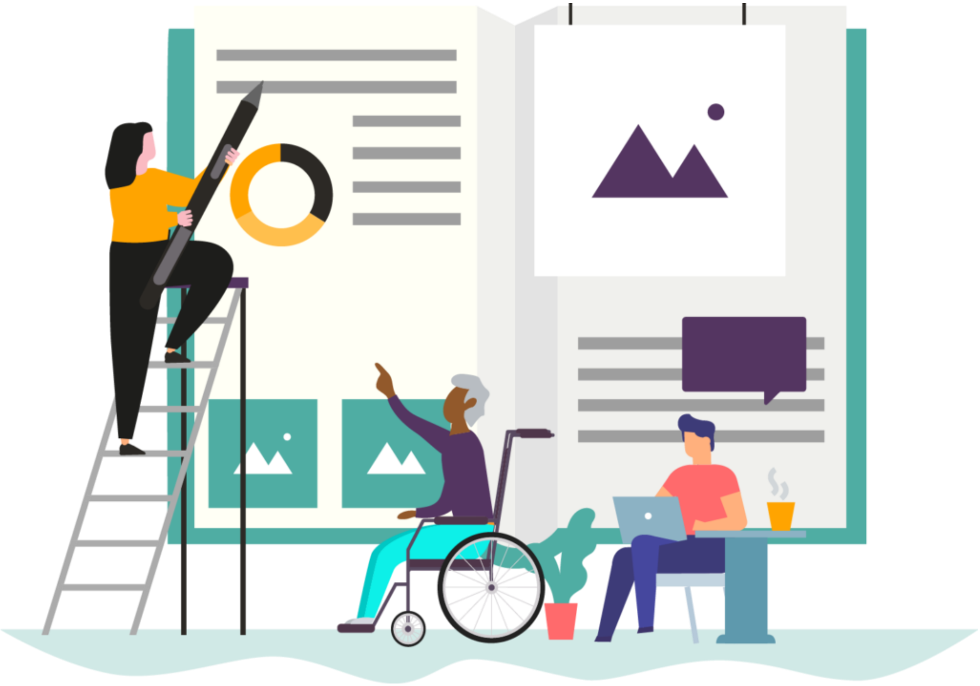
Scottish Fiscal Commission

Devolution and the interaction of UK and Scottish Budgets



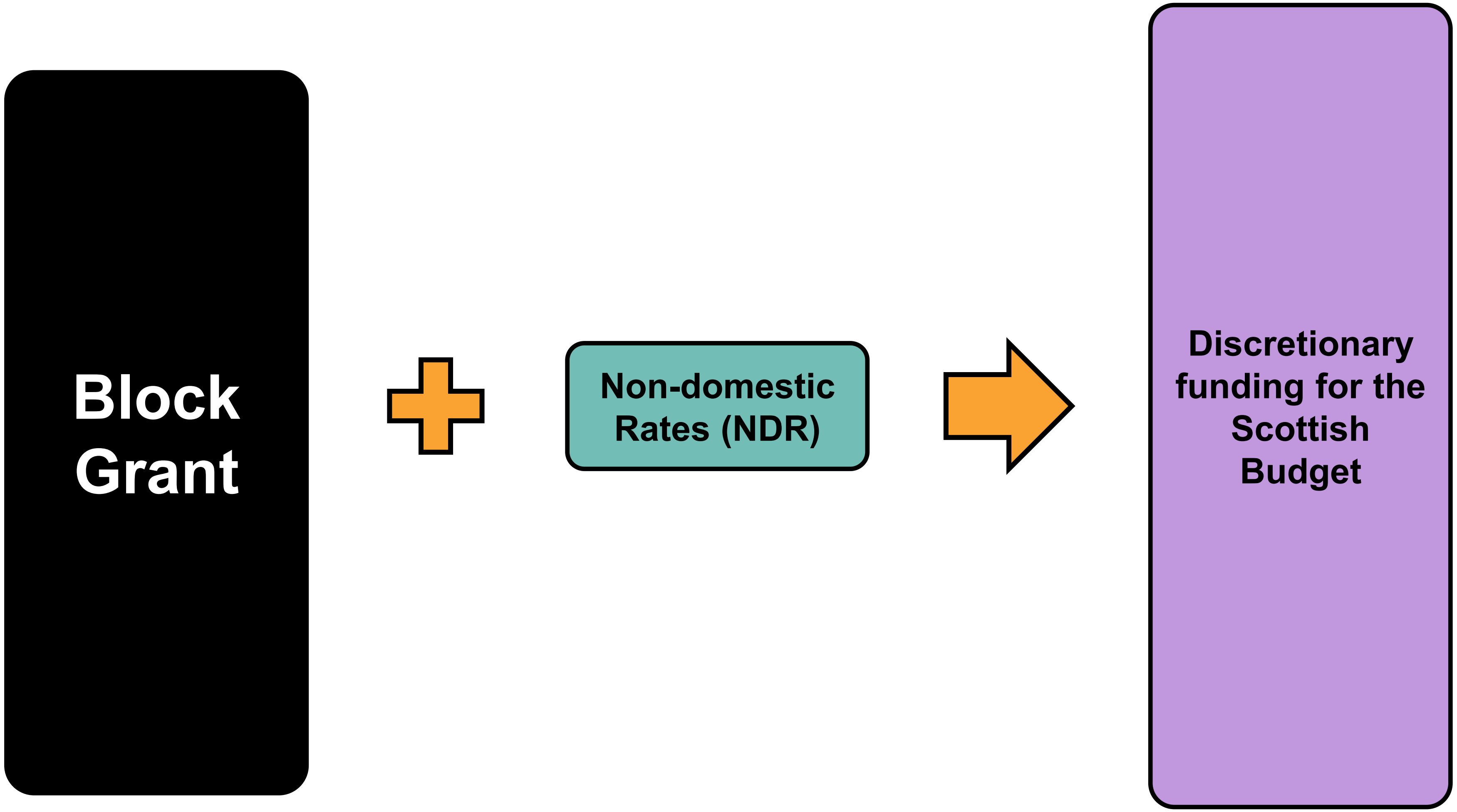
Will cover

- The evolution of the Scottish budget and powers
- A broad overview of how the Budget is constructed
- What does this all mean? Messages from our work
- Q and A or happy to speak throughout the day

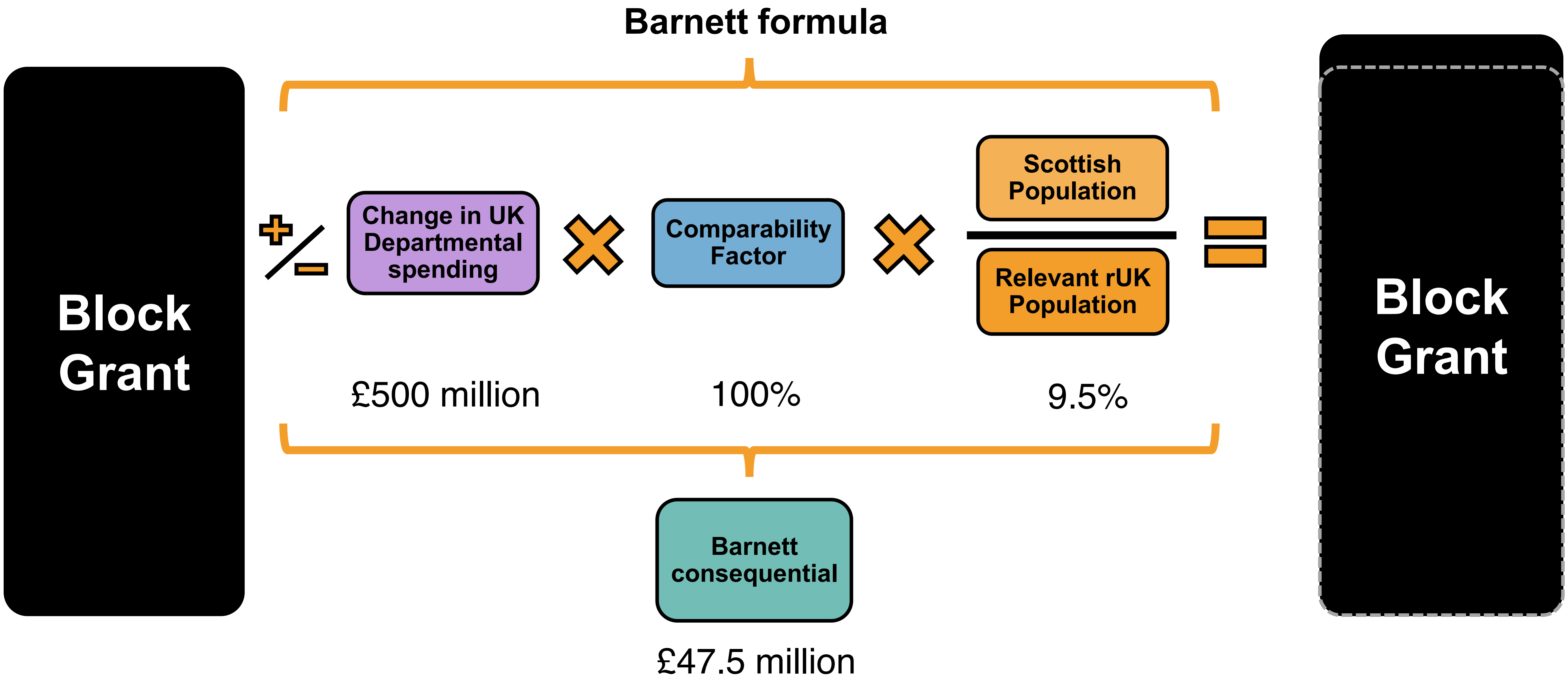
The Scottish Budget process and powers

- Process not event
- Initially about dividing up a fixed budgetary cake, but has evolved in tandem with the political journey of Scotland
- Composition of budget changed following the addition of significant new powers in Scotland Act 2016
- Has become much more complicated - dependent on block grant (UK Govt decisions), tax policy decisions, forecasts (produced by Scottish Fiscal Commission and Office for Budget Responsibility) and subsequent reconciliations, borrowing powers

