HM Government

The agreement between the Scottish Government and the United Kingdom Government on the Scottish Government's fiscal framework

August 2023

Scottish Government
Riaghaltas na h-Alba

THE AGREEMENT

Between the Scottish Government and the United Kingdom government on the Scottish Government's fiscal framework

1. The Smith Commission was convened in September 2014 and charged with reaching a cross-party agreement on the devolution of further powers to the Scottish Parliament. Lord Smith of Kelvin oversaw the process. The Smith Commission published its report detailing Heads of Agreement on 27 November 2014.[1]

2. Both governments are committed to the implementation of the Smith Commission's conclusions including the creation of a new Scottish Government fiscal framework consistent with the overall UK government's fiscal framework.

3. Both the Scottish Government and the UK government are committed to financial responsibility and democratic accountability, incentivising the Scottish Government to increase economic growth while allowing Scotland to contribute to the UK as a whole.

4. Additionally, the Governments are committed to a sustainable overall fiscal position for public finances both within Scotland and the UK as a whole.

5. The Scottish Government will be able to exercise its fiscal powers fully and flexibly while operating within a sustainable fiscal framework for the whole of the UK.

Principles of the Fiscal Framework

6. The agreed fiscal framework set out in this document is consistent with the principles in the Smith Agreement. Annex A sets out the principles for the Scottish Government's fiscal framework recommended by the Smith Commission and agreed by the Scottish and UK governments.

Funding the Scottish Government's budget

7. As set out in the Smith Agreement, changes in the Scottish Government's block grant will continue to be determined via the operation of the Barnett Formula. Under the Barnett Formula, the Scottish Government's block grant in any given

[1] https://www.smith-commission.scot/

financial year is equal to the block grant baseline plus a population share of changes in UK government spending on areas that are devolved to the Scottish Parliament. This will continue to apply to changes in UK government spending on areas that are devolved to the Scottish Parliament. In future, the Scottish Government will retain all devolved and assigned Scottish tax revenues.

8. For all further spending powers other than welfare (and any other areas explicitly set out in this document) the normal approach to machinery of government changes will determine the initial baseline adjustments, with the full programme costs in and for Scotland being transferred at the point of devolution for the remainder of the Spending Review period. This change will be baselined and the Barnett formula will subsequently apply to changes in UK government spending in these areas. For the employment programmes, the Barnett formula will apply to changes in the entirety of UK government spending, including any elements funded through payment by results.

The block grant adjustments for taxation and welfare

9. The block grant to the Scottish Government will be adjusted to reflect the introduction of devolved and assigned revenues, and the transfer of responsibility for welfare.

10. The adjustments will involve two elements: an initial block grant baseline adjustment (a deduction in relation to tax and an addition in relation to welfare) and an indexation mechanism.

<u>Baseline adjustments to the Block Grant</u>

11. The initial baseline deduction for tax[2] will be equal to the UK government's receipts generated from Scotland in the year immediately prior to the devolution of powers. This agreement is without prejudice to the block grant adjustments agreed in respect of Landfill Tax and Stamp Duty Land Tax for 2015-16, no revisions will be applied to the block grant adjustments for that financial year.

12. The baseline adjustment for Stamp Duty Land Tax will take into account the forestalling that is estimated to have occurred, which will reduce the baseline adjustment by £20m. No further forestalling effects in relation to the implementation of new powers will be taken into account.

[2] Revenues from Scottish courts and tribunals will be treated in the same way as devolved/assigned taxes.

13. The initial baseline addition to the block grant for devolved welfare payments will be the UK government's spending on these areas in Scotland in the year immediately prior to the devolution of powers, with the exception of the Cold Weather Payment. Reflecting the substantial volatility of the Cold Weather Payment, the initial baseline addition will be an average of the UK government's spending in Scotland on this benefit from 2008-09 to the year prior to devolution.

14. The indexation mechanisms set out below will be operated separately for each tax and welfare power and applied annually.

Indexation mechanisms

15. The indexation mechanism for tax[3] and welfare will be the Indexed Per Capita (IPC), thereby delivering the same outcome as the 2016 agreement. This will ensure that the Scottish Government's overall level of funding will be unaffected if Scotland's population grows differently from the rest of the UK.

Commencement dates and transition periods

16. The Scottish Rate of Income Tax came into effect from April 2016 and operated for one transitional year before the full devolution of the Smith Income Tax powers. During this transition year there was no reconciliation of forecasts to outturn (for the tax revenues or the block grant adjustment) as previously agreed under Scotland Act 2012.

17. Full devolution of income tax rates and thresholds for non-savings and non-dividend income commenced in April 2017.

18. The Joint Exchequer Committee (JEC) will agree on a suitable point for the commencement for devolution of the Aggregates Levy and Air Passenger Duty.

19. Revenues from courts and tribunals in Scotland will be retained by the Scottish Government from April 2017.

20. The implementation dates for welfare will be agreed by the Joint Ministerial Working Group on Welfare. The Joint Exchequer Committee will oversee the transfers of funding.

[3] Revenues from Scottish courts and tribunals will not be subject to indexation.

Administration and implementation costs

21. There are administration and implementation costs associated with the powers being devolved. In line with the Smith Commission recommendations the UK government will transfer funding to support a share of the associated implementation and running costs for the functions being devolved.

22. In 2016, both Governments agreed that the UK government will provide £200m to the Scottish Government to support the implementation of new powers. This represented a one-off (non-baselined) transfer, supplementing the block grant, to support the functions being transferred. The profile of this transfer was agreed by the JEC.

23. The Governments have agreed a baseline transfer of £66m to cover the ongoing administration costs associated with the new powers. This figure includes the marginal savings realised by the UK government as a result of no longer administering the powers in Scotland devolved under the current Scotland Bill, plus a share of the Scottish Government's running costs. This baseline transfer is indexed through the normal application of the Barnett formula. In line with the Smith Commission report, additional administration and programme costs directly associated with the exercise of the powers in paragraphs 44 to 45 of the Smith Commission Heads of Agreement will be met by the Scottish Government, these relate to the powers to vary elements of Universal Credit.

24. All administration and programme costs incurred by the Scottish Government due to the creation of new welfare benefits or making discretionary payments will be met by the Scottish Government.

25. In line with the approach taken for the Scottish Rate of Income Tax, the Scottish Government will reimburse the UK government for net additional costs wholly and necessarily incurred as a result of the implementation and administration of the Income Tax powers.

26. The Scottish Government will reimburse the UK government for any net additional costs wholly and necessarily incurred in 'switching off' APD and Aggregates Levy in Scotland.

27. Both Governments have agreed to share equally all costs wholly and necessarily incurred as a result of the implementation and administration of VAT assignment.

28. All other demonstrable and jointly agreed net costs to the UK government wholly and necessarily incurred as a result of the devolution of powers will be met by the Scottish Government.

29. All costs incurred by the UK government where the Scottish Government is expected to meet the costs will be subject to audit.

Value Added Tax (VAT)

30. Receipts from the first 10p of the standard rate of VAT and the first 2.5p of the reduced rate of VAT in Scotland will be assigned to the Scottish Government.

31. The assignment of VAT will be based on a methodology that will estimate expenditure in Scotland on goods and services that are liable for VAT. It was agreed in the 2016 Fiscal Framework agreement that the full details of the VAT assignment methodology will be jointly developed and agreed by both HMRC and Scottish Government officials.

32. Once completed and agreed by officials. the assignment methodology and operating arrangements will be presented for joint ministerial sign-off at a future meeting of the Joint Exchequer Committee. The JEC will also agree arrangements for production of VAT revenue forecasts and a suitable point for the commencement of VAT assignment.

33. To allow the development and testing of the methodology for calculating Scotland's aggregated share of VAT liabilities, VAT assignment will continue to be forecast and calculated each year, but with no impact for the Scottish Government.

No detriment due to policy spillovers effects

34. The Smith Commission stated that there should be no detriment as a result of UK government or Scottish Government policy decisions post-devolution.

35. Specifically, where either government makes a policy decision that affects the tax receipts or expenditure of the other, the decision-making government will either reimburse the other if there is an additional cost, or receive a transfer from the other if there is a saving.

36. These financial consequences of policy decisions have been termed policy spillover effects.

37. The main categories of these can be divided into:

- Direct effects – these are the financial effects that will directly and mechanically exist as a result of the policy change (before any associated change in behaviours); and

- Behavioural effects – these are the financial effects that result from people changing behaviour following a policy change.

38. Other indirect or second-round effects may also arise from policy changes, and the Governments have agreed that the financial consequences of these should not be included in the scope of the “no detriment” principle. This is because of the difficulty in demonstrating and agreeing both causality and the scale of any financial impact.

