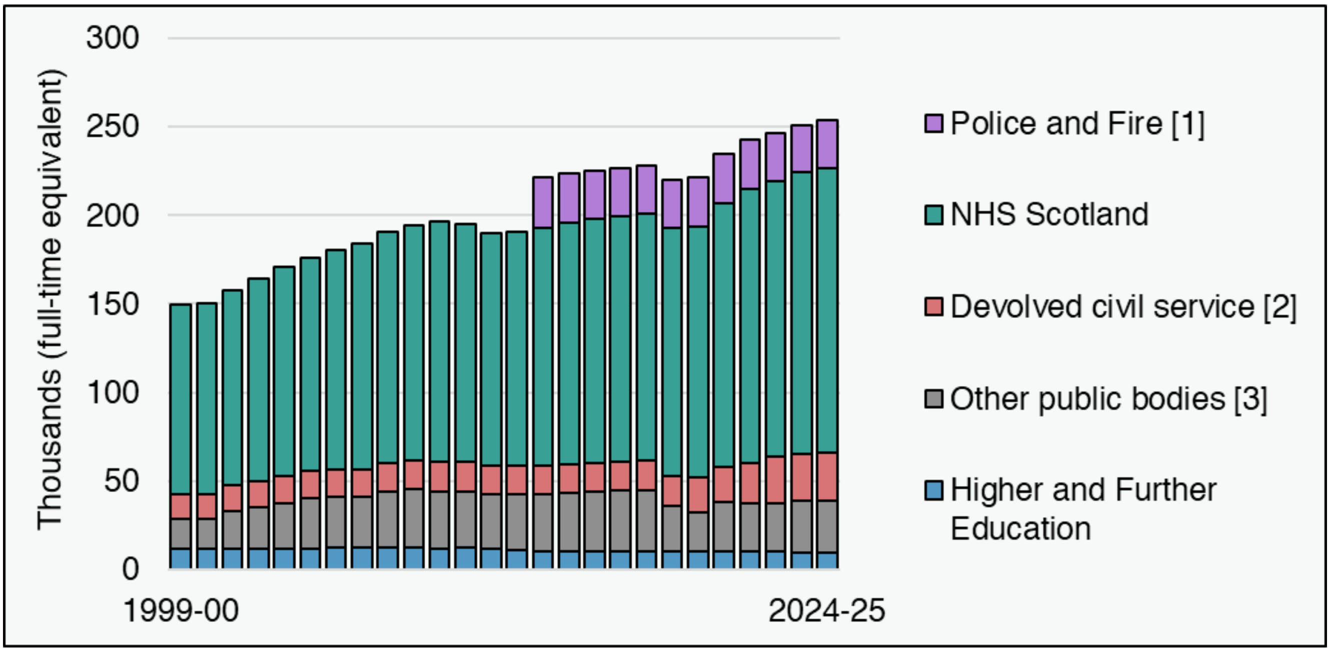
[35] Scottish Parliament (2025) Official Report: meeting of the Parliament 25 June 2025

except for small decreases in 2010-11 and 2011-12. In our Fiscal Sustainability Report, we showed how population ageing is likely to put pressure on health services in the long term. This pressure, and the commitment to protect frontline services, mean there is little scope for workforce reductions in the NHS without large productivity gains.

3.60 The devolved civil service, which had been broadly stable in size since the beginning of devolution, has grown rapidly since 2018-19. By 2024-25, it was almost 60 per cent larger than in 2018-19. The creation of new executive agencies such as Social Security Scotland to deliver the newly devolved social security payments is one cause. However, the core Scottish Government also grew rapidly. This is partly because of the COVID-19 pandemic response, and partly because of preparing for the UK's exit from the EU.[36]

**Figure 3.10: Devolved public sector workforce without local government, by sector**

**Within the groups under the Scottish Government's direct control, the NHS and the devolved civil service have grown most rapidly**




Description of Figure 3.10: Stacked bar chart showing the size of the public sector workforce under the Scottish Government's direct control from 1999-00 to 2024-25, in full-time equivalent. Higher and further education is broadly flat over time. Other public bodies fluctuate, growing until 2008-09, stabilising, and falling again from 2018-19. The devolved civil service was broadly flat until 2017-18 but then grows rapidly. NHS Scotland grows steadily over time, except for 2010-11 and 2011-12. Police and Fire is added in 2013-14 and remains broadly constant from then.

Source: Scottish Government (2025) Public Sector Employment Statistics

Quarterly levels have been averaged by financial year.

[1] Police and fire were brought under the Scottish Government's direct control in 2013-14. Prior to that, they were local government staff.

[2] Includes the core Scottish Government, the Crown Office and Procurator Fiscal, executive agencies such as Social Security Scotland, and non-ministerial offices such as the Scottish Fiscal Commission.

[3] Includes public corporations, like Scottish Water or CalMac Ferries, and other public bodies.

[36] Institute for Government (2025) Civil service staff numbers

# Chapter 4
# Upcoming fiscal developments

4.1 The next four months of 2025 will see three significant Scottish fiscal publications. In September the Scottish Government will present the Autumn Budget Revision for 2025-26. The 2026-27 Scottish Budget is expected in December and it will be accompanied by the first full Scottish Spending Review (SSR) since 2011.

4.2 These publications come at a time of economic uncertainty. The Scottish and UK economies have faced a volatile economic environment since the start of the year, mainly because of ongoing developments in international trade policy. This uncertainty continues to be reflected in weak consumer and business sentiment.[37]

4.3 Economic conditions are likely to remain challenging in the coming months. The global trade landscape is still evolving and remains unpredictable as tariff negotiations continue. There are also risks from the recent rise in employer National Insurance contributions (NICs) as businesses continue to adjust to increased labour costs. We will provide our updated forecast of the Scottish economy alongside the 2026-27 Scottish Budget.

## 2025-26 Autumn Budget Revision

4.4 The Scottish Government normally amends its budgets twice a year, in the autumn and in the spring. The Autumn Budget Revision (ABR) will be published in late September or early October.

4.5 The ABR is expected to set out how the funding provided by the UK Government for the rise in employer NICs will be allocated between portfolios in 2025-26. The Budget as passed in early 2025 did not account for the funding and spending implications of this tax rise. This was because the UK Government stated it would compensate UK public sector organisations but had only provided an aggregate estimate. Main Estimates in May 2025 confirmed the funding for the Scottish Government, after HM Treasury agreed compensation individually with UK Government departments.

4.6 In our May 2025 report, we noted that the Scottish Block Grant had increased by £339 million because of the rise in employer NICs. These were the Barnett consequentials resulting from increases in UK Government departments' budgets. We also noted that, based on the Scottish Government's latest estimation of its own costs for this tax measure, it expected a funding gap of around £200 million to £400 million depending on how widely the Scottish devolved public sector is defined.[38]

4.7 Beyond the published analysis, there is not yet information about funding for each Scottish portfolio for employer NICs costs. We expect the upcoming ABR to show how funding is being allocated and whether funding for employer NICs comes from

[37] Scottish Government (2025) Scottish economic bulletin: August 2025

[38] Scottish Government (2025) National Insurance Contributions: public sector costs

previously unallocated funding, from savings from within existing spending plans, or from a combination of both.