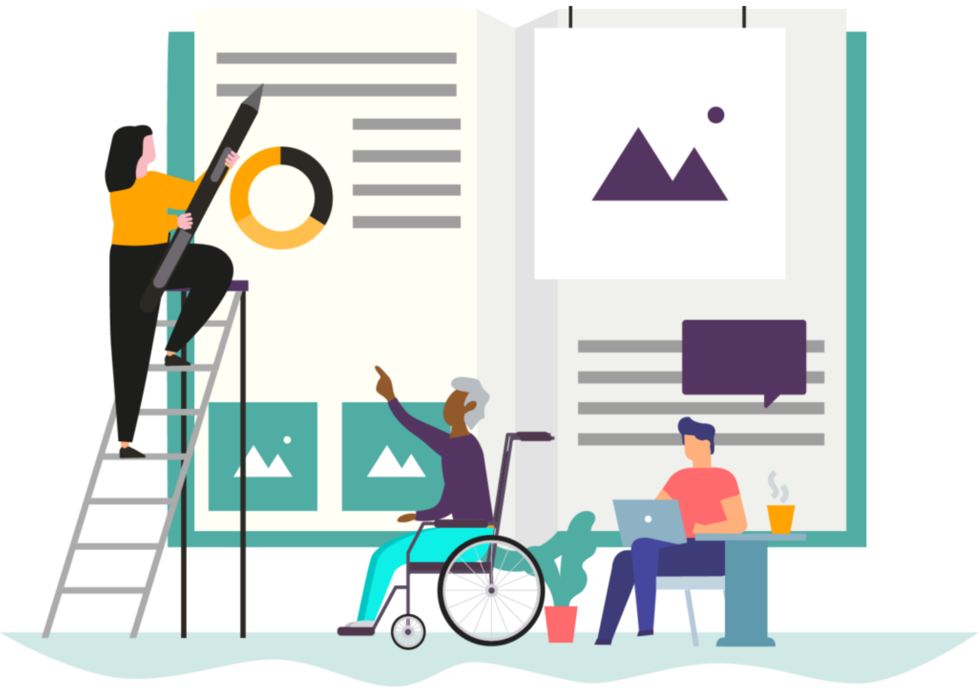
1999: Budget mostly comprised of fiscal transfer from UK Govt (the Block Grant), non-domestic rates the only devolved tax.



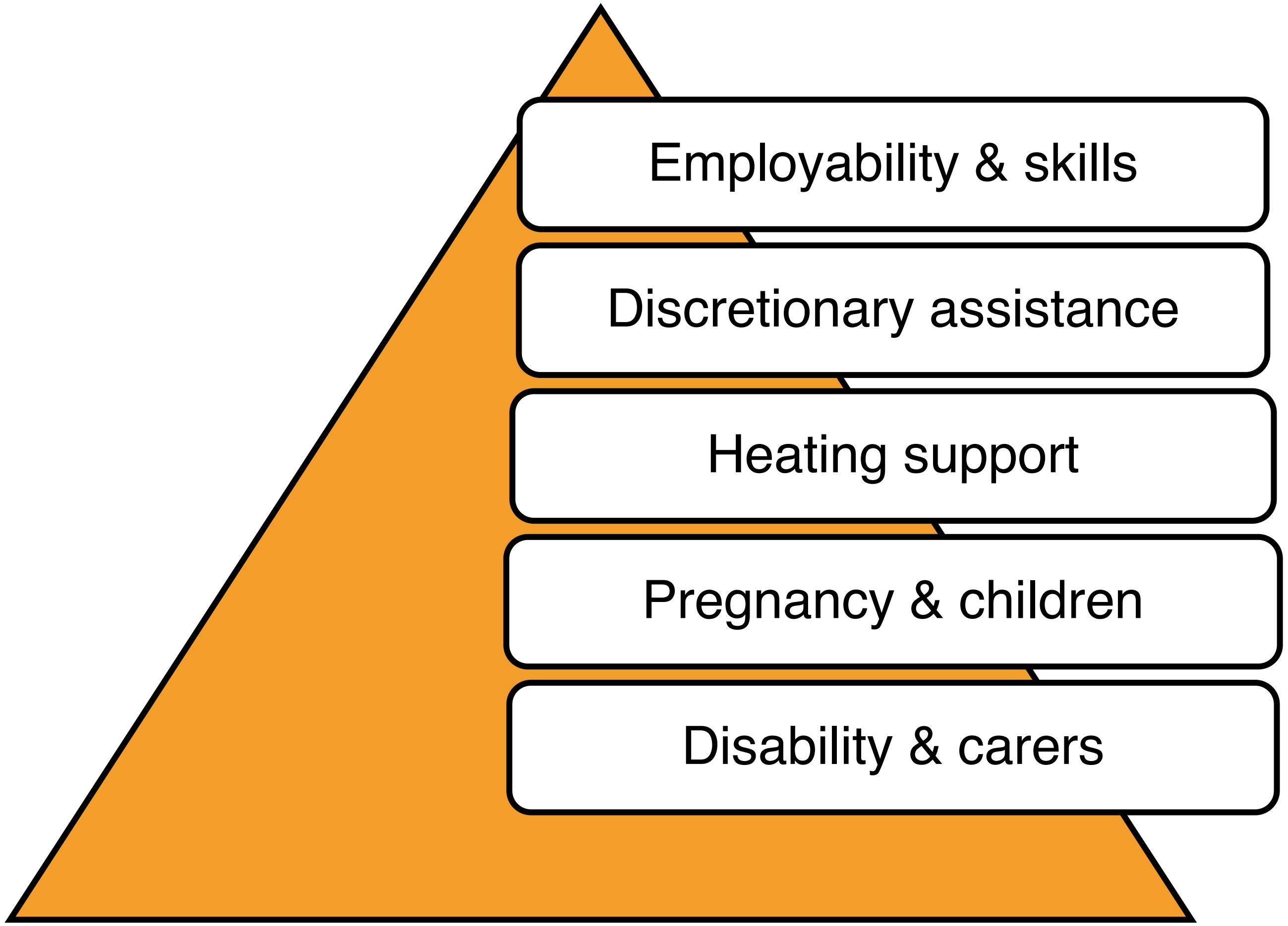
Block Grant changed yearly via Barnett formula



Post 2016: Social Security & Tax Devolution



Some social security has been devolved



To pay for these benefits, the Scottish Government now receives additional funding to the block grant

This additional funding is roughly equivalent to cost of delivering the same level of social security spend per person as in England and Wales

UK Govt. transfers extra funding for social security

Scottish Government is now responsible for devolved social security in Scotland

As the UK Government is no longer paying these benefits, it gives the Scottish Government funding for it on top of the Block Grant.

Social security Block Grant Adjustments

Spending may end up exceeding funding

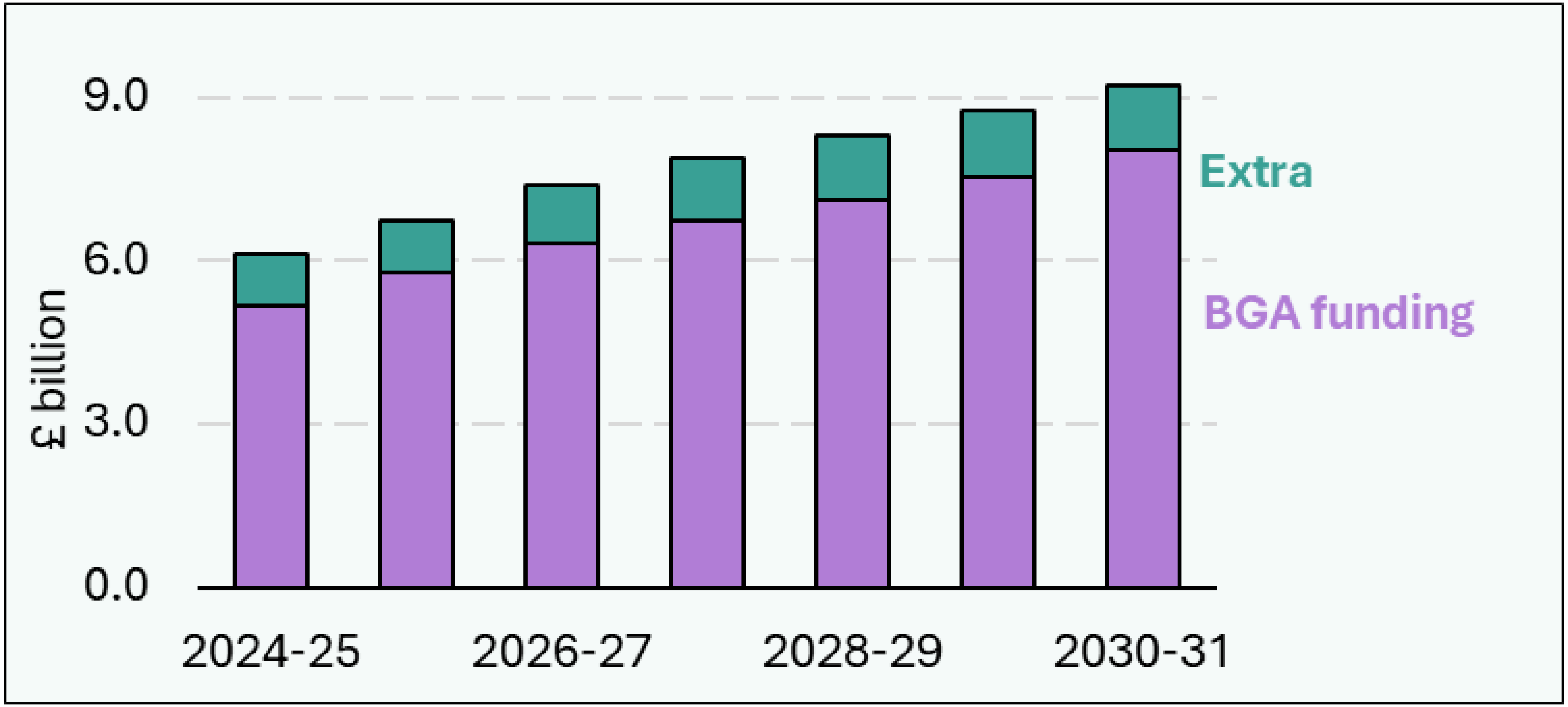
Social security Block Grant Adjustments − **Replacement payments** − **Payments unique to Scotland** = **Extra cost of social security**

The extra cost is largely the result of deliberate choices by Scottish Ministers.