39. The UK and Scottish Governments have agreed to account for all direct effects.

40. Behavioural effects that involve a material and demonstrable welfare cost or saving will be taken into account where these are in exceptional circumstances. Behavioural effects that impact tax revenues can be taken into account where, in exceptional circumstances, they are demonstrated to be material and both governments agree that it is appropriate to do so.

41. Assessment of causality and of the scale of any financial impacts will be based on and supported by a shared understanding of the evidence.

42. Any decision or transfer relating to a spillover effect must be jointly agreed by both Governments. Without a joint agreement, no transfer or decision will be made.

43. Issues relating to spillovers will first be discussed by officials in both Governments. Where officials are unable to reach an agreement this will be discussed by Ministers at the JEC. Where the Governments are unable to reach agreement at official or ministerial level a dispute can be raised. The arrangements for resolving disputes on spillover effects and the wider fiscal framework are set out below under dispute resolution.

Capital borrowing

44. The Governments have agreed that from 2023-24 onwards, the statutory limit on borrowing for capital expenditure will be increased to and maintained at £3bn in 2023-24 prices (using the OBR’s GDP deflator forecast at the time of the Scottish Government’s draft Budget). The annual limit on the amount of borrowing for capital expenditure will also be increased. From 2023-24 onwards, it will now be maintained at £450m a year in 2023-24 prices (again using the OBR’s GDP deflator forecast at the time of the Scottish Government’s draft Budget). Both limits will be uprated annually.

45. The Scottish Government will notify the Treasury monthly on its planned capital borrowing, its outstanding debt and repayment profile, but will be able to borrow within the agreed limits as it deems appropriate.

46. These capital borrowing limits are in addition to the Scottish Government's capital block grant, which will continue to be calculated in accordance with the Barnett formula.

47. The UK government will amend the Scotland Act accordingly to increase the aggregate borrowing limit as necessary.

48. The Scottish Government may borrow through the UK government from the National Loans Fund, by way of a commercial loan (directly from a bank or other lender), or through the issue of bonds. Borrowing for capital expenditure will be in pounds Sterling.

49. The repayment arrangements are to remain consistent with the Scotland Act 2012 and to be finalised in a revised Memorandum of Understanding between the Scottish Government and UK government. Under these arrangements, the term of any loan would normally be for 10 years, but where the lives of the assets being purchased through the loan justify longer or shorter terms, these can be agreed.

Resource borrowing

50. Under the Scotland Act 2012, the Scottish Parliament is responsible for around £9bn in taxation. Under the Smith Agreement powers as agreed in 2016, the Scottish Parliament was responsible for nearly £21bn in devolved and assigned tax revenue and over £2bn in demand-led welfare spending. The Governments have agreed a set of fiscal tools to enable the Scottish Government to manage the additional risks and volatility associated with the devolution of these powers.

51. Prior to the fiscal framework agreed in 2016, the Scottish Government had a total resource borrowing limit of £500m that could be used in specified circumstances. Scotland Act 1998 first enabled the Scottish Government to borrow up to £500m from the National Loans Fund (NLF) to meet an in-year excess in expenditure over income or to provide a working balance in the Scottish Consolidated Fund.

52. The Scotland Act 2012 extended this facility to enable the Scottish Government to borrow from the NLF across financial years when devolved tax revenues are lower than forecast. This form of borrowing is repayable within four years rather than in-

year. An annual limit of £200m was set administratively within a statutory £500m overall limit.

53. Under this agreement, the Scottish Government will have the power to borrow up to £600m each year within a statutory overall limit for resource borrowing of £1.75bn, with both limits in 2023-24 prices (using the OBR's GDP deflator forecast at the time of the Scottish Government draft Budget). The Scottish Government may pursue resource borrowing within these limits for the following reasons:

- for in-year cash management;
- for forecast error in relation to devolved and assigned taxes and demand-led welfare expenditure arising from forecasts of Scottish receipts/expenditure and corresponding UK forecasts for the block grant adjustments.

54. These enhanced borrowing powers will apply from 2023-24 onwards, and will be maintained in real terms going forward, with annual and overall limits to be uprated annually.

55. Resource borrowing will continue to be from the National Loans Fund, and the repayment period will be between three and five years, as determined by Scottish Ministers at the time of borrowing. The Scottish Government will provide regular monthly forecasts to the Treasury of the amount of resource borrowing it expects to make, outstanding debt and repayment profiles, but will be able to borrow within the agreed limits as deemed appropriate.

Scotland Reserve

56. The Scotland Act 2012 provided the Scottish Government with a cash reserve to build up funds when devolved revenues are higher than forecast and drawdown funds when devolved revenues are lower than forecast. The reserve must be held within the UK government rather than with a commercial bank.

57. For five years from June 2011, the Scottish Government has been able to make discretionary payments into the cash reserve up to a total £125m limit. This is so that the Scottish Government may accumulate a reserve in advance of new powers being devolved. From April 2015, the Scottish Government has been able to pay surplus tax receipts into the reserve.

58. The new Scotland Reserve will now enable the Scottish Government to smooth all types of spending and manage tax volatility and determine the timing of expenditure. The Scotland Reserve applies from 2017-18 onwards.

59. The Scotland Reserve will be separated between resource and capital. Payments may be made into the resource reserve from the resource budget including tax receipts. Funds in the resource reserve may be drawn down to fund resource or capital spending. Payments may be made into the capital reserve from the capital budget. Funds in the capital reserve may be drawn down to fund capital spending only.

60. The Scotland Reserve will replace the existing cash reserve. The Budget Exchange Mechanism will no longer apply to the Scottish Government's resource or capital budgets.

61. The Scotland Reserve will be capped in aggregate at £700m in 2023-24 prices (using the OBR's GDP deflator forecast at the time of the Scottish Government draft Budget), and therefore uprated annually. The Governments have agreed that annual drawdowns from the reserve will be unlimited. There are also no annual limits for payments into the Scotland Reserve.

62. The Scotland Reserve will be held within the UK government's Exchequer. The detailed arrangements for the operation of the Scotland reserve and access arrangements will be agreed between the Governments.

Fiscal scrutiny

63. Alongside the devolution of further powers to the Scottish Parliament, the Smith Commission recommended that the Scottish Parliament should expand and strengthen independent fiscal scrutiny of Scotland's public finances.

64. The Scottish Fiscal Commission was established on a non-statutory basis in 2014, with a remit to independently scrutinise and report on the Scottish Government's devolved tax revenue forecasts and projections of economic determinants underpinning forecasts of non-domestic rate income (NDRI).

65. In 2016 the Scottish Fiscal Commission Act was laid in the Scottish Parliament. The Act relates to the tax powers devolved to the Scottish Parliament under the Scotland Acts of 1998, 2012 and 2016.

66. To reflect additional devolved tax and spending powers devolved by the Scotland Act 2016 and the original fiscal framework the remit of the Scottish Fiscal Commission were expanded.

67. The future effectiveness of the Scottish Fiscal Commission and the OBR in scrutinising Scotland's devolved public finances and the operation of Scotland's

new fiscal framework will be dependent on close and constructive working between the two bodies.

68. In order to support these independent bodies in discharging their statutory functions, the Governments have agreed to introduce a reciprocal statutory duty of cooperation between the Scottish Fiscal Commission and the OBR. The practical working arrangements will be set out in a Memorandum of Understanding.

Forecasting

69. Forecasts of tax revenue and demand-led welfare expenditure in Scotland and the corresponding forecasts in the rest of the UK will be required to support the working of the fiscal framework (as the forecasts for the rest of the UK will be used to determine the block grant adjustment forecasts).

70. The Scottish Fiscal Commission will prepare independent forecasts of demand-driven welfare spending, revenues from the fully devolved taxes and income tax, and onshore GDP in Scotland. The founding legislation for the Scottish Fiscal Commission requires the Commission to prepare forecasts of fully devolved taxes and contains regulation making powers to enable the Commission to prepare forecasts of these other factors.

71. The OBR will continue to produce economic and fiscal forecasts for the whole of the UK, as well as all forecasts of UK government tax and spending required for the operation of the fiscal framework.

72. Arrangements for the production of forecasts of VAT revenues has been agreed by the JEC.

73. The UK and Scottish governments have agreed that appropriate and reciprocal information-sharing arrangements will be put in place to enable both governments (as well as the OBR and the Scottish Fiscal Commission) to undertake their respective responsibilities.

Welfare Benefits

74. The Governments have agreed that any new benefits or discretionary payments introduced by the Scottish Government must provide additional income for a recipient and not result in an automatic offsetting reduction by the UK government in their entitlement elsewhere in the UK benefits system. Any new benefits or discretionary payments introduced by the Scottish Government will not be deemed

to be income for tax purposes, unless topping up a benefit which is deemed taxable such as Carer’s Allowance.