4.8 As we discussed in Chapter 2, the Scottish Government has agreed pay deals for some devolved workforces in 2025-26 beyond what had been budgeted for. The ABR could reflect how much extra funding is allocated to portfolios for this. Any changes in funding for pay deals which do not conclude before the ABR is presented would likely be left for the Spring Budget Revision.

# 2026-27 Scottish Budget

4.9 The Scottish Government announced in the Medium-Term Financial Strategy (MTFS) that it will present the 2026-27 Scottish Budget in December 2025.[39] The Government already indicated elements of its Scottish Income Tax policy for 2026-27 in the 2025-26 Budget: namely, a freeze in the thresholds for the higher, advanced, and top rates of tax. There are still other developments which will take place before the 2026-27 Budget is presented.

- The UK Budget 2025, in autumn 2025, could lead to changes to the Block Grant in 2026-27. While the Spending Review 2025 confirmed funding for the year 2025-26, any changes to UK Government spending plans could lead to changes in funding for the Scottish Government.
- Office for Budget Responsibility forecasts alongside the UK Budget will inform the tax and social security Block Grant Adjustments (BGAs). In particular, the forecast of the Personal Independence Payment (PIP) BGA will reflect the updated UK Government policy, following the removal of the changes to PIP from the legislation recently passed by the UK Parliament. We discussed this in Chapter 2.
- Our forecasts alongside the 2026-27 Scottish Budget will determine how much the Scottish Government can expect to raise in devolved tax revenues, and how much will be spent on devolved social security. Our forecasts will be based on the Scottish Government's policies including those announced in the 2026-27 Scottish Budget and Spending Review.

4.10 There are two sources of funding where there has been some new information since June: ScotWind and the Scotland Reserve.

## Crown Estate Revenues

4.11 ScotWind is a programme of leasing part of the Scottish seabed for the development of offshore windfarms. Energy companies paid Crown Estate Scotland for an option to develop windfarms on the seabed, and they will make regular lease payments once these are operational. As a devolved body since 2016, net profits from Crown Estate Scotland support the Scottish Budget directly.

4.12 Initially, the Scottish Government planned to use proceeds from ScotWind as a tool to balance the resource side of the Budget and they were used for that purpose in

[39] See Executive Summary and Annex E. Scottish Government (2025) Medium-Term Financial Strategy.

2022-23. No proceeds have been used in 2023-24 or 2024-25 despite initial plans to do so. In 2025-26 the Scottish Government plans to use ScotWind proceeds to support capital budgets. Figure 4.1 outlines the latest plans. Based on these, £349 million remains available to support either the 2026-27 Budget or later budgets.

**Figure 4.1: Use of Crown Estate revenues, 2022-23 to 2026-27**

| £ million | 2022-23 outturn | 2023-24 outturn | 2024-25 outturn | 2025-26 plans |
|---|---|---|---|---|
| Opening balance [1] | 755 | 659 | 659 | 713 |
| Additions [2] | 0 | 0 | 54 | 0 |
| Drawdowns, of which: | 96 | 0 | 0 | 364 |
| Supporting resource budget | 96 | 0 | 0 | 23 |
| Supporting capital budget | 0 | 0 | 0 | 341 |
| Balance remaining | 659 | 659 | 713 | 349 |

Source: Scottish Fiscal Commission, Scottish Government.

[1] In 2022-23, £699.2 million from the first round of ScotWind leasing, with an extra £56 million added as part of the clearing process.

[2] £54 million from the separate Innovation and Targeted Oil and Gas leasing round.

Figures may not sum because of rounding.

4.13 As in previous years, the Scottish Government could decide to reduce the planned use of ScotWind in 2025-26. This would free up more funding to support spending in 2026-27 or beyond. At this point, the Scottish Government has no plans to use ScotWind proceeds in 2026-27 or beyond.

## Scotland Reserve

4.14 There are currently no plans to use the Scotland Reserve to support spending in 2026-27. The Scottish Government plans to use all the underspends from 2024-25 to support spending in 2025-26. However, as 2025-26 develops, these plans could change. If underspends emerge during this financial year, there would be funding in the reserve available to support the 2026-27 Budget.

4.15 As we discussed in Chapter 3, the requirement for the Scottish Government to balance the budget means there will always be some level of underspends that are carried forward through the Reserve. By December 2025 the Scottish Government may be clearer on how spending will compare to the plans set out at the ABR and the likely scale of underspend in 2025-26 which can be used to support spending in 2026-27 or beyond.

# Scottish Spending Review

4.16 The Scottish Government's June 2025 MTFS set out projections for funding and spending over the next five years. Based on current trajectories, the Government expects spending to outpace available funding for both resource and capital. Figure 4.2 shows the resource and capital gaps presented in the MTFS. The gap for both resource and capital is expected to exceed £2 billion by 2029-30, around 4 per cent of planned spending in 2029-30 for resource, and around 23 per cent for capital.

**Figure 4.2: Resource and capital gaps in the MTFS**

| £ million (nominal terms) | 2026-27 | 2027-28 | 2028-29 | 2029-30 |
|---|---|---|---|---|
| **Resource** | | | | |
| Funding | 53,975 | 55,235 | 57,100 | 59,099 |
| Spending | 54,938 | 57,132 | 59,453 | 61,723 |
| Gap | -963 | -1,897 | -2,353 | -2,624 |
| **Capital (excluding FTs)** | | | | |
| Funding | 7,109 | 7,004 | 7,059 | 7,067 |
| Spending | 8,180 | 8,501 | 8,962 | 9,213 |
| Gap | -1,071 | -1,497 | -1,903 | -2,146 |

Source: Scottish Fiscal Commission, Scottish Government.

Figures may not sum because of rounding.

4.17 To achieve a balanced budget, the Scottish Government will need to make changes. In its 2025 Fiscal Sustainability Delivery Plan (FSDP) it set out some actions to close the fiscal gap. This included a workforce reduction target of 0.5 per cent on average each year. The Government estimated this will save £100 million in 2026-27 and £700 million by 2029-30. Other actions were less specific, relating to public sector efficiencies and reform and increasing "public value".

4.18 In June 2025 we highlighted that having set out the scale of the challenge the SSR needs to translate the ambitions identified in the FSDP into concrete action. It provides the Scottish Government with the opportunity to address the request from the Finance and Public Administration Committee, subject committees, public bodies, and others to move beyond single year funding settlements to a medium-term fiscal planning approach across Scotland's devolved public sector.