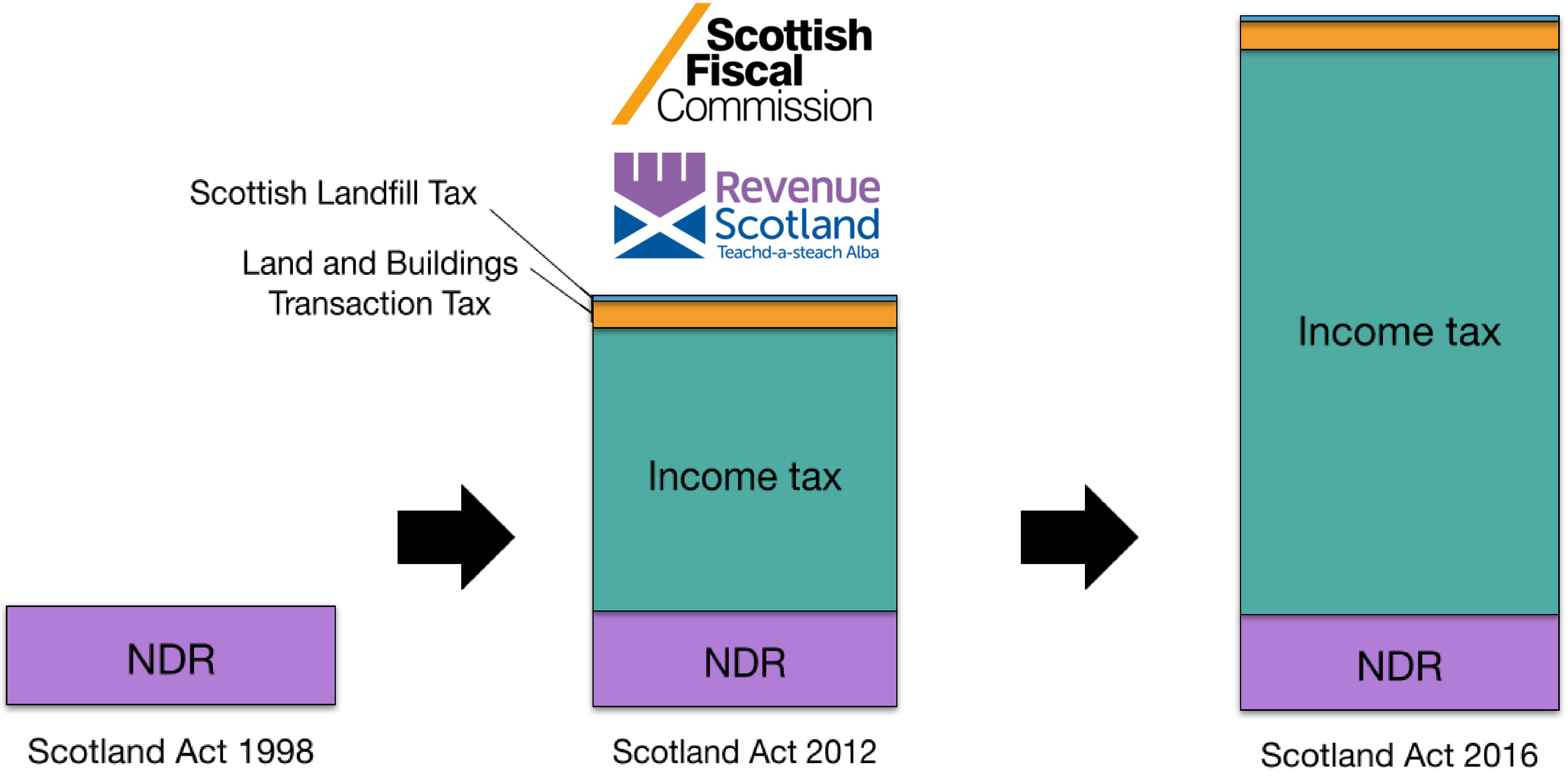
It must be funded from the overall Scottish Budget.

Social security spending: powers but fiscal risks

Social security spending exceeds BGA funding in all years – between £1.0-£1.2bn

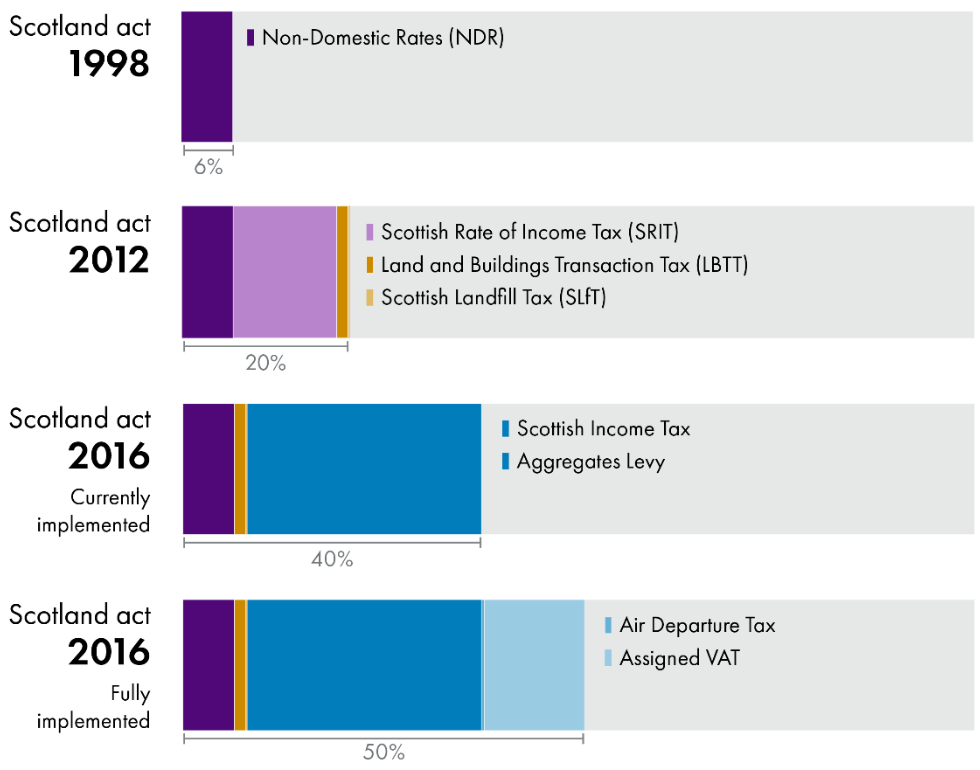


More taxes were devolved from 2012 onwards



Increasing importance of tax powers

- Non-savings non-dividend income tax (£21,508 million in 2026-27)
- Land and Buildings transaction tax (£1,049 million in 2026-27)
- Scottish Landfill Tax (£27 million in 2026-27)
- Scottish Aggregates Tax (£42 million in 2026-27)
- Non-domestic rates (£3,387 million in 2026-27)
- Local Government: Council tax (circa £3,000 million in 2026-27)
- **Coming next year:**
- Air Departure Tax (£428 million in 2027-28)
- **Still to be operationalised**
- Assigned share of VAT (£7,970 million in 2025-26)



Tax devolution does not always mean more!

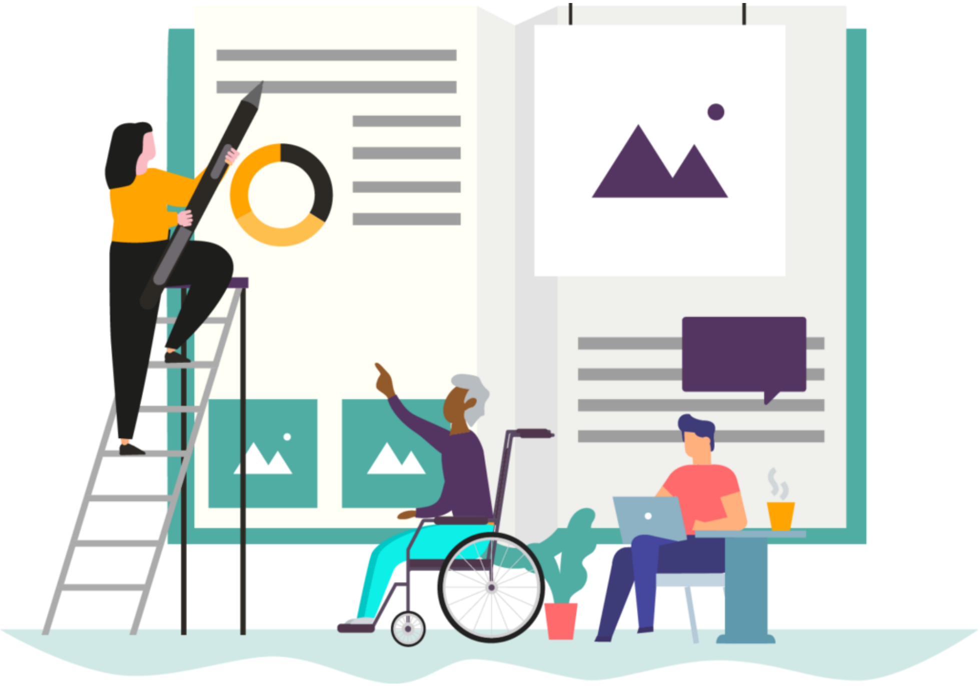
Just like for Social Security, the Scottish block grant is ‘adjusted’ to account for the fact that some taxes are now devolved – a so-called Tax ‘Block Grant Adjustment’

Scottish Tax Revenues − **Tax Block Grant Adjustments** = **Tax net position**

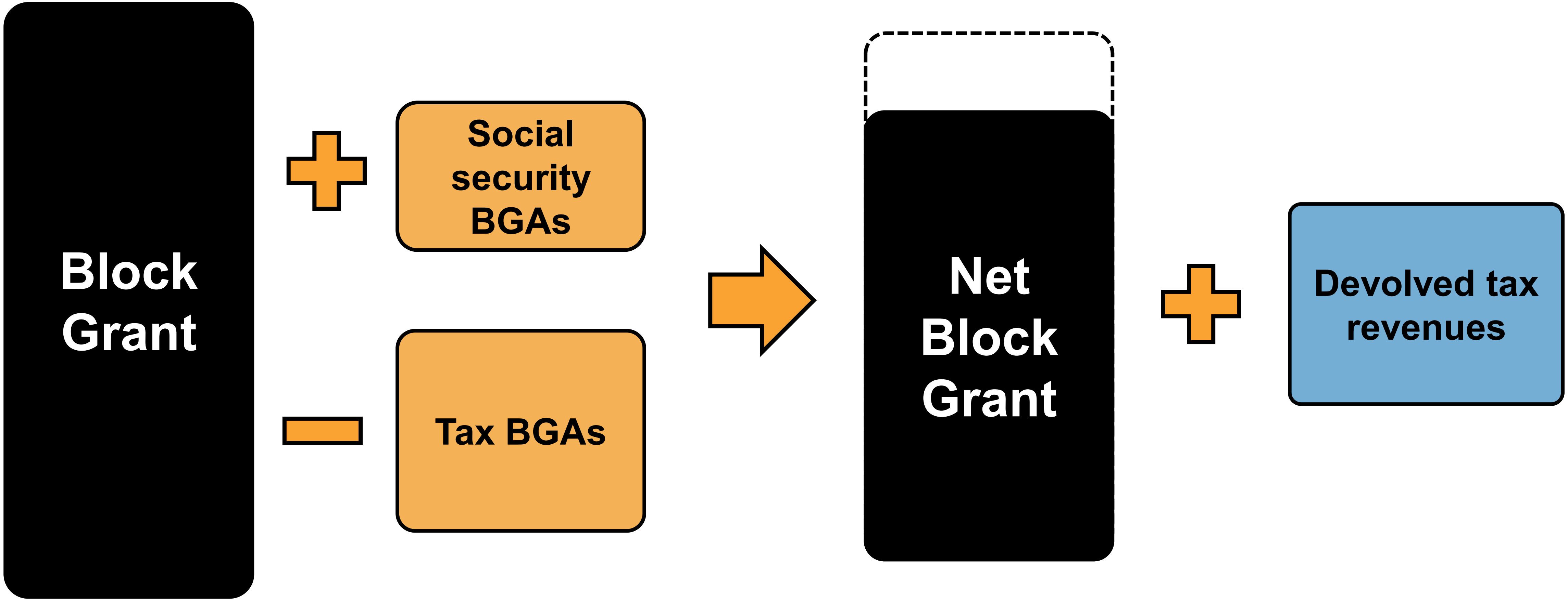
The tax net position can be positive or negative. It depends on

- Tax policy
- The performance of the Scottish economy relative to that of the rest of the UK

How is the Budget funded?