75. The Governments have also agreed that the UK government’s Benefit Cap will be adjusted to accommodate any additional benefit payments introduced by the Scottish Government.

Crown Estate

76. In 2016, the Governments agreed that the Scottish Government will take on responsibility for managing the Crown Estate assets in Scotland.

77. The managers of Crown Estate assets in Scotland will continue to receive the same benefits as the Crown Estate Commissioners in terms of exemption from corporation tax, income tax, capital gains tax and other Treasury finance rules.

78. Responsibility for the Coastal Communities Fund was devolved to the Scottish Government in the 2016 agreement.

79. The Governments have agreed that a baseline deduction to the Scottish Government’s block grant will be set at a newly agreed incremental rate from 2024-25, which is not subject to indexation.

80. From 2024-25, the new baseline adjustment will be:

Year	2024-25	2025-26	2026-27	2027-28	2028-29 onwards
Baseline Adjustment	£10m	£10m	£15m	£20m	£40m

81. A baseline addition will be made for the funding of the Coastal Communities Fund equal to the UK government spending in the year immediately prior to devolution. This is subject to the normal operation of the Barnett formula.

82. The Scottish Government will also assume full responsibility for all associated liabilities relating to the Crown Estate assets in Scotland.

Governance

83. The Joint Exchequer Committee (JEC), operating by consensus, will govern the completion, implementation, operation and review of the fiscal framework. The JEC will also discuss any other issues arising which Ministers from either Government refer to the JEC.

Dispute Resolution

84. The dispute resolution mechanism set out below has the following scope:

- All disputes arising from the consideration of direct and behavioural spillover effects, including both gains and losses.
- It would also apply to the resolution of inter-administration disputes relating to the fiscal framework, including calculation of the block grant adjustment and other aspects of the fiscal framework, but excluding the review arrangements described in paragraphs 20 to 23 of this Agreement.
- It would not apply to any other issues of inter-governmental dispute or disputes between UK government and other devolved administrations and the MoU procedure would continue to apply in these cases.

85. If the difference of view cannot be settled at working level, it would become a disagreement and be referred to senior officials (at Director level or above), including consideration at Joint Exchequer Committee (Official) (JEC(O)). If no resolution can be reached, the matter becomes a formal dispute and would be referred to Ministers to be raised and discussed at a meeting of JEC.

86. If it becomes clear that there is a dispute that cannot be resolved between Ministers, there is an automatic pause placed on the disputed finances, i.e. no decisions or actions can be taken by either Government in relation to the disputed amount until the dispute is resolved.

87. Both Governments will draw up a statement of fact on the dispute. Technical input on the dispute may be sought from the OBR and the Scottish Fiscal Commission. The findings of any technical input and analysis will be published.

88. The statement of fact and the technical input from the OBR and Scottish Fiscal Commission will be considered by both governments, who commit to using their best endeavours to resolve the dispute.

89. If no agreement can be reached then the dispute falls – there would be no specific outcome from the dispute and so no fiscal transfer between the Governments.

90. If either Government wishes to pursue the dispute further it can be referred to the Dispute Avoidance and Resolution Process set out in the Review of Intergovernmental Relations[4]

Reporting

91. The Smith Commission recommended that both Governments provide updates to their respective parliaments, including through the laying of annual update reports [Paragraph 95 (9)]. These reports should set out the changes agreed to the Scottish Government's fiscal framework.

92. Section 33 of the Scotland Act 2012 makes provision for Scottish and UK Ministers to report on the implementation and operation of the finance powers/functions devolved under that Act. These reports are required to set out:

- action taken towards commencement of the provisions;
- an assessment of the operation of provisions which have commenced;
- an assessment of the operation of any other powers to devolve taxes or to change the powers of Scottish Ministers to borrow and any other changes affecting the finance provisions inserted or amended by the Act;
- the effect on payments into Scottish Consolidated Fund; and,
- any other matters concerning sources of revenue for the Scottish Administration which should be brought to the attention of both Parliaments.

93. Both Governments will separately prepare and publish a similar type of report for functions and duties being devolved under the Scotland Act 2016. These reports will also be provided to both the UK and Scottish Parliaments.

94. Any annual report provided to either Parliament would sit alongside and be complementary to existing scrutiny by both Parliaments, such as the legislative process, committee inquiries and questions to ministers. It is also open to both Parliaments to request updates from their respective Governments on the operation of the framework.

[4] Microsoft Word - The Review of Intergovernmental Relations - OFFSEN.docx (publishing.service.gov.uk)

Implementation and operation

95. The Governments have agreed that the Joint Exchequer Committee – Officials (JEC(O)) will see its remit expanded to include detailed implementation and operation of the financial provisions of any Scotland Act 2016. The remit of the JEC(O) will be expanded to cover the remit of the Intergovernmental Assurance Board established to oversee implementation and operation of the fiscal provisions of the Scotland Act 2012. JEC(O) will oversee, at official level, the delivery of the fiscal framework. Membership will also be expanded to include relevant interests from UK government departments and equivalent officials in the Scottish Government.

96. The Governments have agreed that there will be no in-year updates to the forecasts for income tax and VAT revenues, or the associated block grant adjustments. These forecasts will be used until they can be reconciled to outturn.

Review

97. In line with the Smith Commission recommendations, the fiscal framework as a whole will be reviewed periodically.

98. It will be open to either government to propose changes to the fiscal framework as part of future reviews. The Joint Exchequer Committee will jointly agree conclusions, recommendations and revisions of the review.

Completion

99. An annex to this agreement covering the operational and governance aspects of the fiscal framework will be updated and published as soon as possible. This annex will set out the detailed arrangements on the fiscal framework including the methodology and data sources for calculating the baseline adjustments and indexing the BGAs and arrangements for sharing information and data. The governance arrangements will cover bilateral engagement, official engagement, Memorandums of Understanding and audit. An updated Terms of Reference for the Joint Exchequer Committee will be set out along with updated terms of reference for Joint Exchequer Committee – Officials (JEC(O)).

ANNEX A: Smith Commission Principles for Scottish Government's Fiscal Framework

95 (1) Barnett Formula: the block grant from the UK government to Scotland will continue to be determined via the operation of the Barnett formula.

95 (2) Economic Responsibility: the revised funding framework should result in the devolved Scottish budget benefiting in full from policy decisions by the Scottish Government that increase revenues or reduce expenditure, and the devolved Scottish budget bearing the full costs of policy decisions that reduce revenues or increase expenditure.

95 (3) No detriment as a result of the decision to devolve further power: the Scottish and UK governments' budgets should be no larger or smaller simply as a result of the initial transfer of tax and/or spending powers, before considering how these are used.

(a) This means that the initial devolution and assignment of tax receipts should be accompanied by a reduction in the block grant equivalent to the revenue forgone by the UK government, and that future growth in the reduction to the block grant should be indexed appropriately.

(b) Likewise, the initial devolution of further spending powers should be accompanied by an increase in the block grant equivalent to the existing level of Scottish expenditure by the UK government, including any identified administrative savings arising to the UK government from no longer delivering the devolved activity, and a share of the associated implementation and running costs in the policy area being devolved, sufficient to support the functions being transferred, at the point of transfer.

95 (4) No detriment as a result of UK government or Scottish Government policy decisions post-devolution:

(a) Where either the UK or the Scottish Governments makes policy decisions that affect the tax receipts or expenditure of the other, the decision-making government will either reimburse the other if there is an additional cost, or receive a transfer from the other if there is a saving. There should be a shared understanding of the evidence to support any adjustments.

(b) Changes to taxes in the rest of the UK, for which responsibility in Scotland has been devolved, should only affect public spending in the rest of the UK. Changes to devolved taxes in Scotland should only affect public spending in Scotland.

95 (5) Borrowing powers: to reflect the additional economic risks, including volatility of tax revenues, that the Scottish Government will have to manage when further financial responsibilities are devolved, Scotland's fiscal framework should provide sufficient, additional borrowing powers to ensure budgetary stability and provide safeguards to smooth Scottish public spending in the event of economic shocks, consistent with a sustainable overall UK fiscal framework. The Scottish Government should also have sufficient borrowing powers to support capital investment, consistent with a sustainable overall UK fiscal framework. The Scottish and UK governments should consider the merits of undertaking such capital borrowing via a prudential borrowing regime consistent with a sustainable overall UK fiscal framework.

(a) The Scottish Government's borrowing powers should be agreed by the Scottish and UK governments, and their operation should be kept under review in conjunction with agreement on the mechanism to adjust the block grant to accommodate the transfer of taxation and spending powers.