4.19 The Scottish Government will need to decide the level of detail it publishes in its SSR. The last Spending Review was in 2022; it only covered resource spending, although it was published alongside an update to the previous capital spending review.[40] Budgetary information then was only provided at Level 2, which offers information on major spending programmes within each portfolio. However, this meant that not all public bodies had a multi-year budget outlook. For example, several key public bodies' budgets are presented in Level 3 or 4 budget lines, such as Skills Development Scotland (Level 3), the Scottish Environmental Protection Agency (Level 3), and Health Boards (Level 4).

4.20 The SSR will take place before the next Scottish Parliament election. Implementing the SSR will mainly be the responsibility of the Scottish Government and Scottish Parliament elected in May 2026. It is important that the SSR provides a meaningful

[40] Scottish Government (2022) The Outcome of the Targeted Review of the Capital Spending Review – Updated Spending Allocations for 2023-24 to 2025-26

basis for informed debate by all political parties on how the fiscal challenges the Scottish Government faces can be addressed.

# Adult Disability Payment

4.21 In recent years there has been a substantial increase in demand for disability benefits across the UK, with a larger relative increase in caseload in Scotland for Adult Disability Payment (ADP) than in England and Wales for PIP. We think the UK-wide higher demand is because of a deterioration in health, meaning more people are eligible, and the cost-of-living pressures, meaning more eligible people apply for the payments. As the eligibility criteria for ADP in Scotland and PIP in England and Wales are largely aligned, we think the larger increase in caseload in Scotland is the result of the Scottish Government's approach to delivering the payment. This approach includes support for people through the application process, increased promotion of the payment to increase take-up, and the process for award reviews resulting in a smaller share of people no longer receiving the payment.

4.22 We assume the number of successful applications for ADP will progressively decrease from recent elevated levels as cost-of-living pressures ease. In June 2025, we still forecast the caseload to rise from 529,000 in 2025-26 to 703,000 in 2030-31 because the number of people entering the payment remains higher than those exiting. This rise in caseload, along with annual uprating of payments, leads to our forecast of ADP spending rising from £3.6 billion in 2025-26 to £5.4 billion in 2030-31.

4.23 Within this context for ADP, the Scottish Government has made commitments which could result in policy or delivery changes. If the Scottish Government were to make changes to ADP, we would assess the impact in future forecasts once the changes are confirmed.

4.24 Firstly, the Independent Review of Adult Disability Payment produced its final report on 31 July 2025.[41] It made 58 recommendations, aimed at improving the client experience and ensuring disabled people can access support. The Scottish Government intends to publish its initial response to the review in early 2026 and stated that the recommendations will be assessed against criteria including deliverability and cost.

4.25 Secondly, in its FSDP, the Scottish Government stated it is assessing the extent to which the current ADP award review process is delivering as intended.[42] Recent statistics show a lower-than-forecast proportion of ADP recipients having their awards reduced or ended following an award review. As a result, more individuals are remaining on the caseload, or having their awards maintained, which contributes to higher overall ADP spending.

4.26 These changes relate to Scottish Government spending on ADP, but there are also changes being made to the UK Government's spending on the equivalent benefit, PIP, in England and Wales, as discussed in Chapter 2. These changes have potential implications for the social security BGA funding the Scottish Government receives.

[41] Scottish Government (2025) Independent Review of Adult Disability Payment: final report

[42] Scottish Government (2025) Fiscal Sustainability Delivery Plan

# Chapter 5 Improvements to the Scottish Budget

5.1 This Fiscal Update accompanies our Forecast Evaluation Report.[43] Every other year we publish a Statement of Data Needs: this sets out the additional data, and improvements to data, which we require to help us produce and evaluate our forecasts, and provide analysis and commentary on the Scottish Budget and fiscal sustainability. Our next Statement of Data Needs will be published in 2026. We have, however, identified two issues relating to how information is presented in the Budget. These are discussed in this Chapter with suggested changes that could improve transparency and scrutiny.

## Comparator at Budget time

5.2 When the Scottish Government presented the 2025-26 Scottish Budget in December 2024, it compared its spending plans with 2024-25 plans as amended two months earlier at the Autumn Budget Revision (ABR). This was a welcome improvement. Prior to that, the comparison was made to budgets as originally introduced, rather than as most recently revised.

5.3 Between those two events the new UK Government presented its first budget, providing a large fiscal expansion with immediate in-year increases in resource spending. This resulted in the resource Block Grant rising by £1.4 billion in-year. Earlier in Chapter 3, Figure 3.1 showed how, excluding COVID-19 funding, the in-year increase in the Block Grant was considerably larger than in any of the previous four years. Since the expansion was permanent, the Block Grant remained larger for 2025-26 too.

5.4 Given the scale of funding changes since the ABR, comparing spending plans for the 2025-26 Budget to the 2024-25 position at ABR did not reflect how spending would change between the two years.

5.5 Figure 5.1 shows the year-on-year changes in resource portfolio spending plans, using both the ABR and the Spring Budget Revision (SBR) as comparators for 2024-25. The latest position for 2024-25 was presented in the SBR, which allocated the large in-year uplifts from the UK Budget. This comparison shows that resource spending in 2025-26 was 1.4 per cent larger in real terms when compared with the latest position for 2024-25. The largest portfolio (Health and Social Care) remained broadly flat. The second largest portfolio, Finance and Local Government, saw a fall of 1.2 per cent. Of the largest portfolios, only Social Justice, covering devolved social security payments, was expected to grow even after the extra funding allocated in the SBR.

5.6 This is in marked contrast to the position we reported in December 2024, where the overall resource budget was presented as increasing in 2025-26 by 3.7 per cent relative to the ABR. Within that, all but one small portfolio were shown as growing in real terms,

43 Scottish Fiscal Commission (2025) Forecast Evaluation Report – August 2025

with the Health and Social Care portfolio growing by 3.4 per cent as opposed to 0.3 per cent growth when measured against the most recent comparator.

5.7 If the Scottish Government were to agree with the Finance and Public Administration Committee a threshold for in-year funding changes following the ABR, it could improve scrutiny of the Budget. If the threshold is exceeded, it should trigger a requirement for the Scottish Government to indicate, as part of the Budget documents for the year ahead, the new level of funding and how that funding would be spent, with decisions to be confirmed in the SBR. This would effectively mean the Scottish Government should provide an early indication of how it plans to allocate the funding in the SBR, which could then be the basis for comparisons between years. This would mean year-on-year comparisons in spending would be more informative.