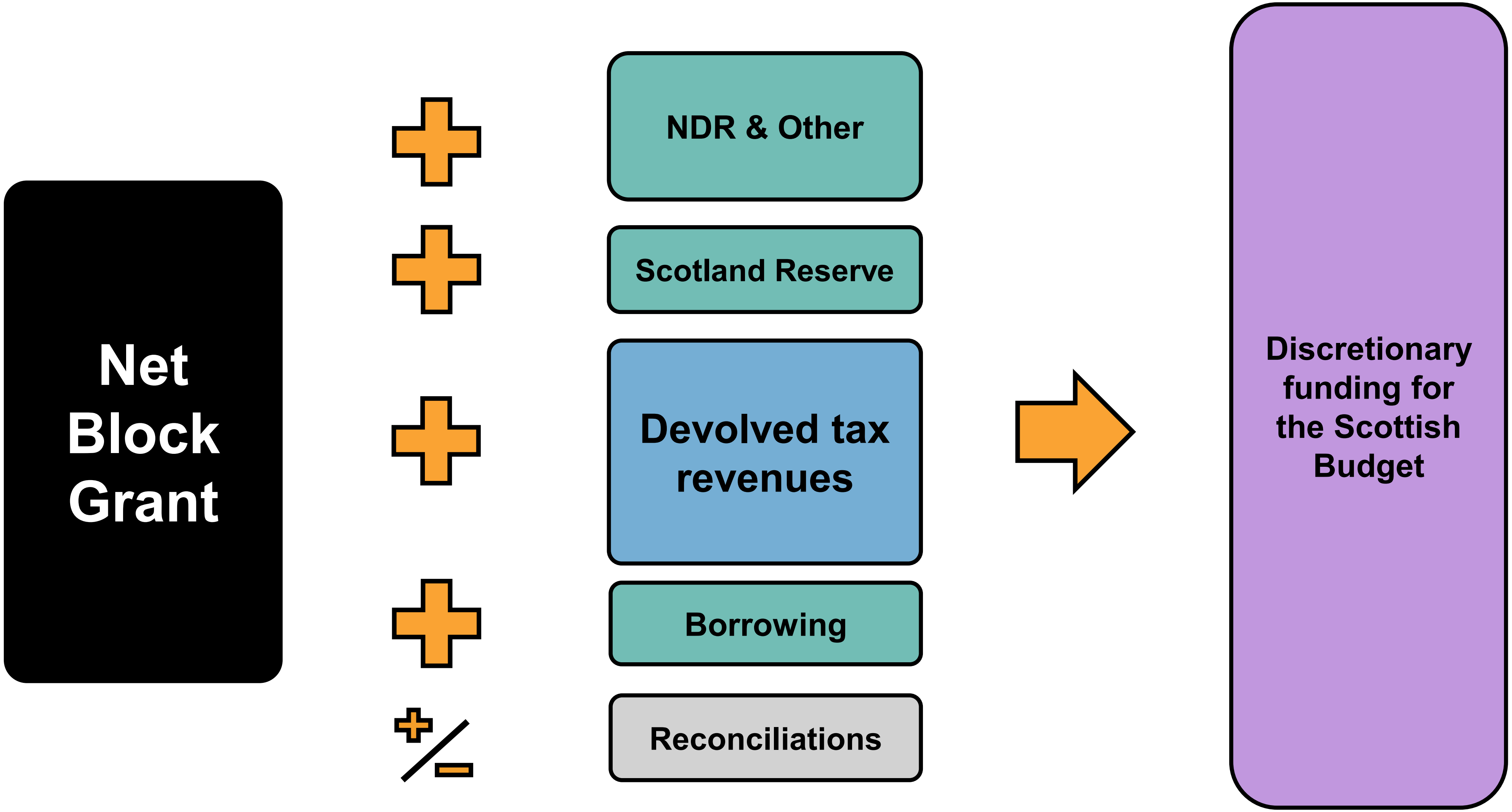
All these combine to shape funding



Governance: Fiscal Framework

- Agreed between the Scottish and UK government in 2016
- Updated (slightly) in 2023 – basically increased borrowing amounts/limits and Scotland Reserve limits to account for inflation from 2024-25
- Sets mechanism for adjusting the block grant (reduction for tax, addition for Social Security)
- Sets Scotland Reserve and limits – allows carry over of unspent monies into the following year, up to limit of £700 million (uprated for inflation since 2024-25)
- Sets borrowing powers and limits:
  - Capital (£450 million per annum up to limit of £3,000 million uprated for inflation since 2024-25)
  - Resource (£600 million per annum for forecast error up to limit of £1,750 million, uprated for inflation since 2024-25)

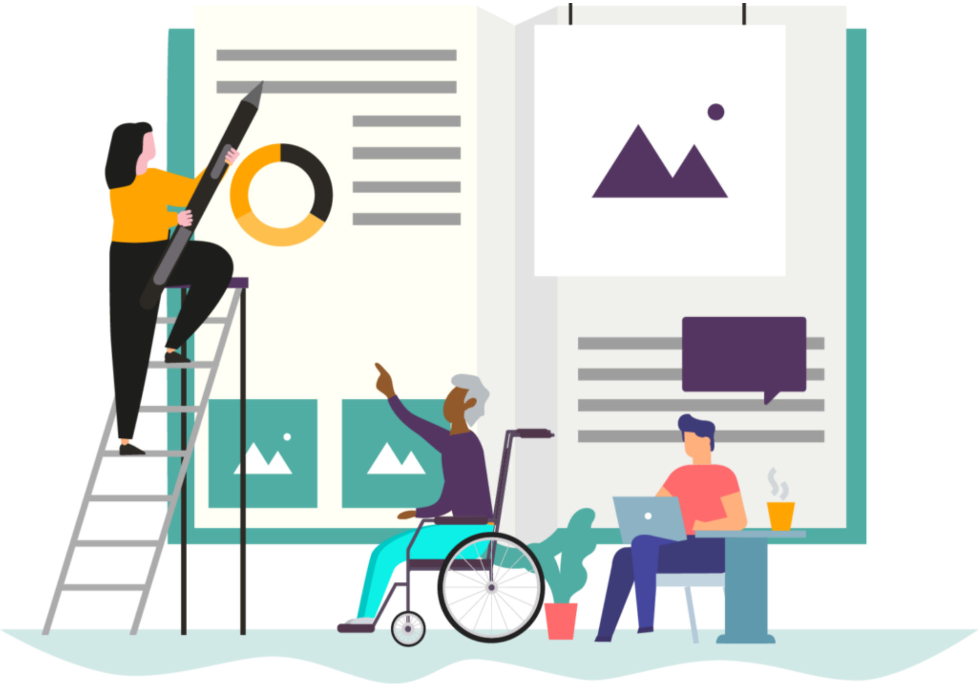
Government has some tools to balance books