(b) Borrowing powers should be set within an overall Scottish fiscal framework and subject to fiscal rules agreed by the Scottish and UK governments based on clear economic principles, supporting evidence and thorough assessment of the relevant economic situation.

95 (6) Implementable and Sustainable: once a revised funding framework has been agreed, its effective operation should not require frequent ongoing negotiation. However, the arrangements should be reviewed periodically to ensure that they continue to be seen as fair, transparent and effective.

95 (7) Independent Fiscal Scrutiny: the Scottish Parliament should seek to expand and strengthen the independent scrutiny of Scotland's public finances in recognition of the additional variability and uncertainty that further tax and spending devolution will introduce into the budgeting process.

95 (8) UK Economic Shocks: the UK government should continue to manage risks and economic shocks that affect the whole of the UK. The fiscal framework should therefore ensure that the UK government retains the levers to do that, and that the automatic stabilisers continue to work across the UK. The UK Parliament would continue to have reserved power to levy an additional UK-wide tax if it was in the UK national interest.

95 (9) Implementation: the Scottish and UK governments should jointly work via the Joint Exchequer Committee to agree a revised fiscal framework for Scotland based on the above principles. The two governments should provide updates to the Scottish and UK Parliaments, including through the laying of annual update reports, setting out the changes agreed to Scotland's fiscal framework.

ANNEX B: Revenue and Expenditure Covered by the Fiscal Framework

100. Following the recommendations of the Smith Commission a number of new tax and spending powers are being devolved to the Scottish Parliament in the current Scotland Bill.

Devolved and Assigned Tax Powers:

- The Scottish Parliament will be given the power to set rates and bands of non-saving non-dividend income tax.
- The first 10p in VAT receipts at the standard rate and the first 2.5p in VAT receipts at the reduced rate will be assigned to the Scottish Parliament.
- Air Passenger Duty and Aggregates Levy are to be fully devolved.

101. Under the Smith Commission Agreement the Scottish Government will also retain fines, forfeitures and fixed penalties imposed by courts and tribunals in Scotland, as well as sums recovered under Proceeds of Crime.

102. This document also covers fiscal arrangements for the tax powers devolved under the Scotland Act 2012; this covers the Scottish Rate of Income Tax, Stamp Duty Land Tax (now Land and Buildings Transaction Tax) and Landfill Tax (now Scottish Landfill Tax).

Welfare Powers:

103. Powers relating to benefits for carers, disabled people, and those who are ill are being devolved through the Scotland Bill. The Smith Agreement recognises this as referring to the following benefits: Attendance Allowance, Carer’s Allowance, Disability Living Allowance, Personal Independence Payment, Industrial Injuries Disablement Allowance, Severe Disablement Allowance, Cold Weather Payment, Funeral Payment, Sure Start Maternity Grant, Winter Fuel Payment and Discretionary Housing Payments. For the purposes of the fiscal framework these benefits are referred to as “devolved welfare”.

104. In addition the following powers will be devolved to the Scottish Parliament:

- Powers to vary housing cost elements of Universal Credit.
- Administrative powers to change payment arrangements for Universal Credit.

- Power to top-up reserved benefits.

- Power to create new benefits in areas other than pensions.

Spending Powers:

The fiscal framework also covers the arrangements for “devolved public services” under the Scotland Act 2016.[5]

105. In addition two key areas being devolved are the Crown Estate and the contracted employment programmes on expiry of the current commercial arrangements. These two areas have more complex funding arrangements and are, therefore, covered separately in the fiscal framework.

Administration and Implementation Cost

106. The fiscal framework also sets out the arrangements for administration and implementation costs.

[5] This covers the following spending powers: Equal opportunities, Tribunals, Roads, Policing of railways and railway property, British Transport Police, Onshore petroleum, Consumer advocacy and advice, Betting, gaming and lotteries, Broadcasting, Regulation of telecommunications and postal services, Commissioners of Northern Lighthouses, Maritime and Coastguard Agency, Rail, Fuel poverty, Energy market regulation and renewables, Competition policy, Election and franchise, EU, and Health and social affairs.

Annex C: Operation and Governance of the Scottish Government's Fiscal Framework

A.1. This annex forms part of the fiscal framework agreement between the UK government and the Scottish Government. It describes how the key elements of the framework will be implemented and will operate. This ensures that the effective operation of the fiscal framework should not require ongoing negotiation.

A.2. This annex sets out the arrangements for:

- Part 1 - initial baseline adjustments;
- Part 2 – indexation methodologies;
- Part 3 - process for calculating the resource block grant and tax revenues;
- Part 4 – resource borrowing;
- Part 5 – implementation and administration costs;
- Part 6 - memorandums of understanding;
- Part 7 - data and information sharing arrangements; and,
- Part 8 - governance arrangements.

A.3. Further annexes set out the terms of reference for the Joint Exchequer Committee (JEC) and the Joint Exchequer Committee (Officials) (JEC(O)).

Part 1: Initial Baseline Adjustments

A.4. An initial baseline adjustment will be made to the Scottish Government's Resource Block Grant for each of the functions and powers being devolved to the Scottish Parliament. For new spending powers this will be an addition to the Block Grant, whilst for new revenue raising powers this will be a deduction from the Block Grant.

A.5. These baseline adjustments will be separately calculated for each of the devolved taxes and devolved benefits in order to aid transparency in how the block grant adjustments are calculated.

Taxation

A.6. The two Governments have agreed that the initial baseline block grant adjustments will be equal to the UK government's receipts from the relevant tax generated from Scotland in the year immediately prior to the devolution of powers (year 0). The baseline year is therefore the year prior to devolution. As set out in Part 2, the indexation mechanisms will then be applied to determine the adjustments for year 1 onwards.

A.7. The detailed arrangements for calculating the baseline adjustment in year 0 are as follows[6]:

- Forecasts of the UK government's receipts in Scotland in year 0 will be produced for each tax during year 0 and used to apply a provisional baseline adjustment.[7]
- After the end of year 0, once outturn tax receipts are available, the provisional baseline block grant adjustments will be recalculated.
- To avoid multiple iterations of reconciliations, these calculations will be made at the same time as the reconciliation for year 1 receipts; see Part 3 for further information.

A.8. The table below reflects the agreed basis for baseline adjustments for tax.

Revenue source	Methodology for calculating baseline adjustment
Income tax	Total non-saving non-dividend income tax receipts in Scotland under UK government income tax policy in 2016-17. Initially this will be forecast and then reconciled against outturn once data is available.
Air passenger duty	An average of the GERS[8] and HMRC methodologies for apportioning UK Air Passenger Duty (APD) revenues to Scotland, applied to a forecast of UK-wide receipts in 2017-18. This forecast will be reconciled to outturn based on outturn UK receipts

[6] These arrangements don't apply to Stamp Duty Land Tax and Landfill Tax as 2014-15 (year 0) outturns are already known.
[7] The timing of which is set out at Part 3.
[8] Government Expenditure and Revenue Scotland (GERS) http://www.gov.scot/Topics/Statistics/Browse/Economy/GERS

	and based on the share estimated by the HMRC and GERS methodologies.
Aggregates levy	An average of the GERS and HMRC methodologies for apportioning UK Aggregates Levy (AL) revenues to Scotland, applied to a forecast of UK-wide receipts in the year immediately preceding devolution. This will be reconciled to outturn based on outturn UK receipts and based on the share estimated by the HMRC and GERS methodologies. The JEC will agree on a suitable point for the commencement for devolution of the aggregates levy and the baseline year once current state aid and other legal issues have been resolved.
Landfill tax	An average of the GERS and HMRC methodology for apportioning UK Landfill Tax revenues to Scotland will be applied to UK receipts in 2014-15. This agreement is without prejudice to the one-off block grant adjustment agreed in respect of Landfill Tax for 2015-16.
Stamp Duty Land Tax	Receipts in Scotland in 2014-15 will be used as published in HMRC statistics with a reduction to account for the £20m forestalling effects associated with residential tax receipts in 2014-15. This agreement is without prejudice to the one-off block grant adjustment agreed in respect of Stamp Duty Land Tax for 2015-16.
Assigned VAT	The methodology for apportioning VAT revenues to Scotland will be used to estimate receipts in the year immediately prior to assignment. This will be reconciled to outturn using the same methodology once the relevant data is available.
Revenues from courts and tribunals	Revenues from courts and tribunals in Scotland (including fines, forfeitures, fixed penalties and amounts recovered under Proceeds of Crime legislation) collected by the Scottish Government in 2016-17 will be used as the baseline deduction. This will initially use outturn data from the Scottish Consolidated Fund for the latest year available and updated to use the year prior to devolution once available.

