Dear Susan

THE 2005-06 AUTUMN BUDGET REVISION (ABR)

1. At the Finance Committee meeting on 10 January, we undertook to provide you with further information in writing on a number of points. I will deal with these in the order they were raised.

Strategic Waste Fund and Flood & Coast Protection (budget adjustments)

2. Dr Murray asked the reasons for the adjustments to Strategic Waste Fund and Flood and Coast Protection budgets.

3. The original Strategic Waste Fund budget for 2005-06 was £111.53 million. Following value for money assessments of applications for funding from all 32 local authorities, some £102 million for 2005-06 was allocated from the Strategic Waste Fund budget. That left £9 million unallocated this year.

4. Due to capital slippage resulting from delays in construction and upgrade of recycling centres, the entire £102 million will not be claimed in this financial year. Therefore, at the Autumn Budget Revision £25 million was transferred to Central Unallocated Provision for later use and £4.93 million was transferred to be paid through the GAE funding mechanism (total adjustment of -£29.93 million).

5. The Flood Prevention grant scheme is entirely demand led, and is dependent upon local authorities coming forward with suitable schemes that meet the Executive’s criteria for funding. Although many local authorities are in the process of developing their flood prevention programmes, there have been very few applications for funding in this financial year. At least two large flood prevention schemes that we had budgeted for in 2005-06, namely the Braid Burn in Edinburgh and the Dunfermline scheme, will not now get underway until financial year 2006-07. We have, therefore, placed money in the CUP in order to ensure that funding for these, and other local authority schemes, is available when needed.
Strategic Waste Fund (processing applications)

6. Mr Swinney expressed concern that there may be delays in processing applications, which could lead to fines for not reaching the requisite levels of recycling.

7. All 32 local authorities have received phase 1 funding (kerbside recyclate collection etc) with the last letter of award being made to Highland Council in September 2004. This is the funding currently being distributed to councils (i.e. the £81.6 million for 2005-06).

8. Over and above this we have requested that authorities submit bids in the form of Strategic Outline Cases by the end of January 2006. These will detail the waste treatment infrastructure that needs to be put in place to divert additional municipal waste from landfill. As at 16 January none of these Strategic Outline Cases has been received.

9. The guidance on the strategic outline cases can be found at the website http://www.scotland.gov.uk/Publications/2005/07/2690741/07425 which indicates that the Executive expected to have made decisions by Autumn/Winter 2006. The expectation now is that the process will be completed sooner.

Water Services Budget (private water supplies)

10. Mr Arbuckle asked about the reduction in the water services budget in relation to private water supplies.

11. The allocation for Private Water Supplies was reduced at Autumn Budget Revision, and will be further reduced in the Spring Budget Revision, because the Private Water Supplies Regulations and associated Grant Regulations to enable payments to be made are not yet in place. This has occurred as a result of greater than anticipated complexities in setting the Private Water Supplies regulations and because of additional time being allocated, to ensure proper consideration was given to the substantial consultation response received in summer 2005.

12. Both sets of Regulations are expected to be laid before Parliament by 31 March 2006 and expenditure can be expected after they come into force. Prior to that date expenditure is being incurred on information and education material for those dependent on private supplies and in the preparation of a technical manual for local authorities - both are key elements of our policy to improve private water supplies.

Environment & Rural Affairs Budget Management (Agencies & NDPBs)

13. The Convener, Mr McNulty, noted that more money was being spent on some ERAD lines, and less on others and questioned the management of budgets.

14. The re-deployment of in year savings in the ERAD budget is a sign of good budget management. If, having set an original budget for any particular spending, we find, as the year progresses, that demand for actual spending in some areas is lower than planned, it is no more than common sense that we should use such savings to offset the costs of pressures elsewhere.

15. While there are increases proposed for the Scottish Agricultural and Biological Research Institutes and Royal Botanic Garden, totalling just over £4m, these increases in the Science element of the budget are offset by a saving of £2.260m in demand under the Flexible Fund for Research Development. The net increase in this area of spending is then largely attributable to a one off increase agreed this year to allow additional scientific equipment purchases.
16. The increase for the Scottish Fisheries Protection Agency is to cover additional enforcement activity required in the light of the infraction proceedings taken against the UK by the EC Commission which asserts that we are not doing enough to protect fish stocks.

17. The increase for Scottish National Heritage (SNH) is mainly to cover additional, one off costs of relocation which were not built into the SNH SR 2004 baseline and were always planned to be met by use of other savings. The increase for National Parks reflects a shortfall in the previous baseline for the spending, up to 2005-06, which has been managed by an in-year increase, using savings from elsewhere on the budget but for which baseline provision is made from 2006-07.

Fisheries Capital Grants (budget reduction)

18. Mr Ballard asked about the reduction in the Fisheries Capital Grants budget. This simply reflects latest estimates of likely 2005-06 expenditure under the demand-determined EU Financial Instrument for Fisheries Guidance (FIFG) and the related Back-up Grants Schemes.