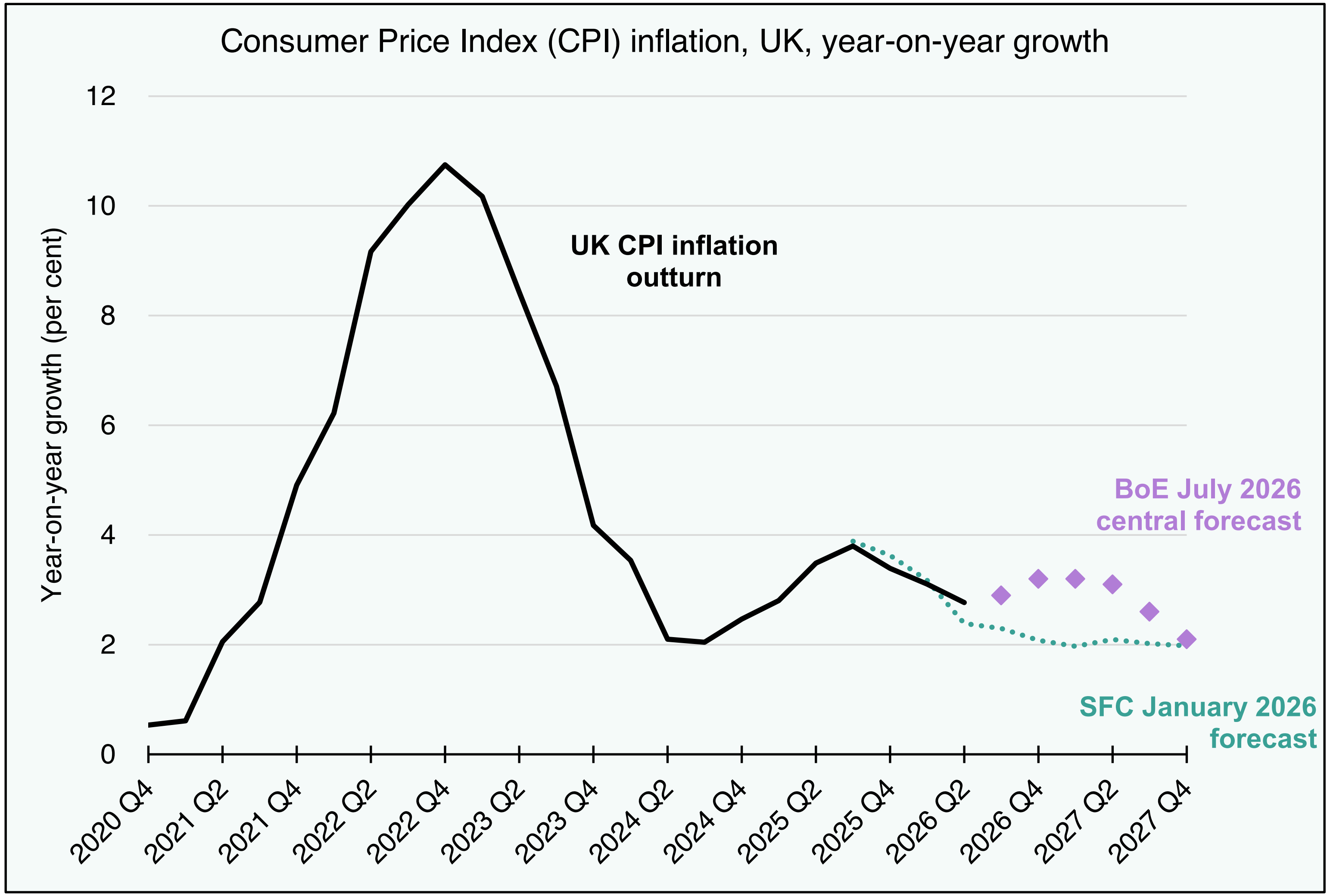
The creation and role of the SFC

- Scotland's independent fiscal institution established in 2017
- Directly accountable to the Scottish Parliament for delivery of functions set out in the Scottish Fiscal Commission Act 2016
- Produce forecasts of Scottish GDP, devolved taxes and spending on social security
- We also set out the Scottish Government funding position in forecasts and provide an assessment of borrowing projections.
- Forecast twice per annum - underpinning Budget (usually in December) and alongside the Medium-term financial strategy (usually May)
- Produce fiscal updates (usually August)
- Fiscal sustainability work – demography, health, climate, pre-election paper on challenges facing this Parliament
- We regularly appear at Committees, and are here to help you in your scrutiny work

Messages from our work: Economy



Inflation higher than previously expected

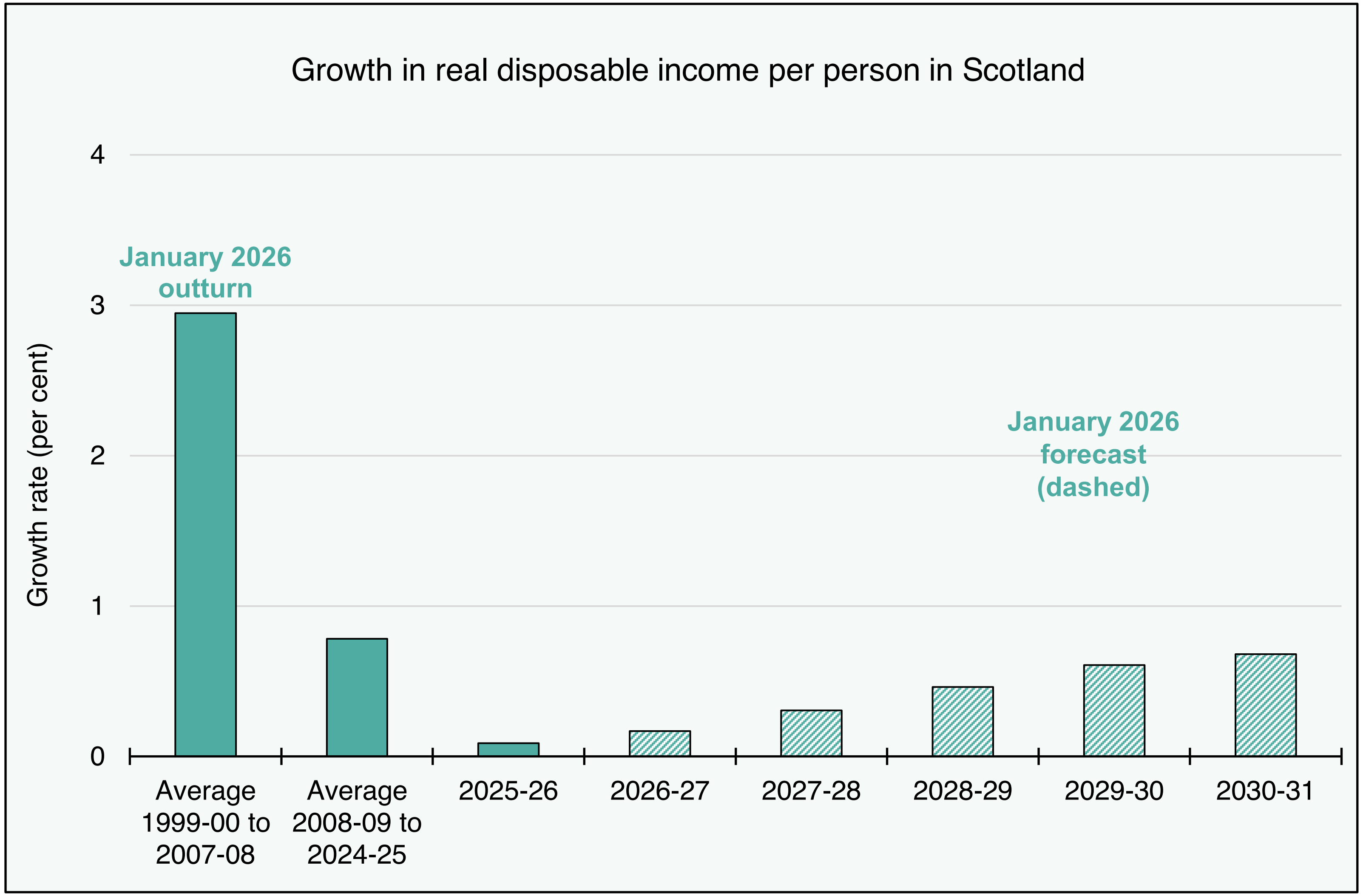


- Since our last forecast in January 2026, the economic outlook has weakened
- Inflation is now expected to be higher over the course of the year

Source: Economy section of the Fiscal Update, Figure 2.1, page 9: [Fiscal Update – August 2026]

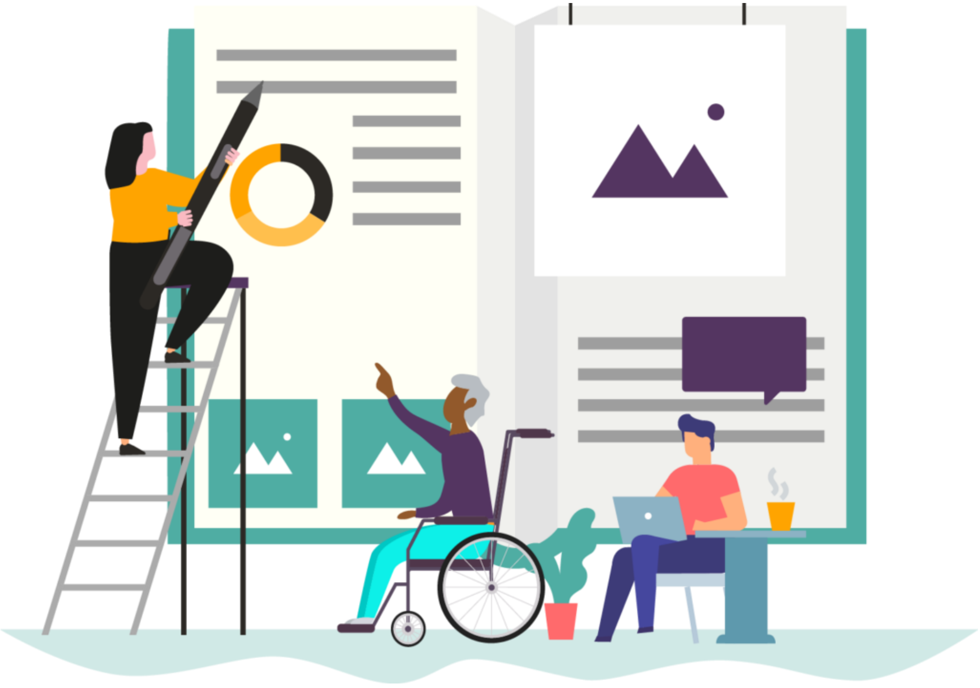
Slow growth in living standards

- In January 2026, we highlighted expectations of slow growth in living standards over the next five years
- Growth may be further weakened by higher inflation, with low-income groups particularly vulnerable



Source: Economy section of the Fiscal Update, Figure 2.3, page 11: [Fiscal Update – August 2026]