**Figure 5.1: Effect of different comparators for changes to resource portfolio allocations**

| Portfolio | Share of budget [1] | Real-terms change from 2024-25 (ABR) | Real-terms change from 2024-25 (SBR) | Percentage point difference |
|---|---|---|---|---|
| Health and Social Care | 39.3 | 3.4 | 0.3 | -3.1 |
| Finance and Local Government | 25.6 | 2.6 | -1.2 | -3.8 |
| Social Justice | 14.6 | 7.9 | 8.1 | 0.2 |
| Justice and Home Affairs | 6.8 | 2.2 | 0.3 | -1.9 |
| Education and Skills | 6.2 | 3.0 | 1.7 | -1.3 |
| Transport | 3.0 | 1.7 | 1.8 | -0.1 |
| Rural Affairs, Land Reform and Islands | 1.8 | -3.1 | -2.7 | +0.3 |
| Deputy First Minister, Economy and Gaelic | 1.2 | 3.7 | 20.7 | +17 |
| Constitution, External Affairs and Culture | 0.6 | 9.3 | 9.9 | +0.6 |
| Crown Office and Procurator Fiscal Service | 0.4 | 7.3 | 7.7 | +0.4 |
| Net Zero and Energy | 0.2 | 11.1 | 61.9 | +50.8 |
| Scottish Parliament and Audit Scotland | 0.3 | 6.4 | 6.2 | -0.2 |
| Total resource spending | 100.0 | 3.7 | 1.4 | -2.3 |

Source: Scottish Fiscal Commission, Scottish Government.

Figures exclude in-year budget-neutral transfers, except those which were included from the outset in 2025-26. See Box 2.1 of the December 2024 SEFF for more details.

Real-terms rates using the forecast growth in the GDP deflators from the Office for Budget Responsibility's October 2024 Economic and fiscal outlook for comparability with Figure 2.9 from our December 2024 SEFF.

[1] Based on the resource part of the 2025-26 Budget as approved by the Parliament after changes through the Budget Bill stages.

Figures may not sum because of rounding.

# Internal transfers

5.8 The Scottish Government makes large transfers between portfolios in Budget Revisions. Some of these are budget-neutral (add up to zero) and reflect that, while one portfolio has policy responsibility for an area, in practice another one incurs the spending.

5.9 For example, delivering the Real Living Wage for social care workers and training for nurses to enter the profession were policies of the Health and Social Care portfolio. However, social care is delivered by local government, and universities and colleges are the responsibility of the Education and Skills portfolio. Therefore, the Finance and Local Government and the Education and Skills portfolios need funding to deliver these policies, and those transfers happen during the year at Budget Revisions.

5.10 For the 2025-26 Budget, the Scottish Government decided to baseline some of these transfers which means these transfers will be in the portfolio that will incur the spending from the outset. For example, the delivery of a real living wage for social care workers has now been included in the Finance and Local Government portfolio in the 2025-26 Budget. This approach reduces the need for internal transfers during the year and simplifies tracking changes in budgets over time.

5.11 However, some transfers will still take place in Budget Revisions. For example, any funding committed to adult social care will still be transferred during the year from the Health and Social Care portfolio to Finance and Local Government as local authorities remain responsible for delivery of social care services.

5.12 After a request from the Convener of the Finance and Public Administration Committee during one of the 2025-26 Budget debates, the Cabinet Secretary for Finance and Local Government committed to consider if more can be done to simplify the presentation of future budgets beyond the changes already implemented.[44]

5.13 As Figure 5.2 suggests, internal transfers that have not been baselined are still substantial in size, leading to large changes in spending plans during the year. This means the portfolio allocations presented in the Budget do not represent the intended spending plans for the year ahead.

5.14 The 2025-26 Scottish Budget included an Annex which compared the ABR position without the internal transfers with the 2025-26 position.[45] While this was a welcome improvement in transparency, the scale of internal transfers the Scottish Government expected to occur during the 2025-26 financial year remained unclear. More complete information would have been to present the ABR 2024-25 position against the 2025-26 Budget, showing the expected and routine internal transfers for 2025-26. An additional limitation of the approach the Scottish Government has taken is that it only provides a portfolio comparison of the internal transfers and does not allow a comparison to be made on a COFOG basis.

5.15 There are therefore further improvements which the Scottish Government could make to improve the comparisons made between spending years set out in Budget documents.

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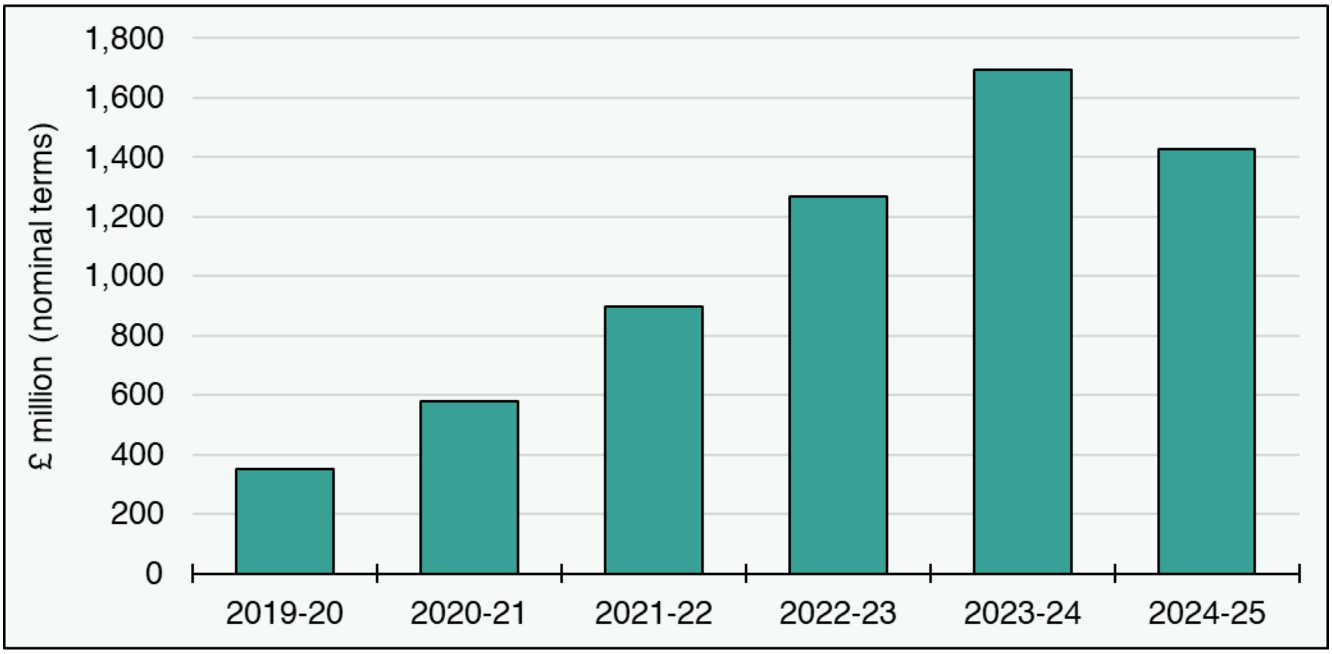
[44] Scottish Parliament (2025) Official Report – Meeting of the Parliament on 30 January 2025

[45] See Table A.07. Scottish Government (2024) Scottish Budget 2025-26.

These improvements could include the publication of further information on internal transfers, or the Budget could be presented with all spending shown at the outset under the portfolio where it will ultimately incur the spending.