NHS & Teachers’ Pensions (budget increase)

19. Several members of the Committee asked about the £509m increase in provision for pensions through the ABR. This was required for two main reasons:

19.1 The UK Government’s decision to change the discount factor. This accounts for around £300m of the total ABR increase; and

19.2 The revaluation of NHS liabilities in the 2004-05 Pension Scheme Statements made necessary by an actuarial error in a previous scheme valuation. This accounts for £200m of the ABR increase.

20. The balance of the increase in provision is required because of amended forecasts to income streams. This is not uncommon and it is because of the volatility of income and expenditure that pension scheme are resourced as Annually Managed Expenditure (AME) and not part of the Departmental Expenditure Limit (DEL). The £509m is entirely non-cash expenditure and has no cash impact in 2005-06.

UK Government decision to reduce the discount factor

20.1 From 1 April 2005, the UK Government reduced the discount factor used to calculate interest from 3.5% to 2.8%. This applied to all unfunded public sector pension schemes in the UK covering the civil service, health, teaching and the armed forces. Whilst the total pension scheme liabilities in the balance sheet are unaffected by this change, it means that more resources have to be put through the accounts each year in order to compensate for the lower rate of return. In other words, paying the same liability over the same period of time at a lower rate of interest requires more annual expenditure.

20.2 The ABR was the first window for this resource to be requested following the announcement of the change in policy. This is recorded in the scheme statements under the heading ‘current service cost’. It is non-cash expenditure, there is no cash draw down and, subsequently, no impact on the net cash.
Actuarial Error

20.3 When the Government Actuary Department (GAD) completed an updated scheme valuation for the NHS pension scheme in 2005, they identified an error in the estimation of past service in their previous valuation of scheme liabilities as at 31 March 1999, carried out in August 2000. The impact of this error was to undervalue the scheme liabilities and a compensating adjustment was therefore necessary.

20.4 The scheme statements for 2004-05 redressed this error by restating the actual liabilities of the scheme. Because there is a higher opening liability at 1 April 2005, there is a higher notional interest charge required for 2005-06. The ABR was the first window for this resource to be requested.

20.5 We can confirm that this is the result of a one-off error and that the Government Actuary Department agreed to revise its checking procedures to ensure that such errors do not occur again. There is no impact on other pension schemes.

Scottish Water (Water Industry Commission budget)

21. Mr Mather asked about the increase to the Water Industry Commission budget. The £2.1 million increase represents a sum of three grants:

21.1 £0.3m for reporters who provide an independent check of the costs incurred by Scottish Water in the delivery of the capital programme. From 1 April 2006, these costs will be funded from charges;

21.2 £1.7m for the set up of retail licensing. From 1 April 2008 the Water Industry Commission will be responsible for issuing retail licenses to successful applicants. Scottish Water, however, is required to apply for a licence prior to this date. This figure was an estimate and will be reduced to £1.4m in the Spring Budget Revision; and

21.3 £0.1m for a one-off grant to assist with the costs of the Strategic Review of Charges.

Transitional Reduction Scheme (definition)

22. The Convener asked about the £7m for the Transitional Charges Reduction Scheme. This is the final year of this scheme which has never had baseline provision and therefore requires a budget to be created at the ABR. The scheme caps water and sewerage charges for those households in receipt of Council Tax Benefit.

Concessionary Fares and Smartcards

23. Mr McAveety asked about the increases for concessionary fares and smartcards.

24. The proposed budget increase for smartcard applications results from a decision to compress this £9m project into one year. The aim is to make as much progress as possible with this project before the national concessionary fares scheme comes into effect in April 2006.

25. The increase from £10m to £25m relates to the current concessionary fares scheme (not the new national scheme), operated by local authorities to provide free local off-peak travel. While most of the cost of these local schemes is allocated through the local government finance settlement the balance is paid directly from this budget head. The £25m budget now proposed compares with grants of approximately £22m paid in respect of 2004-05.
26. For the national scheme, the Executive has been in negotiations with the Confederation of Passenger Transport. The outcome of these discussions is that there is an agreed cap on costs of £159m in 2006-07 and of £163m in 2007-08.

M74 Completion (land acquisition)

27. The Convener asked for information on the process and costs for the land acquisition for the completion of the M74.

28. The Executive has been pursuing a policy of acquisition of land for the M74 well in advance of the scheme start to allow businesses time to find new premises and relocate. This is particularly important in the case of a number of major businesses who will require in excess of 2 years for this. If we are to avoid any further slippage in the scheme delivery programme after the judgment on the Court of Session appeal then the Executive must continue to work with some of the remaining businesses in this category. This will require the land acquisition and compensation to be paid sooner rather than later.