Benefits Spending

A.9. The two Governments have agreed that the initial baseline block grant adjustments will generally be equal to the UK government's spending on the relevant benefit in Scotland in the year immediately prior to the devolution of powers (year 0). The baseline year is therefore the year prior to devolution. As set out in Part 2, the indexation mechanisms will then be applied to determine the adjustments for year 1 onwards.

A.10. The table below reflects the agreed basis for baseline adjustments for devolved benefits.

Devolved welfare element	Methodology for calculating baseline
Most benefits	The baseline addition will be the UK government's spending on each of the relevant benefits (i.e. those being devolved) in Scotland in the year immediately prior to the devolution of powers. This will initially be based on an OBR forecast and reconciled to outturn using DWP's statistics.
Cold Weather Payments	The baseline will be the average of the spending on the Cold Weather Payment in Scotland from 2008-09 to the year prior to devolution, reconciled to outturn, and based on DWP statistics.

A.11. The detailed arrangements for calculating the baseline adjustment in year 0 are as follows:

- Forecasts of the UK government's spending in Scotland in year 0 will be produced for each benefit during year 0 and used to apply a provisional baseline adjustment (as part of a multi-year average for the Cold Weather Payment).[9]
- After the end of year 0, once outturn spending is available, the provisional baseline block grant adjustments will be recalculated.

[9] The timing of which is set out at Part 3.

- To avoid multiple iterations of reconciliations, these calculations will be made at the same time as the reconciliation for year 1 spending; see Part 3 for further information.

Crown Estate

A.12. The baseline deduction to the Scottish Government's block grant will be set at a newly agreed incremental rate from 2024-25, and will not be subject to indexation.

A.13. From 2024-25, the new baseline adjustment will be:

2024-25	2025-26	2026-27	2027-28	2028-29 onwards
10	10	15	20	40

A.14. The baseline addition for the Coastal Communities Fund will equal the UK government spending in the year immediately prior to devolution. This baseline addition is subject to the normal operation of the Barnett formula.

Other Spending

A.15. For all DEL spending areas being devolved the normal approach to machinery of government changes will determine the initial baseline adjustments in respect of programme expenditure. Part 5 sets out the agreed baseline transfer for administration spending. The UK government will transfer planned spending in Scotland (including any planned employability funding through payment by results) for all remaining years of the Spending Review period, to which the Barnett Formula will subsequently apply. There will be no reconciliation to outturn.

Part 2: Indexation methodologies

A.16. This part sets out the agreement on how the indexation mechanisms will operate with reference to corresponding UK government receipts and benefit spending. This section also sets out the data required.

Taxation data

A.17. For revenues, “corresponding UK government receipts” are the revenues from the equivalent taxes or other revenue-raising powers collected by the UK government in the rest of the UK, specifically described in the table below. The scope of the UK government receipts will be updated with any devolution of tax powers to other parts of the UK. For example, when Stamp Duty Land Tax (SDLT) and landfill tax are devolved to the Welsh Assembly in April 2018, the change in UK government revenues between 2017-18 and 2018-19 will exclude SDLT and landfill tax receipts from Wales in both years.

Revenue source	Corresponding UK government receipts
Income tax	Non-savings, non-divided income tax receipts
Assigned VAT	VAT receipts from the first 10p of the standard VAT rate and the first 2.5p of the reduced VAT rate
Air passenger duty, aggregates levy, stamp duty land tax and landfill tax	Corresponding UK government receipts for each of the fully devolved taxes

Benefits spending data

A.18. For benefits, “corresponding UK government benefit spending” is the expenditure on the equivalent benefits by the UK government in England and Wales. The scope of the UK government spending will be updated with any devolution of welfare powers to other parts of the UK.

Population Statistics

A.19. Mid-year population estimates published by the Office of National Statistics (ONS) and National Records of Scotland (NRS) will be used for all calculations. The latest available mid-year estimates will initially be used to determine the provisional block grant adjustments (alongside forecasts of UK government tax receipts and benefit spending). As part of the wider process of reconciling from forecasts to outturn, the mid-year population estimates used initially will be replaced by those for the relevant years.

Tax and benefits indexation mechanisms

A.20. The Governments have agreed that the block grant adjustment for tax and benefits should be effected by using the Indexed Per Capita (IPC) method for tax and benefits.

A.21. Under the IPC model the initial block grant adjustment will be increased in line with the percentage growth in the equivalent UK government tax receipts per head or benefit spending per head, multiplied by Scottish population growth. In year t+1, the block grant adjustment is therefore calculated as:

$$BGA_{t+1} = \frac{X_{t+1}^{UKG}}{X_t^{UKG}} * \frac{\frac{P_{t+1}^{S}}{P_t^{S}}}{\frac{P_{t+1}^{UKG}}{P_t^{UKG}}} * BGA_t$$

where BGA denotes the block grant adjustment, t denotes the year, P denotes the population and X denotes either tax receipts or benefit expenditure, S denotes Scotland and UKG denotes UK government.

A.22. The block grant adjustments for tax and benefits for any year will be re-calculated and a final reconciliation carried out once outturn data in respect of relevant UK government tax receipts and benefit spending are known and when the relevant mid-year population estimates have been produced. Further details on this process are provided in Part 3 below.

Other spending areas

A.23. For all other areas of devolved spending not specifically mentioned in this annex, the Barnett Formula will apply. For the employment programmes, the Barnett formula will apply to changes in the entirety of UK government spending, including any elements funded through payment by results.

Part 3: Process for calculating the resource block grant and tax revenues

A.24. This section describes the process and timings for calculating the resource block grant alongside the Scottish Government's receipt of tax revenues.

A.25. The Scottish Government will be able to access the block grant and forecast of HMRC-collected tax revenues (income tax and VAT) as required during the year, while also receiving revenues from the fully devolved taxes as they are collected.

A.26. The Scottish Fiscal Commission will be responsible for preparation of independent forecasts of Scottish Government tax receipts and benefit expenditure, and Scottish onshore GDP. It is expected to assume this role in full for the financial year 2018-19 onwards, which means producing forecasts from summer 2017 (based on the current Scottish Government budget timetable). However, for the short period while the Scottish Fiscal Commission is preparing to assume responsibility for independent forecasts, the Scottish Government will produce the forecasts and the Scottish Fiscal Commission will provide independent scrutiny and assurance of the reasonableness of the forecasts.

Block Grant Calculation

A.27. As set out in the Smith Agreement, changes in the Scottish Government's block grant will continue to be determined via the operation of the Barnett Formula. Under the Barnett Formula, the Scottish Government's block grant in any given financial year is equal to the block grant baseline plus a population share of changes in UK government spending on areas that are devolved to the Scottish Parliament. This will continue to apply to changes in UK government spending on areas that are devolved to the Scottish Parliament at each UK government spending round and fiscal event when decisions are made to change UK government spending in these areas.

A.28. The Statement of Funding Policy[10] will continue to set out the detailed arrangements for the operation of the Barnett Formula.

Adjustments to the Block Grant

A.29. Adjustments to the block grant for tax and benefits will provisionally be based on a forecast of relevant UK government receipts and expenditure in the rest of the UK and the latest available mid-year population estimates, as outlined in paragraph C.18. The adjustments will be calculated separately for all relevant areas of expenditure and revenue to aid transparency, and will then be applied to the Scottish Government's Resource Block Grant for the relevant financial year.

[10] HM Treasury (October 2021) Statement of funding policy: funding the Scottish Government, Welsh Government and Northern Ireland Executive https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1137609/Statement_of_Funding_Policy_update_Feb_2023.pdf

A.30. The adjustments for the next financial year will be calculated by the UK government in line with the provisions of this annex at the Autumn Statement provided this occurs at least three months in advance of the start of the financial year.

A.31. Where the Scottish Government's Draft Budget occurs before the UK Autumn Statement, the UK government will additionally provide a provisional estimate of the adjustments for budgeting purposes based on the previous UK Budget forecasts, which will be revised at the Autumn Statement. If the Autumn Statement has not occurred at least three months in advance of the start of the financial year, then the provisional estimate of the adjustments calculated for budgeting purposes in the Scottish Government's Draft Budget will be applied to the block grant for the next financial year.

A.32. Following the financial year to which the adjustments relate, once outturn data is available on tax receipts and on benefit spending and for mid-year population estimates, the adjustments to the block grant will be recalculated using this outturn data and the results reconciled. Any difference compared to the original calculation will be applied to the block grant in respect of the following financial year, provided this information is available at least two months in advance of the Scottish Government's Draft Budget. In the event that this information is not available at least two months in advance of the Scottish Government's Draft Budget then the Scottish Government may determine whether the adjustment will apply in the following financial year or the second following financial year.