**Figure 5.2: Absolute value of budget-neutral internal transfers**

**The volume of internal transfers has tended to rise as budgets grow**




Description of Figure 5.2: Column chart showing the absolute value of internal transfers happening during the financial year, from 2019-20 to 2024-25. They increased from £351 billion in 2019-20 to £1.4 billion in 2024-25, with a peak of £1.7 billion in 2023-24.

Source: Scottish Fiscal Commission, Scottish Government.

Sum of internal transfers between portfolios and between programmes within a portfolio, less the internal transfers that were baselined in 2025-26.

# Annex A
# Restatement of funding positions

A.1 Funding for the Scottish Budget changes during the year. The only sources fixed at the time of setting the budget are the forecast Scottish Income Tax revenues, the Income Tax Block Grant Adjustment (BGA), and the amount of Non-Domestic Rates (NDR) that the Scottish Government decides to distribute among local authorities. Everything else is subject to change, with shifts to funding levels being implemented at Budget Revisions.

A.2 We have tracked funding levels for the Scottish Budget since April 2020, when the outbreak of the COVID-19 pandemic heavily disrupted the normal cycle of UK fiscal events, leading to in-year changes of an unprecedented scale. We have done so either in standalone Fiscal Updates, or in chapters or annexes of our Scotland's Economic and Fiscal Forecasts (SEFFs).[46]

A.3 However, we have not systematically reported the outturn funding positions for all years. We also have changed some aspects of how we report the funding position, meaning that what we showed in the past is not directly comparable to more recent reports.

A.4 In this annex we explain what has changed in how we report funding levels, and we restate the outturn funding position for all years since 2020-21.

## IFRS16

A.5 The International Financial Reporting Standard 16 (IFRS16) is an accounting standard concerning leases. Prior to IFRS16, operational and financial leases had different accounting treatments. The new standard removed that distinction, so now all leases must create an asset and a corresponding liability in the balance sheet. The asset must be depreciated over time, and the liability reduced as lease payments are made.

A.6 IFRS16 was adopted progressively in the public sector over three years. From 2022-23 to 2024-25, bringing leases into the balance sheet required greater capital budgets to acquire the assets and greater non-cash budgets to depreciate them. However, resource budgets are to be lower as now only the interest charges are counted as resource spending – the principal is a reduction of a liability, not an expense.

A.7 HM Treasury broadly met the Scottish Government's funding requirements to implement IFRS16 as part of the Block Grant. This is why, during the implementation of IFRS16, we omitted related transfers from the funding position because they did not have a material impact on the Scottish Government's spending power.

A.8 However, since 2025-26 there is no specific IFRS16 funding as the standard is fully adopted. Therefore, to meaningfully compare 2025-26 or future Budgets to earlier years, we must include it in the restated funding positions for 2022-23, 2023-24 and 2024-25.

[46] See the Fiscal Updates of April 2020, September 2020, January 2021 and March 2021, and among SEFFs, Chapter 2 in August 2021, December 2021 and May 2022, and Annex D in December 2022, May 2023, December 2023 and December 2024

## Underspends

A.9 The Scottish Government must run a broadly balanced budget. It is not allowed to overspend, and its ability to underspend without losing funding is limited to the capacity of the Scotland Reserve to carry it forward. Because of this, the budget management process tends to produce underspends, which are then added to the reserve for drawdown in later years.

A.10 We have so far showed drawdowns from the Scotland Reserve. However, previously we did not make deductions from funding for underspends each year to avoid double counting across years. We now restate the funding positions from 2020-21 to 2024-25 netting off outturn underspends from Scotland Reserve drawdowns.[47]

## Repayment of financial transactions

A.11 Financial transactions (FTs) are a ring-fenced subset of capital funding. It can only be used to invest in financial assets. Financial assets are those which are liabilities in someone else's balance sheet: for example, loans to the private sector via the Scottish National Investment Bank, or acquiring equity in dwellings through help-to-buy schemes.

A.12 The Scottish Government has funding within the Block Grant for two kinds of FTs:

- Gross FTs. These must be repaid to HM Treasury (HMT) as creditors repay their liabilities, with the Scottish Government retaining the interest income.
- Net FTs. These do not have to be repaid to HMT. Proceeds from repayments and interest income can be recycled into new FT spending.

A.13 While borrowing and Scotland Reserve drawdown decisions are made towards the end of the financial year, how much is repaid in FTs is agreed with HMT after the financial year has finished, based on the emerging provisional outturn spending position. It is therefore the last funding decision in the lifecycle of a Scottish Budget.

A.14 Since we had stopped reporting the funding position by the time year-end decisions were made, we did not reflect these repayments. This creates an inconsistency when we undertake spending analysis with outturn data, as this will be after repayments are made. Therefore, we have restated the outturn funding positions for 2020-21 to 2024-25 with a reduction in FTs discretionary funding to account for repayments to HMT.

## Cost of borrowing

A.15 Under the fiscal framework, the Scottish Government has powers to borrow for resource and capital spending. Borrowing increases funding in the year when the loan is taken out, but results in less funding in later years as debt is repaid with interest.

A.16 Prior to 2022-23, the cost of servicing debt was a spending allocation within the Finance portfolio. However, it was always removed from the Budget Bill as the Parliament did not vote on whether to approve it.

[47] Underspends for 2024-25 are still based on provisional outturn. Final underspends will be determined in early 2026.

A.17 From 2022-23, we and the Scottish Government show borrowing repayments as a deduction from discretionary resource funding. This way, portfolio allocations are made from the funding left after servicing debt. To give a consistent time series, we restate the funding positions for 2020-21 and 2021-22 with the cost of debt shown as a funding deduction.

**Figure A.1: Detailed outturn resource funding position, 2020-21 to 2024-25**

| Funding source (£ million) | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 [1] |
|---|---|---|---|---|---|
| **Block Grant** | | | | | |
| SR settlement [2] | 29,464 | 30,923 | 34,322 | 34,942 | 35,576 |
| COVID-19 funding | 8,600 | 5,631 | 0 | 0 | 0 |
| Non-COVID-19 Barnett consequentials | 238 | -3 | 216 | 1,816 | 3,558 |
| IFRS16 funding | | | -211 | -217 | -222 |
| Non-Barnett funding [3] | 618 | 716 | 704 | 715 | 715 |
| **Post-2016 fiscal framework** | | | | | |
| Devolved revenues [4] | 13,004 | 13,217 | 14,654 | 16,696 | 19,802 |
| Tax and non-tax BGAs [5] | -12,825 | -12,529 | -14,713 | -16,129 | -18,110 |
| Social security BGAs [5] | 3,185 | 3,313 | 3,703 | 4,405 | 5,182 |
| Adjustment for forecast error, of which: | 30 | 0 | 32 | 150 | -338 |
| Reconciliations | -177 | -319 | -15 | 46 | -338 |
| Borrowing | 207 | 319 | 47 | 104 | 0 |
| Net Scotland Reserve drawdown, of which: | -187 | -200 | 355 | -15 | -237 |
| In-year drawdowns | 171 | 405 | 605 | 250 | 265 |
| Underspends added after year-end | -358 | -605 | -250 | -265 | -501 |
| **Other sources** | | | | | |
| Other funding [6] | 297 | 281 | 1,210 | 391 | 300 |
| Non-Domestic Rates (NDR) distributable amount | 1,868 | 2,090 | 2,766 | 3,047 | 3,068 |
| Less: resource borrowing costs | 0 | -21 | -77 | -114 | -132 |
| Less: capital borrowing costs | -66 | -75 | -83 | -103 | -135 |
| Resource funding for discretionary spend | 44,227 | 43,343 | 42,878 | 45,582 | 49,027 |

Source: Scottish Fiscal Commission, Scottish Government.