Messages from our work: Funding



More funding this year

Latest 2026-27 resource and capital funding position

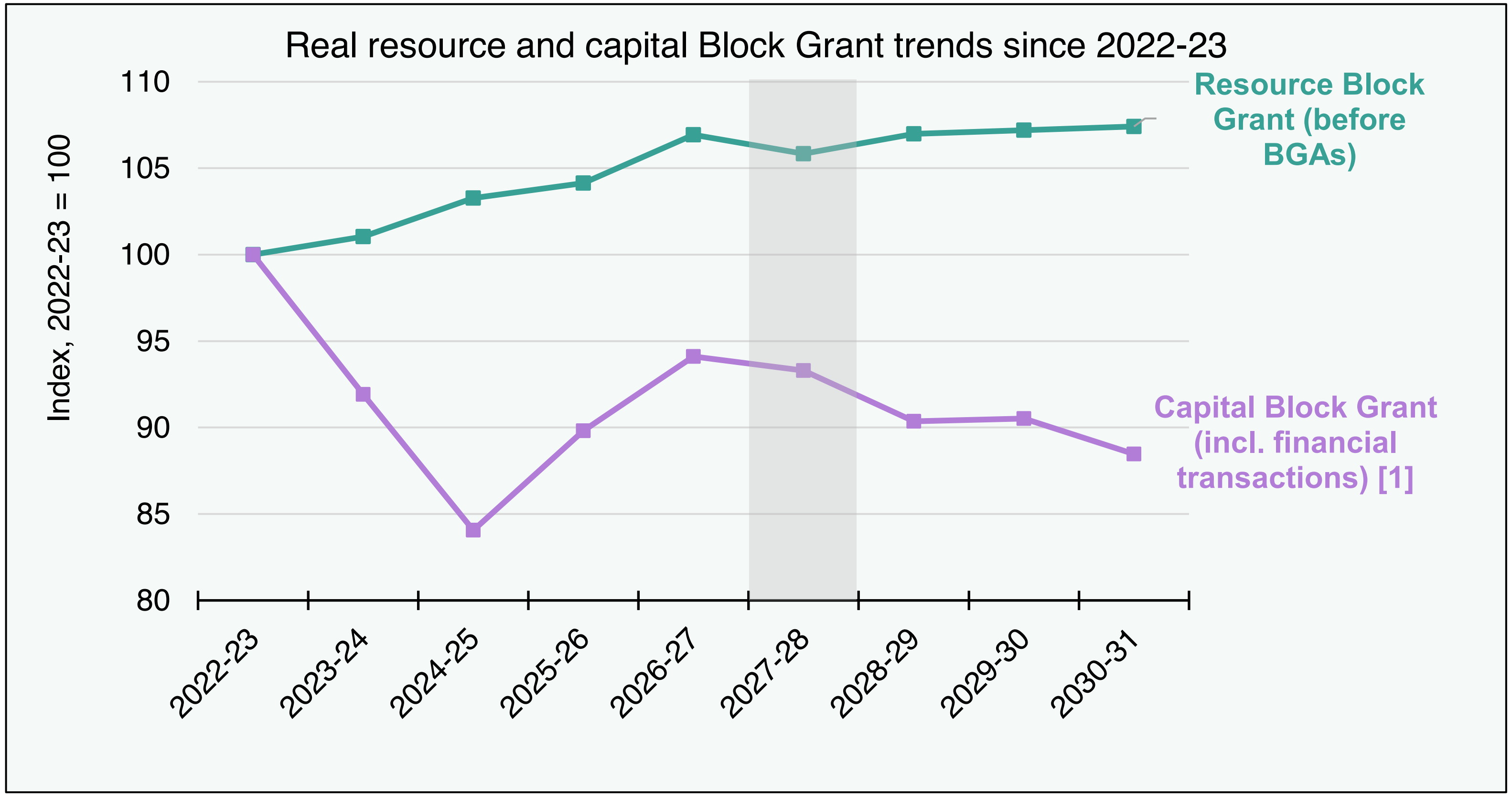
Source of funding (£ million)	January 2026	Changes since January 2026	Latest position
Resource			
Block Grant (before BGAs)	42,671	+625	43,296
Scotland Reserve drawdown	150	+162	312
Other sources	11,294	+44	11,337
Resource funding available for discretionary spend	**54,115**	**831**	**54,946**
Capital (including FTs)			
Block Grant	6,957	-63	6,893
Scotland Reserve drawdown	0	+48	48
Other sources	612	+43	654
Capital funding available for discretionary spend	**7,568**	**28**	**7,596**
Total funding available for discretionary spend	**61,683**	**859**	**62,542**

- After the change in UK leadership, the UK Budget on 28 October could have a significant effect on funding.
- We know of two changes already: additional SEND spending and the Defence Investment Plan
- We see increases to both resource and capital funding in 2026-27 relative to our January forecast

Source: Fiscal Update Supplementary Figures, Figure S3.5: [Fiscal Update – August 2026]

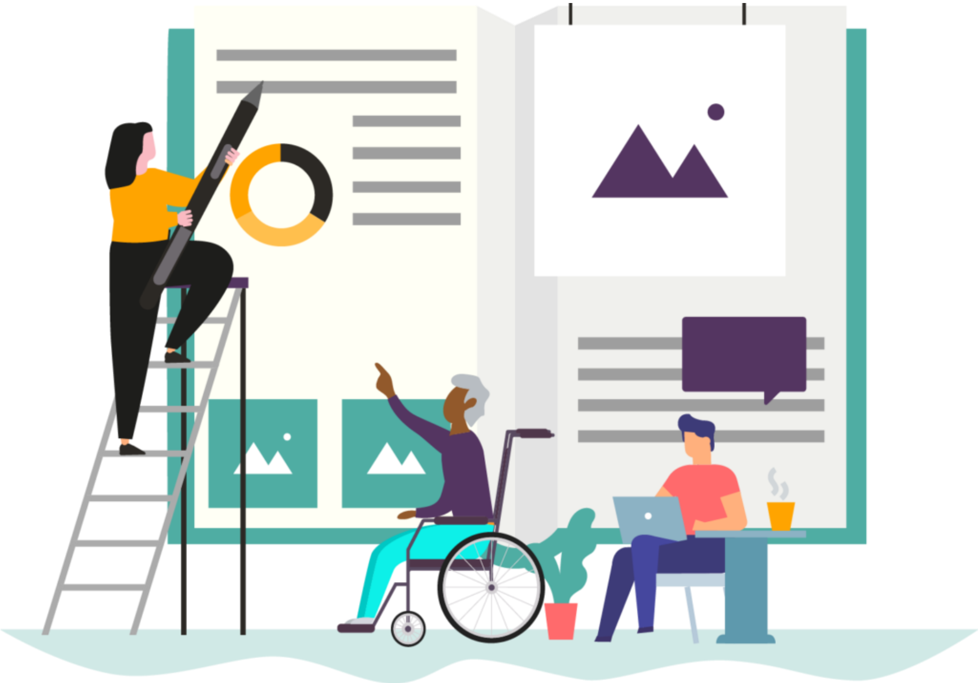
Next year's funding looks challenging

- Both resource and capital Block Grant funding currently expected to fall after adjusting for inflation in 2027-28.
- UK Budget on 28 October may change this position
- Scottish Government decisions on other parts of funding will also be important

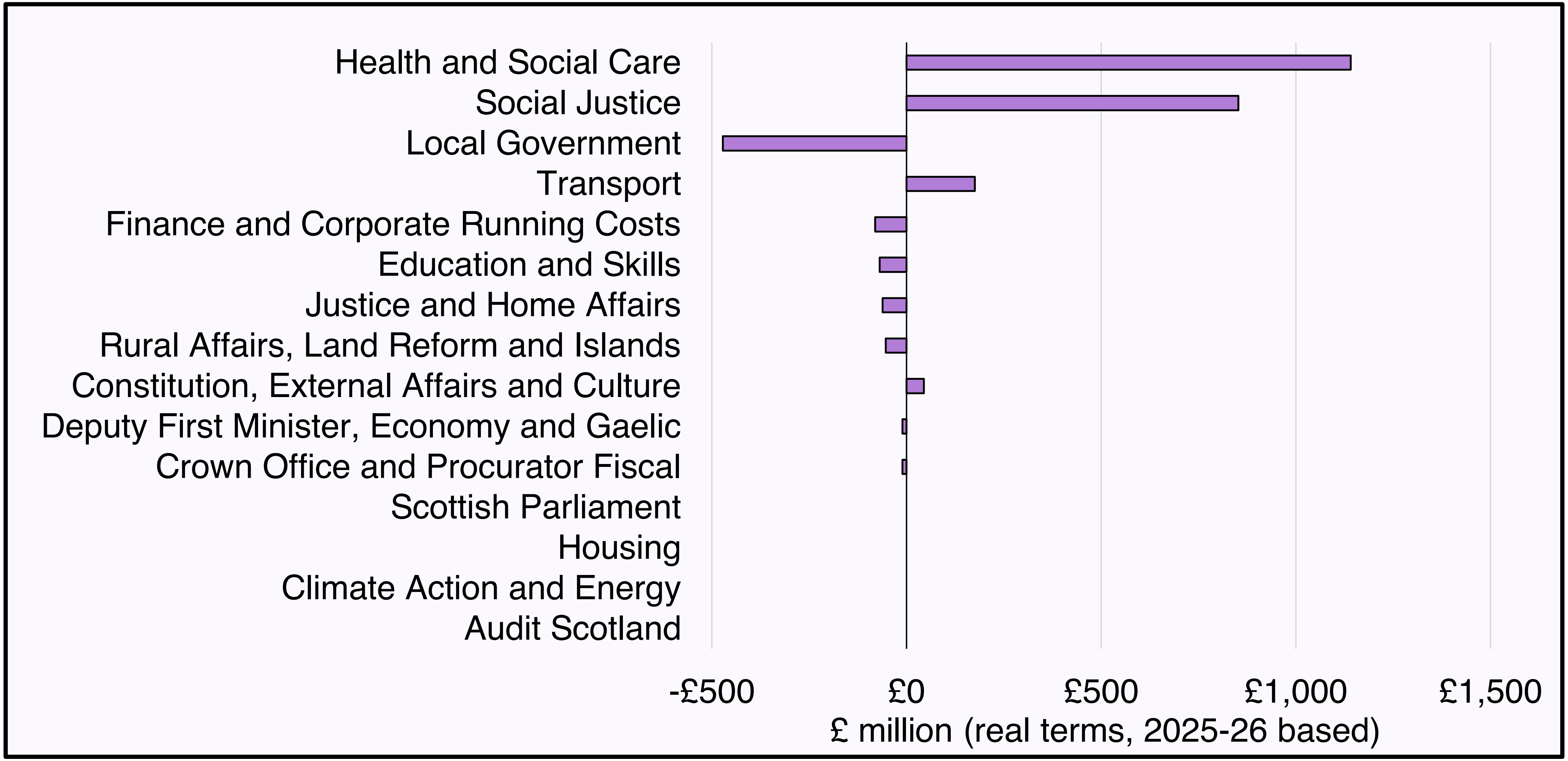


Source: Funding section of the Fiscal Update, Figure 3.2, page 19: [Fiscal Update – August 2026]