Timing of tax forecasts and reconciliations

A.33. The forecasts of Scottish Government tax receipts will be available for inclusion in the Scottish Government's budget each year, and in the case of VAT and income tax these will ultimately be reconciled to outturn. The forecasts of UK government tax receipts used to determine the block grant adjustments will also all be reconciled to outturn. However, the arrangements are slightly different for different types of devolution/assignment as set out below.

Income tax and VAT

A.34. For income tax, the forecast of revenues raised in Scotland will be available for the Scottish Government to draw down in the upcoming financial year.

A.35. Once outturn figures for income tax receipts are available the Scottish revenues and the block grant adjustment will be recalculated on the basis of this outturn data. In the case of income tax, outturn data will be available around 15 months after the end of the financial year. As there was a transition period for income tax, no reconciliation was applied to the forecast tax receipts or block grant adjustment for the Scottish rate of income tax in 2016/17. However outturn data for 2016/17 once available, was used to re-calculate the final baseline block grant adjustment, which was reconciled to the original baseline adjustment.

A.36. Following the reconciliation after the end of each financial year, any difference in Scottish tax receipts or block grant adjustment compared to the original calculations will be incorporated into the equivalent funding for the following financial year, provided this information is available at least two months in advance of the Scottish Government's Draft Budget. In the event that this information is not available at least two months in advance of the Scottish Government's Draft Budget then the Scottish Government may determine whether the adjustment will apply in the following financial year or the second following financial year.

A.37. There will be no in-year updates to either the Scottish income tax and VAT forecasts or the associated block grant adjustments.

A.38. Arrangements for the production of VAT revenue forecasts and the process for reconciling forecasts to outturn will be agreed by JEC once further work on the assignment methodology has been completed.

Fully devolved taxes

A.39. The taxes in question are air passenger duty, the aggregates levy, stamp duty land tax and landfill tax. The same approach will also be taken for revenues from courts/tribunals, except without in-year updates.

A.40. The Scottish Government will use receipts as they are collected during the year to fund spending. The block grant adjustment will therefore also be updated during the year to reflect latest forecasts of corresponding tax receipts in the rest of the UK. This will ensure that the Scottish Government is shielded from UK-wide in-year shocks (affecting receipts positively or negatively). In-year updates to the block grant adjustments will occur at the in-year Autumn Statement and will be applied in Supplementary Estimates. Updates to the block grant adjustments will also be made once outturn data is available after the end of the financial year.

A.41. In-year updates to the block grant adjustments to reflect latest forecasts of corresponding tax receipts in the rest of the UK may result from economic impacts or policy changes introduced by the UK government. Any in-year policy changes to fully devolved taxes in the rest of the UK introduced by the UK government after the Scottish

Government’s Budget will not automatically result in an in-year adjustment to the Block Grant. The Scottish Government may determine whether any adjustment that is due will be made in-year to the Block Grant or whether this will be incorporated at the final reconciliation when outturn data is available. The effect of the tax policy change on tax receipts in the remainder of the UK will be included in forecasts used to calculate the block grant adjustment for subsequent years. The Scottish Government will have the power to borrow within the agreed limits in response to a net forecast error between Scottish receipts and the adjustments to the Block Grant (which depend on forecasts of UK government receipts).

A.42. Once outturn figures are available for UK government receipts from the fully devolved taxes, the block grant adjustment will be recalculated and reconciled to the original calculation.

Benefits

A.43. The timing for benefit related adjustments to the block grant will operate in a similar way to that for fully devolved taxes.

A.44. The adjustments will therefore be calculated on the basis of forecasts at each spending round and fiscal event at which a forecast for UK government benefit spending is produced. Forecasts of UK government benefit spending in England and Wales will be produced by the OBR and the block grant adjustment calculated on this basis. Once outturn data is available the block grant adjustments will be recalculated, and reconciled to the original calculation.

A.45. As the Scottish Government makes benefit payments during the year, where UK government in-year spending diverges from forecast the block grant adjustments will be updated during the year. These updates will take place at the in-year Autumn Statement and applied at Supplementary Estimates.

A.46. In-year updates will not automatically apply to any policy changes introduced by the UK government after the Scottish Government’s Budget. The Scottish Government may determine whether the adjustment will be made in-year to the Block Grant or whether this will be incorporated within the end-year reconciliation (and the policy change will also be included within forecasts for subsequent years).

Future revisions to operational arrangements

A.47. To ensure the continued smooth operation of the fiscal framework, the operational and governance arrangements for the fiscal framework shall be reviewed as part of the periodic reviews into the fiscal framework.

A.48. These arrangements are based on the current Parliamentary budget timetables in the UK and in Scotland (the latter agreed between the Scottish Government and the Scottish Parliament). Should there be substantial changes to this timetabling arrangement then the timings set out in these arrangements shall be reviewed to ensure that they are still appropriate.

Part 5: Implementation and administration costs

A.49. There will be one-off and ongoing costs to both governments associated with changing or implementing systems (one-off implementation costs), and administering the new arrangements (ongoing administration costs).

A.50. The general approach is that the UK government will make a fixed transfer to the Scottish Government; the Scottish Government is then responsible for all implementation and administration costs (including all jointly agreed net additional UK government costs where these are wholly and necessarily incurred as a result of implementing or operating devolved powers). The one exception to this general approach is that the governments have agreed that any costs associated with the design, implementation and ongoing administration of VAT assignment will be split equally.

A.51. The governments have agreed that the UK government will transfer to the Scottish Government a one-off non-baselined amount of £200m as a contribution towards implementation costs borne by the Scottish Government. A profile of this funding will be agreed by both governments at a future JEC.

A.52. The governments have agreed that the UK government will make a baseline transfer of £66m to the Scottish Government as a contribution towards ongoing administration costs borne by the Scottish Government. The JEC will agree the date of transfer. The comparability factors within the Barnett Formula for areas of spending devolved to the Scottish Parliament will be updated from the point of devolution so that the Scottish Government will receive a population share of planned changes in UK government spending on administration in these areas (as well as a population share of planned changes in UK government programme spending in these areas).

Part 6: Memorandums of Understanding

A.53. To support the effective implementation and operation of the fiscal framework, Memorandums of Understanding (MoUs) will be required between the bodies that will perform the duties that are outlined in this agreement.

A.54. The following MoUs will be agreed for the implementation of the Scotland Act and the ongoing administration of the fiscal framework. Together with other agreements not listed here (those in non-fiscal areas for example), these will set out the arrangements for implementing and operating this fiscal framework.

- Between the UK government and the Scottish Fiscal Commission to enable information sharing requirements covered by the fiscal framework agreement.
- Between the OBR and the Scottish Government to ensure implementation of the Scotland Act 2016 provision on information sharing requirements in this arrangement.
- Between the OBR and the Scottish Fiscal Commission to support these independent bodies in discharging their statutory functions.
- Between Revenue Scotland and HMRC – this is likely to be an extension of the current MoU on compliance and any other relevant areas.
- Between the Scottish Government and the DWP to support the delivery of benefits in Scotland (noting that many such MoUs exist already).
- Between the DWP and any future administrative organisation or delivery partner for the administration of social security in Scotland to support the delivery of benefits in Scotland.
- Between the Scottish Government and UK government to facilitate the introduction and operation of new tax and devolved benefits, which would cover the information and data sharing arrangements set out in Part 7.

A.55. The Memorandums of Understanding will be agreed by the relevant parties and made available to both Parliaments as soon as they are agreed. These MoUs will also be provided as part of the annual implementation reports produced by both governments.

Part 7: Data and Information Sharing Arrangements

A.56. Both governments and both independent forecasters (the OBR and the Scottish Fiscal Commission) will require access to information and data that will enable Ministers, officials, appointed commissioners and office holders to the OBR to discharge their duties in respect of Parliamentary accountability, scrutiny, policy development and forecasting.

A.57. Both governments have the agreed objective to provide each other with as full and open as possible access to technical, operational and policy information including statistics and research and, where appropriate, representations from third parties. These exchanges between administrations may be subject to restrictions or requirements, including statutory and commercial constraints on disclosure of information and confidentiality.

A.58. Each government will ensure that the information it supplies to others is subject to appropriate safeguards in order to avoid prejudicing its interests. Each government will treat shared information with appropriate discretion.

A.59. The Scottish Government and Scottish Fiscal Commission will work with the UK government to explore options to ensure that appropriate provision can be made for the Scottish Government and Scottish Fiscal Commission to have access to the necessary data, information and models held by the UK government to support policy development and produce forecasts of a comparable quality to those produced by the OBR.

A.60. The arrangements set out below do not preclude the supply of additional data and facilities that may be agreed between the UK and Scottish Governments from time to time. Any requests for the regular supply of additional data agreed shall be incorporated into the Memorandums of Understanding.