[1] Provisional outturn. Final outturn will be confirmed with the Scottish Budget Final Outturn Report in spring 2026.

[2] For 2020-21, Spending Round 2019. For 2021-22, Spending Review 2020. For 2022-23 to 2024-25, Spending Review 2021.

[3] Funding agreed between the UK and Scottish governments at Spending Reviews that is not based on the use of the Barnett formula.

[4] Budget-setting forecasts for Income Tax, but outturn amounts for fully devolved taxes (LBTT, SLfT) and non-tax revenues from Fines, Forfeitures, and Fixed Penalties (FFFPs).

[5] Budget-setting forecasts for Income Tax, but adjusted in-year for fully devolved taxes (LBTT, SLfT), FFFPs (until 2023-24) and devolved benefits, based on Office for Budget Responsibility (OBR) autumn forecasts.

[6] Figure A.2 shows a breakdown of 'Other funding'.

Figures may not sum because of rounding.

**Figure A.2: Detailed 'Other' resource funding, 2020-21 to 2024-25**

| Funding source (£ million) | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 [1] |
|---|---|---|---|---|---|
| **Transfers from the UK Government** | | | | | |
| BCTs and MOGs [2] | 11 | 76 | 59 | 132 | 60 |
| Budget switch [3] | | | | 27 | |
| City Deals | | 1 | 1 | 1 | 1 |
| Deferral of Barnett funding [4] | | | 296 | | |
| Net extra Crown Estate BGA | | | | | -3 |
| Fiscal framework admin costs | 66 | | | | |
| HMT compensation, of which: | | | 413 | 20 | 22 |
| Home Office UKSR21 comparability factor error | | | 17 | 20 | 22 |
| Income Tax spillover dispute | | | 375 | | |
| Income Tax outturn data error | | | 21 | | |
| Migrant Surcharge | 30 | 117 | 160 | 161 | 221 |
| Other [5] | 185 | 8 | 27 | 13 | |
| Voluntary NDR payments [6] | | 73 | 2 | | |
| **Directly deposited in the Scottish Consolidated Fund** | | | | | |
| King's and Lord Treasurer's Remembrancer (KLTR) | 5 | 5 | 13 | | |
| Other | | | 10 | | |
| Crown Estate income | | | | 37 | |
| ScotWind, of which: | | | 103 | | |
| Use of proceeds | | | 96 | | |
| Use of interest income | | | 7 | | |
| Voluntary NDR payments | | | 126 | | |
| Total resource other funding | 297 | 281 | 1,210 | 391 | 300 |

Source: Scottish Fiscal Commission, Scottish Government.

[1] Provisional outturn. Final outturn will be confirmed with the Scottish Budget Final Outturn Report in spring 2026.

[2] BCTs stands for Budget Cover Transfers and MOGs for Machinery of Government transfers. For more details about these concepts, see Annex A in Scottish Fiscal Commission (2024) Spending trends in the 2024-25 Scottish Budget.

[3] Switches from capital to resource are normally not allowed but this one was authorised by HM Treasury.

[4] Deferrals are normally done through the Scotland Reserve unless there is explicit agreement from HM Treasury.

[5] Other funding includes multiple small non-Barnett funding sources coming from the UK Government, like HM Treasury transfers for Debt Advice, all added together.

[6] Some retailers with UK-wide presence made a lump-sum payment to the UK Government even though the different parts of the country have different regimes when it comes to local business taxes. The amount was agreed between the UK and Scottish Governments.

Figures may not sum because of rounding.

**Figure A.3: Detailed outturn capital funding position, 2020-21 to 2024-25**

| Funding source (£ million) | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 [1] |
|---|---|---|---|---|---|
| **Capital (excluding FTs)** | | | | | |
| Block Grant, of which: | 4,666 | 5,209 | 5,988 | 5,969 | 5,696 |
| SR settlement [2] | 3,356 | 4,961 | 4,469 | 4,757 | 4,690 |
| COVID-19 funding | 0 | 291 | 0 | 0 | 0 |
| Non-COVID Barnett funding | 997 | -55 | -60 | 113 | 69 |
| IFRS16 funding [3] | 0 | 0 | 861 | 467 | 267 |
| Non-Barnett funding [4] | 313 | 12 | 718 | 632 | 670 |
| Capital borrowing | 200 | 150 | 300 | 300 | 139 |
| Net Scotland Reserve drawdown, of which: | 73 | -74 | 49 | -108 | 109 |
| In-year drawdowns | 80 | 7 | 81 | 32 | 140 |
| Underspends added after year-end | -7 | -81 | -32 | -140 | -31 |
| Other funding [5] | 173 | 117 | 76 | 78 | 101 |
| Total general capital funding | 5,112 | 5,402 | 6,413 | 6,238 | 6,046 |
| **Financial transactions (FTs)** | | | | | |
| Block Grant, of which: | 525 | 236 | 349 | 162 | 123 |
| SR settlement [2] | 148 | 208 | 466 | 186 | 176 |
| COVID funding | 0 | 42 | 0 | 0 | 0 |
| Non-COVID Barnett funding | 377 | -14 | -117 | -23 | -53 |
| Net Scotland Reserve drawdown, of which: | -61 | 183 | -31 | 40 | -21 |
| In-year drawdowns | 0 | 197 | 14 | 45 | 4 |
| Underspends added after year-end | -61 | -14 | -45 | -4 | -25 |
| Other funding [5] | 87 | 0 | 0 | 188 | 0 |
| Less: repayments to HMT | -150 | -243 | 0 | -16 | 0 |
| Total FTs funding | 401 | 176 | 318 | 374 | 102 |
| Total capital funding | 5,512 | 5,578 | 6,730 | 6,612 | 6,148 |

Source: Scottish Fiscal Commission, Scottish Government.

[1] Provisional outturn. Final outturn will be confirmed with the Scottish Budget Final Outturn Report in spring 2026.

[2] For 2020-21, Spending Review 2015. For 2021-22, Spending Review 2020. For 2022-23 to 2024-25, Spending Review 2021.

[3] For more details about IFRS16, see Annex A in Scottish Fiscal Commission (2024) Spending trends in the 2024-25 Scottish Budget.