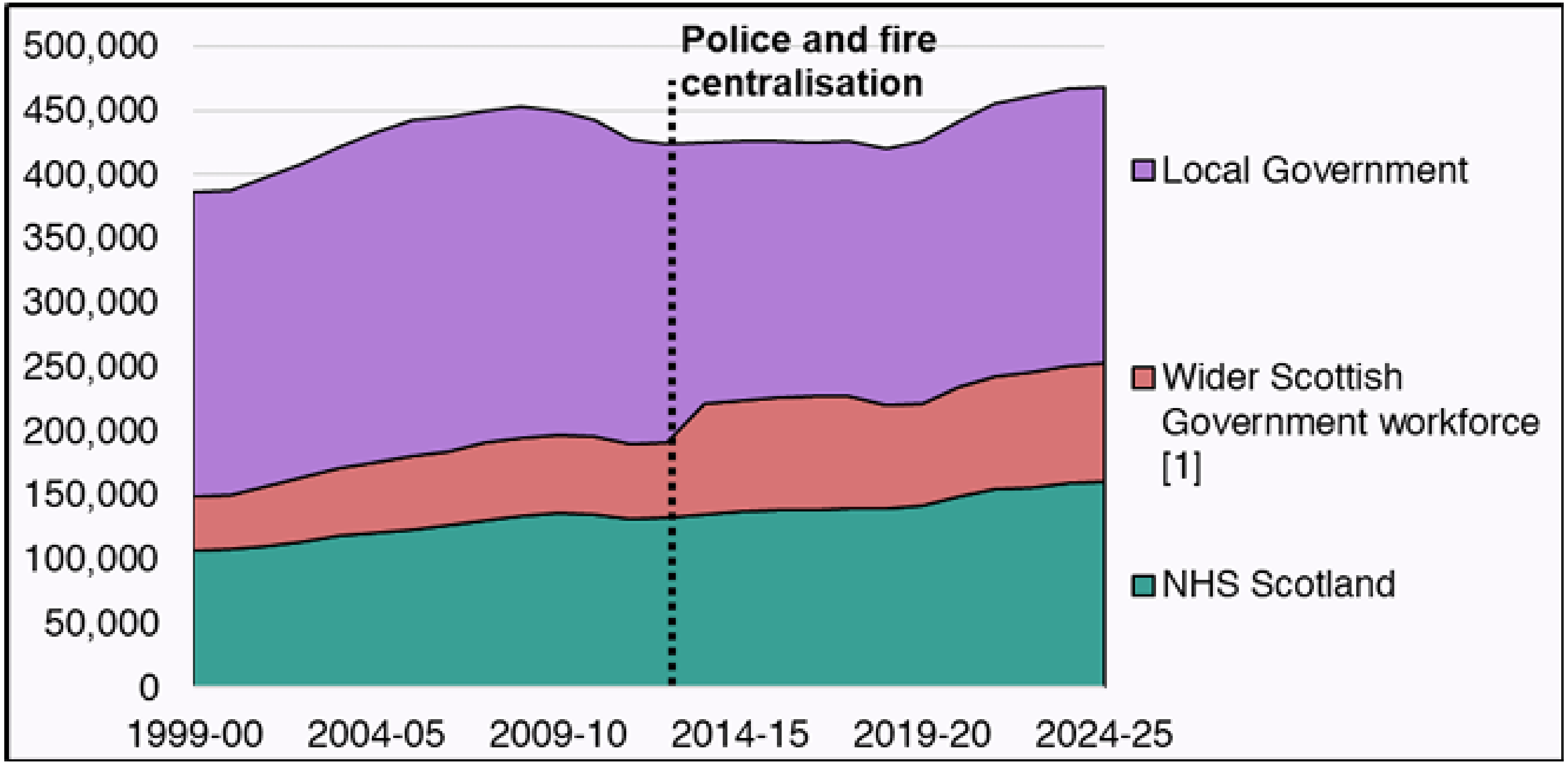
Messages from our work: Spending



Health and Social Care portfolio spending expected to grow the most between 2025-26 and 2028-29



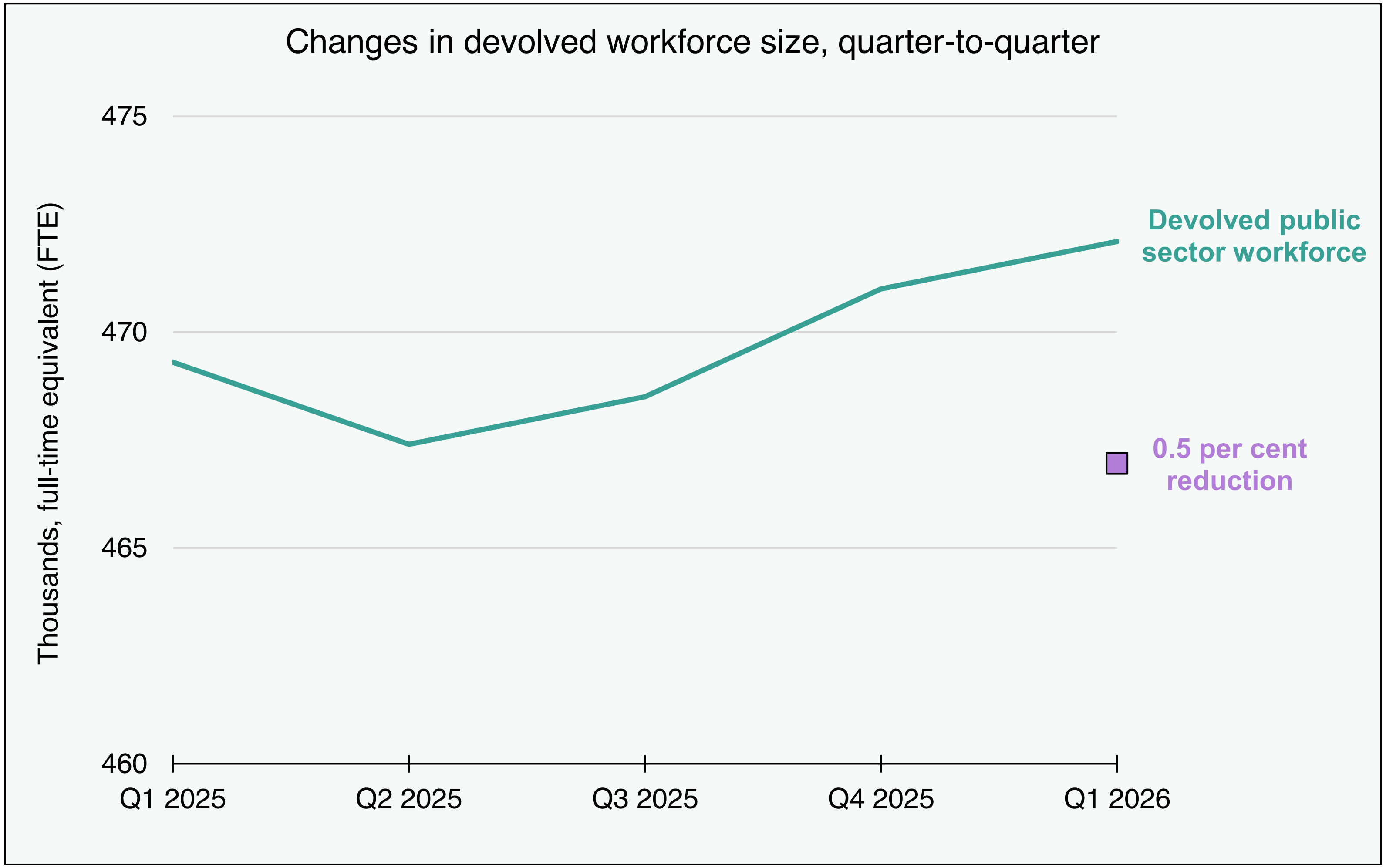
There has been a growing devolved public sector workforce since devolution



[1] Consists of the devolved civil service (Scottish Administration), further education staff, workers of public corporations like Scottish Water or CalMac Ferries Limited, other public bodies, and (since 2013-14) police and fire officers following their centralisation.

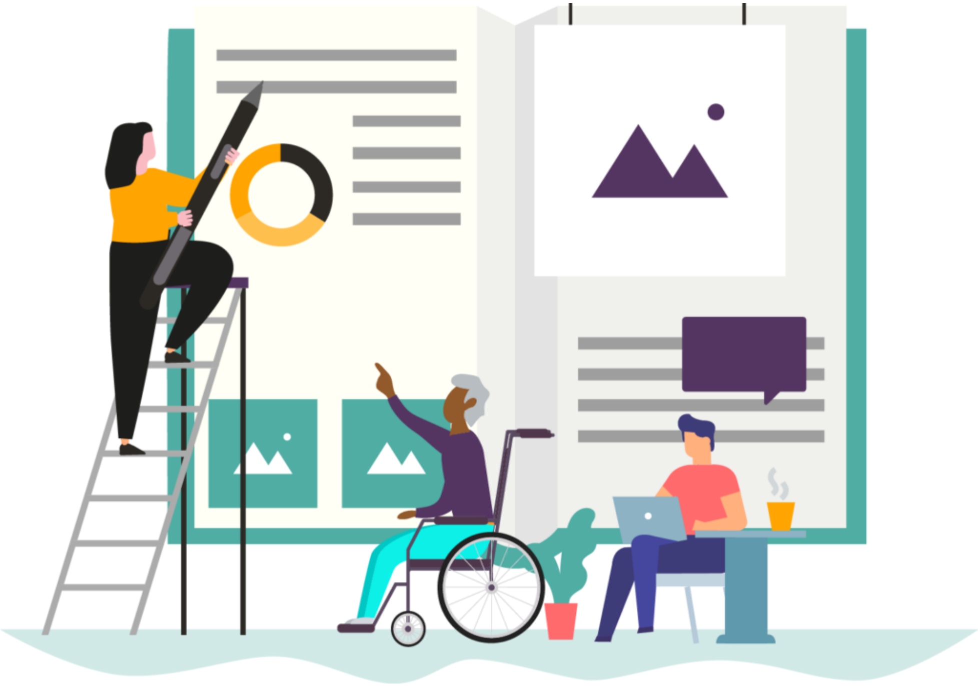
Workforce reductions plans off-track

- The Fiscal Sustainability Delivery Plan set a target for an average annual 0.5 per cent reduction in workforce to 2029-30
- Growth in the size of the workforce last year means greater reductions required in future years to meet this target