A.61. There should be ongoing engagement between UK government officials and Scottish Government officials and the Scottish Fiscal Commission over development and peer support around forecasting of tax receipts and devolved benefit expenditure.

Income tax

A.62. The Scottish Government and the Scottish Fiscal Commission will require access to information, data and models that includes, but is not limited to, income tax data and models to forecast income tax receipts, which must be provided in sufficient time to support production of income tax forecasts in advance of the Scottish Government’s Draft Budget. This will initially be provided via the Public Use Tape income tax data set but the Scottish Government, the Scottish Fiscal Commission and HMRC will explore options to provide access to the income tax data at a level of detail to support policy development and ensure forecasts to underpin the Scottish Government's Budget are of a comparable quality to those forecasts produced by the OBR.

A.63. The UK government and OBR will require access to information and data including, but not limited to, five-year forecasts of Scottish Government income tax receipts alongside the Scottish Government's draft Budget and Budget.

Devolved taxes

A.64. The Scottish Government and the Scottish Fiscal Commission will require access to information and data held by HMRC and, where applicable, held by other bodies/organisations, for example the Civil Aviation Authority in the case of APD. In addition the Scottish Government and the Scottish Fiscal Commission will require access to historical time series data for the devolved taxes to enhance forecasting and scrutiny capabilities. This information must be provided in a timely manner to support policy development prior to devolution and forecasting.

A.65. The Scottish Government and the Scottish Fiscal Commission will also require access to the HMRC methodology and models for estimating the Scottish share of APD and AL receipts and forecasting UK receipts.

A.66. The UK government and OBR will require access to information and data including, but not limited to, five-year forecasts of Scottish Government devolved tax receipts alongside the Scottish Government's draft Budget and Budget (including forecasts of business rates revenues). As part of the reciprocal access to data and information, HMRC will also require access to information about the devolved taxes in order to undertake wider compliance activities (analogous to the arrangements already in place in relation to Land and Buildings Transaction Tax and Scottish landfill tax).

VAT

A.67. Arrangements for forecasting VAT revenues will be agreed at the Joint Exchequer Committee. The data set out below may be used to forecast revenues and to estimate the assigned VAT revenues, so will need to be shared with the Scottish Government and Scottish Fiscal Commission:

- Data to estimate expenditure by households, including but not limited to administrative data on spending and household survey data;

- Data to estimate VAT raised from the public sector, including but not limited to government spending data from PESA;
- Data to estimate VAT raised from the exempt sector, including but not limited to UK Supply-Use Tables;
- Data to estimate VAT raised from tourism expenditure;
- Forecasts of UK VAT revenues; and,
- In addition the Scottish Government and Scottish Fiscal Commission would require access to HMRC's models used for estimating and forecasting VAT arising in Scotland.

A.68. This information must be provided in a timely manner to support budgeting timetables.

GDP

A.69. While forecasts of tax receipts and demand-driven welfare spending will require economic determinants, these are not covered by the arrangements in the fiscal framework and will be determined by the relevant forecasting body.

Devolved Benefits

A.70. In order for the Scottish Fiscal Commission to produce independent forecasts of tax and benefits, the Scottish Government and Scottish Fiscal Commission will require access to historical time series expenditure and caseload data for each benefit operating in Scotland and the associated processing costs where this is not publically available, as well as tools used by DWP to forecast future caseload and expenditure levels for the benefits being devolved.

A.71. Prior to devolution the Scottish Government will require access to case level data for all devolved benefits, where available. This information must be provided in a timely manner to support policy development prior to devolution and forecasting.

A.72. Correspondingly, DWP will require access to timely, reliable and detailed case level data, where and when available, on benefits which have been devolved, so they can continue to support production of the OBR forecasts and administer benefits which have links to devolved expenditure.

A.73. Arrangements for accessing data and information regarding reserved benefits where these have interactions with the benefits being devolved should be discussed further by DWP and the Scottish Government.

Employability

A.74. The Scottish Government and, if appropriate, the Scottish Fiscal Commission will require access to historical time series expenditure and caseload data for the current employability programme operating in Scotland and the associated processing costs where this is not publically available, as well as tools used by DWP to forecast future caseload and expenditure levels for estimating claimant flows into the devolved employability services. All data requests must be proportionate and respect commercial confidentiality and ongoing data sharing arrangements.

A.75. Prior to devolution the Scottish Government will also require access to timely, reliable and detailed case level data on reserved benefits for those benefits linked to the devolved employability services so they can continue to forecast and administer the devolved employability services. Subject to putting in place any necessary additional data sharing agreements, including legal agreements, this information must be provided in a timely manner to support policy development prior to devolution and forecasting. This requirement will continue post devolution.

Block grant adjustment calculations

A.76. The Scottish Government requires access to information and data in relation to all the areas of the operation of the block grant adjustment mechanisms. The UK government already shares the data and calculations that are used to determine the Scottish Government's block grant; this will be extended to cover further tax and benefits devolution. In particular, this will set out how OBR forecasts of UK government tax revenues and benefit spending are used within the agreed funding arrangements.

Budgeting information

A.77. The UK and Scottish governments will agree updated budgeting arrangements that reflect the Scottish Government's new settlement. This will cover how the Scottish Government records its spending and the associated funding (from block grant, taxation, borrowing and the Scotland reserve). The UK government, OBR and ONS will require the Scottish Government to provide a range of information about actual, planned and forecast funding and spending. This includes:

- Planned capital borrowing for the Spending Review period, updated in advance of each financial year
- Planned drawdown of funds from the Scotland reserve in advance of each financial year
- Monthly in-year funding/spending data
- Five-year forecasts for tax revenues and demand-driven benefit spending

Part 8: Governance

Bilateral engagement

A.78. The Joint Exchequer Committee (JEC), operating by consensus, will govern the completion, implementation, operation and review of the fiscal framework. The JEC may also discuss any other issues arising which Ministers from either Government refer to the JEC.

A.79. JEC will have oversight of the implementation of the fiscal arrangements associated with the welfare benefits being devolved, including the transfer of funding into the Scottish Government's block grant baseline and indexation thereafter, forecasting and reconciliation process, and other financial and fiscal issues associated with this framework. The Joint Ministerial Working Group on Welfare will have responsibility for the policy and legislative aspects of devolution of this function.

A.80. The Governments agreed the Terms of Reference for JEC set out in Annex D.

A.81. The Governments have agreed that the remit of the Joint Exchequer Committee – Officials (JEC(O)) will be expanded to include detailed implementation and operation of the financial provisions of any Scotland Act 2016. The remit of the JEC(O) will be expanded to cover the remit of the Intergovernmental Assurance Board established to oversee implementation and operation of the fiscal provisions of the Scotland Act 2012. JEC(O) will oversee, at official level, the delivery of the fiscal framework. Membership will also be expanded to include relevant interests from UK government departments and equivalent officials in the Scottish Government. The Terms of Reference for JEC (O) are at Annex E.

A.82. JEC(O) may wish to consider establishing sub-project boards for specific issues or areas of devolution, such as VAT. These would report to JEC(O) and seek its agreement in making decisions. JEC(O) will also consider and agree MoUs or other such agreements required to support implementation of the framework and the Scotland Act.

Accountability to Parliaments

A.83. Accountability and credibility to both Parliaments is an essential part of this Framework. Both governments expect and welcome detailed scrutiny of the Fiscal Framework in both Parliaments.

A.84. Both Governments agree that there should be accountability of delivery bodies in both jurisdictions to elected representatives. The lines of accountability should be clear and easily understood. Where a body operates in either the UK or Scotland but not both it should be accountable to that Parliament – for example a body set up to distribute benefits in Scotland only should be responsible to the Scottish Parliament. Where a body delivers in both jurisdictions this accountability will be more complex. In these cases both governments agree to make clear how those bodies are accountable - in welfare, this should be through the Joint Ministerial Working Group on Welfare.

Review

A.85. The Smith Commission recommended that the fiscal framework should be reviewed periodically.

A.86. Subsequent reviews should take place on a 5 yearly basis but not more than once in any UK or Scottish electoral cycle. The timing will be agreed between the Scottish and UK Governments at the JEC.

A.87. The exact scope of the review is to be determined by the JEC at least 3 months before the review is to start. Issues to consider under the review could include operation of the fiscal framework including the BGA and indexation methods, no detriment and spillovers, borrowing limits and, if used, operation of dispute resolution procedures. As part of the review input should be sought from the OBR, the Scottish Fiscal Commission, stakeholders and academics but not be limited to these parties. Parliamentary Committees in the Scottish and UK Parliaments are actively encouraged to give evidence to the review.

Role of independent forecasters

A.88. The main duty of the OBR, which it performs independently, is to examine and report on the sustainability of the UK public finances. This includes producing biannual economic and fiscal forecasts for the whole of the UK. This duty is unaffected by the fiscal framework agreement.