[4] Funding agreed between the UK and Scottish Governments at Spending Review times not based on the use of the Barnett formula.

[5] Figure A.4 shows a breakdown of 'Other funding'.

Figures may not sum because of rounding.

**Figure A.4: Detailed 'Other' capital funding, 2020-21 to 2024-25**

| Funding source (£ million) | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 [1] |
|---|---|---|---|---|---|
| **Capital (excluding FTs)** | | | | | |
| BCTs and MOGs [2] | 81 | 5 | 13 | 0 | 6 |
| Budget switch [3] | | | | -27 | |
| City Deals | 90 | 113 | 126 | 82 | 81 |
| Deferrals of Barnett funding [4] | 2 | | | | 15 |
| HMT compensation for Home Office UKSR21 comparability factor error | | | 2 | 2 | |
| Other [5] | | | | 22 | |
| Military contribution to Ukraine | | | -65 | | |
| Total capital other funding | 173 | 117 | 76 | 78 | 101 |
| **Financial transactions (FTs)** | | | | | |
| Deferrals of Barnett funding [4] | 87 | | | | |
| HMT compensation for historical allocation error | | | | 188 | |
| Total FTs other funding | 87 | 0 | 0 | 188 | 0 |

Source: Scottish Fiscal Commission, Scottish Government.

[1] Provisional outturn. Final outturn will be confirmed with the Scottish Budget Final Outturn Report in spring 2026.

[2] BCTs stands for Budget Cover Transfers and MOGs for Machinery of Government transfers. For more details about these concepts, see Annex A in Scottish Fiscal Commission (2024) Spending trends in the 2024-25 Scottish Budget.

[3] Switches from capital to resource are normally not allowed but this one was authorised by HM Treasury.

[4] Deferrals are normally done through the Scotland Reserve unless there is explicit agreement from HM Treasury.

[5] In 2023-24 it includes £16 million for the Reaching 100% programme and £6 million for the Regional Investment Fund.

Figures may not sum because of rounding.

# Annex B
# Policy costing

## Pension Age Winter Heating Payment

B.1 This annex presents our costing for the Scottish Government's policy for Pension Age Winter Heating Payment (PAWHP) announced on 18 June 2025. This includes the payment to all people over State Pension age and the subsequent recovery of payments from those with an annual income of £35,000 or more.

**Figure B.1: PAWHP costing**

| £ million, nominal terms | 2025-26 | 2026-27 | 2027-28 | 2028-29 | 2029-30 | 2030-31 |
|---|---|---|---|---|---|---|
| Spending | 187 | 196 | 199 | 206 | 215 | 225 |
| Payment recovery | 30 | 33 | 36 | 39 | 43 | 47 |

Source: Scottish Fiscal Commission

### Background

B.2 In Scotland, PAWHP replaced the UK Government's Winter Fuel Payment (WFP) in winter 2024-25. The payment provides financial support to eligible people over State Pension age to help towards meeting heating costs in winter.

B.3 In our May 2025 forecast, we published a costing for PAWHP based on the eligibility of most people over State Pension age. Payment amounts differed depending on age, living arrangements, and whether clients were in receipt of qualifying benefits, primarily Pension Credit. We expected that the policy would apply to subsequent years and forecast spending to be £98 million in 2025-26, rising to £113 million in 2030-31.

B.4 On 9 June 2025, the UK Government announced a new policy for WFP in England and Wales. From 2025-26, all people of pension age will receive the payment unless they opt out. Payments will be recovered through the tax system from individuals with an annual income of £35,000 or more. The payment rates are set at £200 and £300 per household in 2025-26, based on the age and living arrangements of the clients. This will lead to higher spending in England and Wales. As a result, the associated Block Grant Adjustment (BGA) funding the Scottish Government is expected to receive will also increase.

B.5 On 18 June 2025, the Scottish Government announced changes to PAWHP in Scotland to align with WFP eligibility. In contrast to WFP, the payment rates are set at £203.40 and £305.10 per household in 2025-26. As policy details were shared too late for us to produce a full costing in June 2025, we produced an illustrative estimate, in which the PAWHP spending was presented as the spending net of payments recovered.

B.6 The Scottish Government laid the Winter Heating Assistance (Pension Age) (Scotland) Amendment Regulations 2025 in the Scottish Parliament on 25 August 2025.[48]

B.7 We have now produced a full policy costing in which we have refined our assumption on the proportion of the pension-age population whose income is above £35,000. Previously, we assumed this proportion to be constant. Payment recovery from those with annual incomes above the threshold is forecast to be £30 million in 2025-26, rising to £47 million in 2030-31.

B.8 We now forecast spending on PAWHP prior to payment recovery to be £187 million in 2025-26, rising to £225 million in 2030-31.

## Measure description

B.9 From winter 2025-26, PAWHP will be delivered through Social Security Scotland. It will be an automatic payment with standard payment rates of £203.40 and £305.10 per household in 2025-26, with the payment rates uprated with inflation in subsequent years. The eligibility and payment rates will be based on:

- the clients' living arrangements: specifically, whether they live alone, with a qualifying person, or in residential care
- the ages of the client and any other qualifying people in the same household: specifically, the date of reaching State Pension age
- the receipt of certain benefits, primarily Pension Credit, by the client or any other qualifying people in the same household

B.10 Payments will later be recovered by HM Revenue and Customs (HMRC) from individuals who have a taxable annual income above the £35,000 threshold. We assume that the threshold will be fixed over the forecast period.

B.11 Individuals can opt out of receiving PAWHP this winter. If an individual decides to opt out, they will receive an award letter acknowledging that they have opted out and have not received a payment. Once opted out, individuals can opt in at a later date.

## Costing

B.12 Our forecast for the number of payments made from 2025-26, prior to payment recovery, is based on our forecast of the population aged above State Pension age and data on WFP in Scotland up to 2023-24, as the eligibility criteria for these two policies are broadly comparable.

B.13 We forecast the number of payments made at each payment rate based on historical trends in the WFP-eligible population. To produce our spending forecasts for PAWHP, we multiply the payment amounts by our forecast for the number of payments made prior to payment recovery. We assume that the number of individuals opting out of receiving PAWHP will be small with a negligible effect on our spending forecast, so have not accounted for this in our forecast.

[48] UK Legislation (2025) The Winter Heating Assistance (Pension Age) (Scotland) Amendment Regulations 2025

B.14 In our costing we assume that the payment amounts of £203.40 and £305.10 will be uprated with inflation from 2025-26 onwards. Figure B.2 shows the payment amounts forecast.

**Figure B.2: Payment rates from winter 2025-26**

| Payment amount, £ | 2025-26 | 2026-27 | 2027-28 | 2028-29 | 2029-30 | 2030-31 |
|---|---|---|---|---|---|---|
| Uprated £200 payment | 203.40 | 210.95 | 214.75 | 219.05 | 223.45 | 227.90 |
| Uprated £300 payment | 305.10 | 316.40 | 322.10 | 328.55 | 335.10 | 341.80 |

Source: Scottish Fiscal Commission

B.15 Our forecast for the number of individuals with annual incomes greater than the income threshold is based on the 2021-22 Survey of Personal Incomes (SPI). To produce the forecast, we apply our population and economy projections to the SPI data and adjust for State Pension age changes.