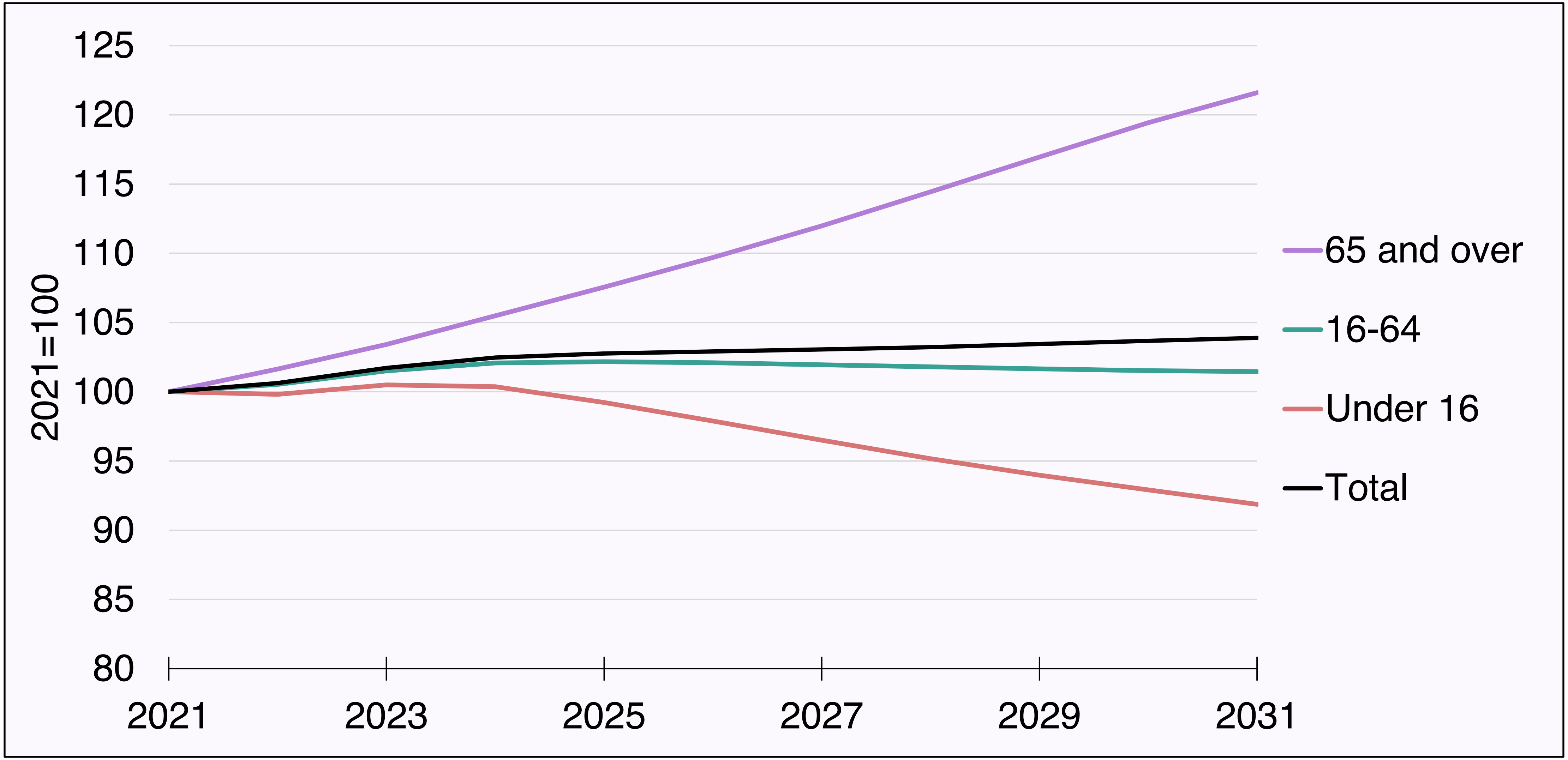


Source: Spending section of the Fiscal Update, Figure 4.2, page 32: [Fiscal Update – August 2026]

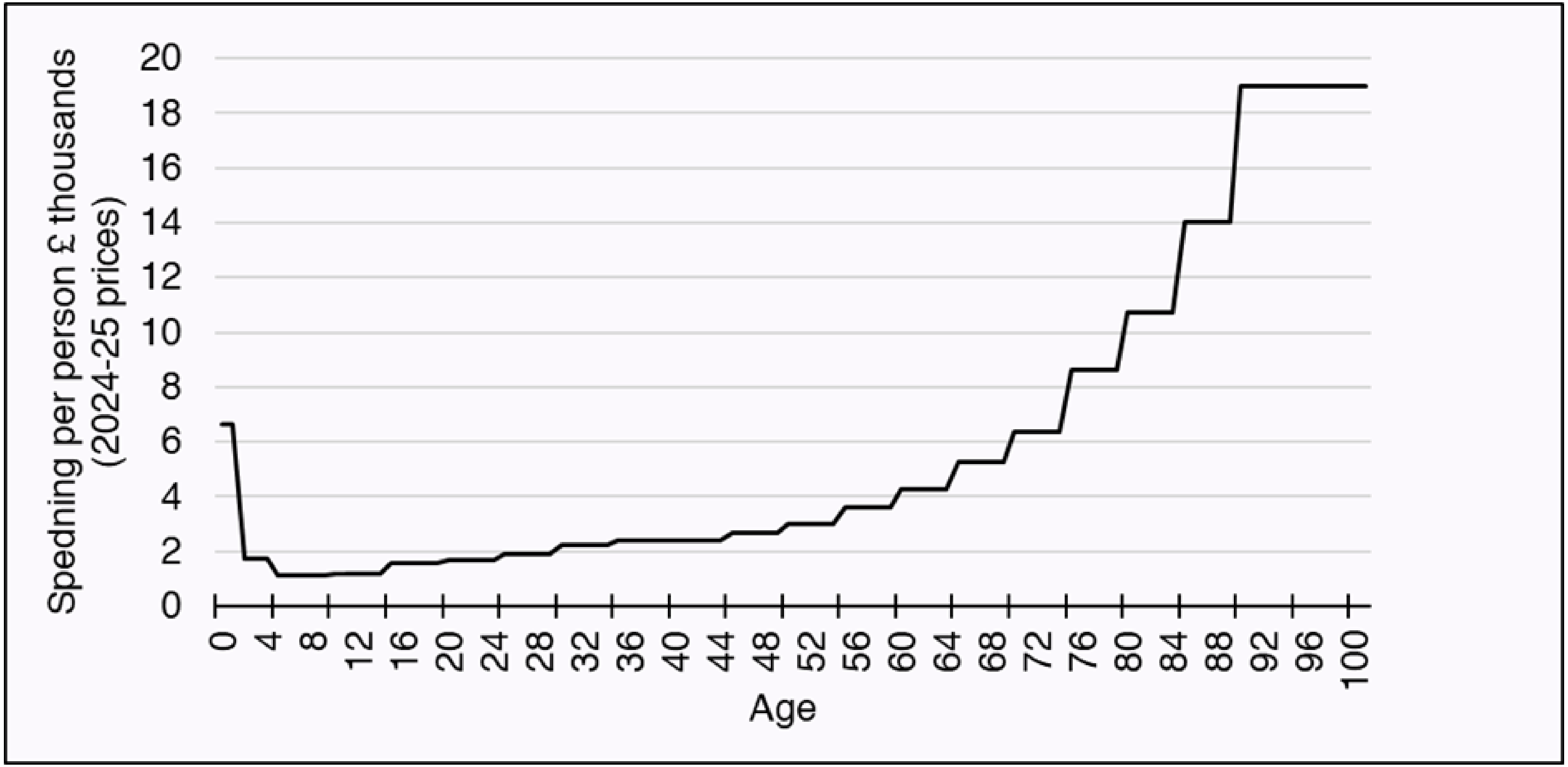
Trends and challenges



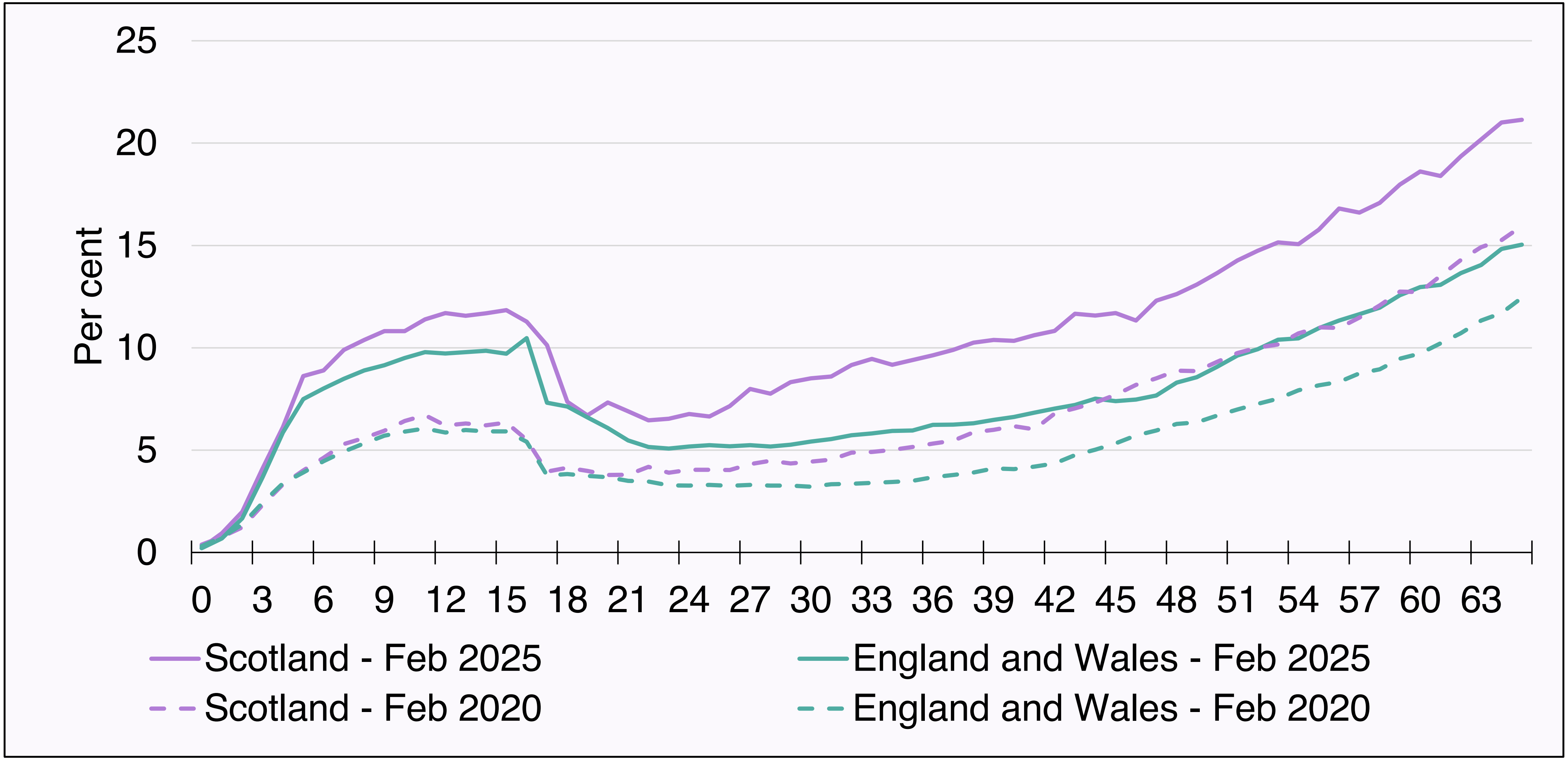
Scotland's over 65 population is growing



Other than for children under five, health spending increases with age



Disability prevalence rate is higher in Scotland for all ages, and has risen since 2020



Thank you for listening