A.89. However, some of the OBR's duties may be affected by the Scotland Bill and associated fiscal framework agreement. The UK government will discuss and agree any areas where the OBR believes that its duties (or how it must perform its duties) are significantly altered.

A.90. In particular, the OBR will need to take into account the Scottish Government's increased fiscal powers within its UK-wide forecasts, while ensuring that UK government tax and spending can be separately identified (to inform forecasts of block grant adjustments).

A.91. The UK and Scottish Governments may also make use of information published by the OBR to operate other areas of the framework. In addition, technical input on the impact of policy spillover effects or on disputes may be sought from the OBR and the Scottish Fiscal Commission. The process for seeking such input will be set out in the relevant MoU. Where input is sought that is beyond the statutory remit of the OBR or the Scottish Fiscal Commission, it will be for the OBR or the Commission, as relevant, to determine its response.

Audit

A.92. In line with the Smith recommendations for strengthening intergovernmental relations, both Governments have agreed to put in place a set of robust auditing arrangements with respect to the operation of this fiscal framework and the Scotland Act 2016. These arrangements should be efficient and effective. They should ensure that duplication is avoided as far as possible and that auditors are not overburdened by new responsibilities once the Smith provisions are fully implemented.

A.93. JEC should agree detailed arrangements based on these provisions.

Annex D: Joint Exchequer Committee (Scotland) – Terms of Reference (2015)

1. The Scottish and United Kingdom Governments established a Joint Exchequer Committee (JEC) in 2011 in the context of the Scotland Act 2012. These Terms of Reference reflect the Smith Commission Agreement and its proceeding implementation in the Scotland Act 2016 and Fiscal Framework.

Purpose

2. The JEC is the intergovernmental ministerial forum to discuss financial and fiscal matters relating to the Scotland Act 2016 and accompanying Fiscal Framework.

3. The JEC will discuss implementation of the relevant aspects of the Scotland Act 2016 and Fiscal Framework. The JEC may also discuss any other issues arising which Ministers from either Government refer to the JEC

4. The JEC will continue discussions on final implementation of the Scotland Act 2012.

5. The JEC will oversee and provide assurance to individual projects tasked with implementing individual elements.

Remit

6. The JEC will consider evidence and options and where appropriate make decisions in the following areas:

   a. Issues where the Scottish and UK Governments need to reach agreement in order to implement specific elements of the Fiscal Framework or the Scotland Acts 2012 and 2016.

   b. The process agreed by Ministers to address "spill over effects" as in paragraphs 44-53 of the Fiscal Framework agreement.

   c. The timetable for implementation of the Fiscal Framework and tax elements of the Scotland Acts 2012 and 2016.

   d. The fiscal issues associated with the implementation of the welfare elements of the Scotland Act 2016.

   e. How best to share data and information between the Scottish and UK Governments to assist implementation and any agreements needed between the two Governments to do this.

   f. Oversight of borrowing powers set out in the Scotland Acts 2012 and 2016 and agreed under the Fiscal Framework.

g. Oversight of additional budgetary flexibilities agreed under the Fiscal Framework.

h. Determining how delivery bodies are accountable to the relevant parliaments.

i. Proposals under Clause 28 of the Scotland Act 2012 to create additional devolved taxes.

j. Auditing arrangements with respect to the operation of this fiscal framework and the Scotland Act 2016.

k. The process, scope, terms of reference and implications when reviewing the Fiscal Framework.

l. Other bilateral financial and fiscal issues between the two Governments that require discussion.

Membership and Meetings

7. The JEC will be made up of Ministers from the UK and Scottish Governments. Ordinarily, these would be the Cabinet Secretary for Finance in the Scottish Government and relevant Ministers from the (UK) HM Treasury (currently the Chief Secretary and Financial Secretary). Officials may attend the JEC with and with consent of their respective Minister.

8. The JEC will be supported by an Officials Group made up of an equal number of officials from the Scottish and UK Governments. The JEC may decide to establish other groups to support it, as it sees necessary.

9. The JEC will meet at least twice a year. The JEC may decide to meet more often, especially in the first years of implementation. The JEC can decide to meet only one or not at all in a given year, but only by written agreement between the parties.

10. The Chair of the meeting should alternate between Ministers from the UK and Scottish Governments, starting with the Scottish Government Minister.

11. The agenda for each meeting is to be agreed between Scottish and UK Government officials prior to the meeting. Ordinarily, the agenda will be agreed and circulated with any papers no more than 3 working days prior to the meeting.

12. Minutes will be written of each meeting, ordinarily by officials from the Government of the Minister chairing the meeting.

13. The meeting will ordinarily take place at a location selected by the Chair. The JEC is able to decide to meet virtually (for example by video-conference or online) where appropriate.

14. All efforts will be made to reduce the cost and environmental impact of JEC meetings, to both Governments.

Decision making

15. Decisions are to be reached jointly by Ministers of both Governments. A decision of the JEC is one which has been agreed by both Government Ministers. Decisions on issues described in these Terms of Reference as falling within the scope of the JEC may not be taken by any other mechanism than the JEC, nor taken forward without the agreement of both the Scottish and UK Governments.

Transparency

16. After each JEC meeting, a Communiqué will be agreed by both Ministers. This will be published online on both Governments' websites and made available to both the UK and Scottish Parliaments.

17. These Terms of Reference will be published online.

18. The discussions at each meeting, the agenda, the minutes and any papers are to be confidential to the UK and Scottish Governments, unless the JEC specifically decides otherwise. Each Government will respect this confidentiality.

Dispute Resolution

19. All efforts will be made to reach agreement at the JEC. Where a dispute arises the dispute resolution procedure set out in the fiscal framework will be used.

20. Prior to referring any matter for consideration under the dispute resolution procedures, every effort will have been made to achieve early and bilateral resolution.

Review

21. These Terms of Reference can be amended, re-written or supplemented as agreed by JEC members.

Annex E: Joint Exchequer Committee (Officials)

Remit

The remit of the JEC(O) will be:

- To support JEC discussions by considering issues and agenda items in advance in order to agree an agenda and identify decisions required;
- Where tasked to do so, take forward consideration of issues with the aim of developing a shared position for subsequent Ministerial agreement at a subsequent JEC meeting;
- to approve, oversee and review a joint implementation programme of agreed key milestones and activities to implement this framework and powers and functions devolved under the Scotland Act 2016;
- to take a joint approach to quality assurance of the implementation process and to agree and review how progress towards these milestones should be driven and measured;
- to ensure that adequate resources are made available in each administration to drive forward necessary progress;
- to identify risks to implementation and oversee appropriate mitigating actions;
- to identify, and resolve, any concerns about the implementation process;
- to report to JEC on key assurance activities;
- to anticipate, and seek to resolve at an early stage, any arising disputes and if required escalate using the dispute resolution procedures agreed as part of the fiscal framework.

Membership

The membership of JEC(O) would be agreed by officials from both the UK and Scottish Governments. We would intend that it included:

Scottish Government

Scottish Exchequer	DG Scottish Exchequer

	Deputy Director: Fiscal Policy and Constitution
	[Policy Team Leaders]
Social Security	Deputy Director

UK government

HM Treasury	Director of Public Services
	Deputy Director: Devolution
	[Policy Team Leaders]
HMRC	Deputy Director: Devolution
DWP	Director: Devolution

Members may nominate deputies to attend on their behalf in the event that they are unable to attend meetings. Members may also nominate supplementary attendees where specific issues are to be discussed that require specialist knowledge.

Members of JEC(O) will retain responsibility for the areas of implementation that fall within the competence of their administration. As members of JEC(O), however, they will engage to seek to find solutions and resolve difficulties collectively.

Chairing

The group will be chaired by DG Finance at the Scottish Government and the Director of Public Services at HM Treasury on an alternating basis.

Secretariat

The Secretariat would be provided by the JEC Secretariat.

Frequency of meetings

It is envisaged that JEC(O) would meet at least two weeks in advance of JEC meetings or on a bi-annual basis if no JEC meetings are scheduled. The frequency of meetings may be reviewed in line with business need.

Progress reporting and quality assurance

It is anticipated that JEC(O), at each meeting, will review progress against the agreed milestones. Where a need for change or a likely delay is identified, the group will receive an interim exception report.

Members of JEC(O) will expect to be notified of any arising disputes together with efforts being made to resolve these disputes, at the earliest possible stage. In the event of failure to resolve the issue locally, the dispute resolution procedure set out in the fiscal framework will be followed.

HM Treasury contacts
This document can be downloaded from www.gov.uk
If you require this information in an alternative format or have general enquiries about HM Treasury and its work, contact:
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