B.16 This approach incorporates fiscal drag as the assumed fixed income threshold implies more individuals crossing the threshold, and therefore not keeping their payments, over the forecast period. We estimate that around 16 per cent of the eligible pension-age population, given by the proportion of individuals with annual incomes more than £35,000, will have their payments recovered in 2025-26, rising to 21 per cent in 2030-31.

B.17 To produce the forecast for payments recovered, we apply the above proportions to the spending forecast prior to payment recovery.

B.18 Figure B.3 shows our forecast for the number of payments made prior to payment recovery and recovered from 2025-26. We forecast the number of payments recovered to be 169,000 in 2025-26, increasing to 234,000 by 2030-31, reflecting the effect of fiscal drag.

**Figure B.3: Forecast number of payments made and recovered from winter 2025-26**

| Number of payments (thousands) | 2025-26 | 2026-27 | 2027-28 | 2028-29 | 2029-30 | 2030-31 |
|---|---|---|---|---|---|---|
| Payments made | 1,055 | 1,061 | 1,049 | 1,060 | 1,086 | 1,113 |
| Payments recovered | 169 | 180 | 189 | 201 | 217 | 234 |

Source: Scottish Fiscal Commission

B.19 Figure B.4 compares our forecast for PAWHP spending following the policy change with our forecast from May 2025. Spending is forecast to be £89 million higher in 2025-26, rising to £112 million higher by 2030-31. While the number of people receiving payments is similar, the new policy increases payment amounts received by those who were not in receipt of qualifying benefits under the previous policy in May 2025.

**Figure B.4: Change in PAWHP forecast since May 2025**

| £ million, nominal terms | 2025-26 | 2026-27 | 2027-28 | 2028-29 | 2029-30 | 2030-31 |
|---|---|---|---|---|---|---|
| May 2025 | 98 | 103 | 103 | 105 | 109 | 113 |
| August 2025 | 187 | 196 | 199 | 206 | 215 | 225 |
| Changes since May 2025 | 89 | 93 | 96 | 101 | 107 | 112 |

Source: Scottish Fiscal Commission

Figures may not sum because of rounding.

## Implications for the Scottish Budget

B.20 The Scottish Government receives BGA funding determined by forecast and outturn spending on the equivalent WFP in England and Wales. At this point, the interaction between the BGA for this payment and recovery by HMRC is unclear. We will provide an update on this in our next forecast.

B.21 Payment amounts will be uprated with inflation each year in Scotland, but we assume that payment amounts in England and Wales will remain at their nominal 2025-26 levels. This will lead to spending rising more quickly in Scotland.

## Uncertainty in the costing

B.22 Our forecast of the number of payments recovered assumes a fixed taxable income threshold. If the £35,000 annual income threshold does not remain fixed and is uprated, then more individuals will be below the threshold and keep their payment. In this case, our forecast under the assumption of a fixed threshold would overestimate the number of payments recovered.

B.23 Payment amounts are uprated with inflation in line with how other benefits are uprated. Inflation forecasts move over time, adding uncertainty to the costing of all inflation-linked benefits.

B.24 We assume that the number of eligible people opting out of receiving PAWHP is small and has a negligible effect on our spending forecast. If there were to be a substantial opt-out cohort with annual incomes above £35,000 then our forecast may overestimate spending prior to payment recovery. However, we would expect there to be a similar reduction from opt-outs to our payment recovery forecast, leading to our forecast for spending with payment recovery deducted being unaffected.

B.25 Any substantial changes to these elements will affect our forecast of the caseload and spending for PAWHP.

# Additional information

## Abbreviations

| | |
|---|---|
| ABR | Autumn Budget Revision |
| ADP | Adult Disability Payment |
| AME | Annually managed expenditure |
| BCTs | Budget Cover Transfers |
| BGA | Block Grant Adjustment |
| CA | Carer’s Allowance |
| COFOG | Classification of the Functions of Government |
| COVID-19 | Coronavirus disease 2019 |
| CPI | Consumer Prices Index |
| DELs | Departmental expenditure limits |
| EU | European Union |
| FFFPs | Fines, Forfeitures, and Fixed Penalties |
| FSDP | Fiscal Sustainability Delivery Plan |
| FTs | Financial Transactions |
| GDP | Gross Domestic Product |
| HMRC | His Majesty’s Revenue and Customs |
| HMT | His Majesty’s Treasury |
| IFRS16 | International Financial Reporting Standards 16 |
| LBTT | Land and Buildings Transaction Tax |
| MoD | Ministry of Defence |
| MOGs | Machinery of Government Transfers |
| MTFS | Medium-Term Financial Strategy |
| NATO | North Atlantic Treaty Organisation |
| NDR | Non-Domestic Rates |
| NHS | National Health Service |

| | |
|---|---|
| NICs | National Insurance Contributions |
| OBR | Office for Budget Responsibility |
| OECD | Organisation for Economic Co-operation and Development |
| PAWHP | Pension Age Winter Heating Payment |
| PIP | Personal Independence Payment |
| PSPP | Public sector pay policy |
| RTI | Real Time Information |
| SBR | Spring Budget Revision |
| SEFF | Scotland's Economic and Fiscal Forecasts |
| SFC | Scottish Fiscal Commission |
| SIT | Scottish Income Tax |
| SLfT | Scottish Landfill Tax |
| SNIB | Scottish National Investment Bank |
| SPI | Survey of Personal Incomes |
| SSR | Scottish Spending Review |
| UC | Universal Credit |
| UK | United Kingdom |
| UKSR | United Kingdom Spending Review |
| UN | United Nations |
| WFP | Winter Fuel Payment |

A full glossary of terms is available on our website: Glossary I Scottish Fiscal Commission.

# Professional standards

The SFC is committed to fulfilling our role as an Independent Fiscal Institution, in line with the principles set out by the Organisation for Economic Co-operation and Development (OECD).[49]

The SFC also seeks to adhere to the highest possible standards for analysis. While we do not produce official statistics, we voluntarily comply as far as possible with the UK Statistics

[49] OECD (2014) Recommendation of the Council on Principles for Independent Fiscal Institutions.

Authority's Code of Practice for Statistics. Further details and our statement of voluntary compliance can be found on our website.[50]

# Correspondence and enquiries

We welcome comments from users about the content and format of our publications. If you have any feedback or general enquiries about this publication or the SFC, please contact info@FiscalCommission.scot. Press enquiries should be sent to press@FiscalCommission.scot.

All charts and tables 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 paper please contact the responsible analyst:

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[50] Scottish Fiscal Commission (2022) Statement of Voluntary Compliance with the Code of Practice for Statistics and Error Policy.

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