29. The total estimated cost for the acquisition of land required for the M74 completion is £188m. This has been provided by the District Valuer who has revised the estimate to take account of compensation cases paid to date.

30. To the end of 2005 a total of 28 business interests (26 owner occupiers and 2 tenants) have been acquired at a total cost of £98.06m. Spend to the end of 2005 within the current financial year is £49.56m. It is anticipated that a further 12 business interests will be acquired by the end of 2005-06 taking the total spend, including compensation paid against ongoing relocations, to the £64.7m budget target. The total spend to end 2005-06 will therefore represent 60% of the total estimated land compensation budget. The Scottish Executive pays 87.35% of the total costs for the M74 with the balance paid by project partners. A list of those business interests purchased and compensated so far and those expected to be completed by end 2005-06 can be provided if requested. Assuming the total spend in 2005-06 as stated then a total of £74.8m or 40% of the budget remains to be spent. This would fall to be spent in 2006-07 either following further voluntary acquisitions or following a successful outcome to the court case by Compulsory Purchase Order.

31. A total of approximately 3,000 people are employed in 109 businesses affected by the scheme. To end 2005 a total of 47 businesses employing 2,400 or 81% of the total jobs were in the category of having already relocated or having relocation arrangements secured or in hand. The District Valuer is actively discussing compensation with a number of other businesses who say that they are suffering hardship and/or who have expressed a desire for the Scottish Ministers to acquire their land and property and provide compensation.

Marketing Development and Advertising Budgets

32. Mr Brownlee asked how marketing development differs from advertising.

33. The Advertising budget consists of four elements:

33.1 Media - the cost of buying space on television, radio, press, etc. which we purchase to display adverts;

33.2 Agency Fees - the money we pay to creative agencies to create and manage our campaigns;
33.3 Production - the costs incurred producing advertising materials such as television commercials; and

33.4 Research - monies paid to research companies to evaluate both creative work and effectiveness.

34. The Marketing Development budget funds those elements of communications work that are not covered by the Advertising budget. This includes costs for elements such as web development and support, PR services to extend campaign reach, editorial promotions with media organisations, secondment costs for agency staff, events and promotions, brand development and management, sponsorship and testing of new delivery concepts such as mobile phone texting.

International Relations (International Aid)

35. John Swinney asked if the International Aid budget is contained within the budget for International Relations.

36. The International Relations budget consists of 3 elements: Fresh Talent, General Promotion of Scotland and International Development. Following the ABR, the funding baseline for each component is £1.3m, £4.625m and £3m for International Development (an element of which is International Aid) respectively.

37. The reduction of £0.47m was in respect of time limited transfers to the Administration Budget. The Relocation Advisory Service which has been established as part of the Executive’s Fresh Talent initiative received £0.4m and £0.07m was transferred to support implementation of the Scotland’s International Image initiative to promote Scotland as a great place to visit, live, learn, work and do business. These transfers reduced the Fresh Talent and General Promotion of Scotland provision by £0.4m and £0.07m respectively.

Accountant in Bankruptcy (relocation)

38. The Convener queried the increase of £2.5 million for the Accountant in Bankruptcy (AiB). It has relocated to North Ayrshire from Edinburgh. Due to the complex nature of the work of the Agency it has been necessary to transfer the work gradually as training of new staff has been completed. This has meant maintaining a parallel operation of experienced staff in Edinburgh during the recruitment and training phase. Under current plans all work will be transferred by June 2006 with the Edinburgh office closed down around end 2006.

39. The latest estimate of the total cost of relocating the Agency is £4.15m; £1.25m in 2004-05; £2.4m in 2005-06; and £0.5m in 2006-07.

40. As part of the transitional arrangements to transfer work, the Agency has a planned programme of increasing staff in North Ayrshire and reducing staff in Edinburgh. There are currently 80 staff in North Ayrshire and a further recruitment campaign is planned shortly. There are 45 staff remaining in Edinburgh; 25 dealing with case enquiries; 7 providing support services to Ayrshire colleagues including Finance and HR; and 13 working on the IT project to replace the Agency’s case management system.

41. The Committee asked for some detailed assessment of particular aspects of the relocation costs and the Minister will be writing to the Committee with that when he responds to a range of issues raised at his 13 December appearance.
Mr Swinney raised the reduction in the 2005-06 provision for the Efficient Government Fund (EGF).

The £60m EGF was launched in October 2004 as a challenge fund to stimulate a sustainably more efficient public sector and to demonstrate the reallocation of resources for better front line use. Its aim is to fund multi partner projects which seek to deliver efficiency savings using proven approaches, such as sharing support services.

The application process is in 2 stages. Stage 1 is an ‘expression of interest’ bid, which allows us to test whether the proposal is eligible for funding and has some prospect of successful delivery. If so, applicants are invited to submit a detailed business case – a Stage 2 bid – which EGF may support with up to 50% of the development costs. It is the consideration, in competition, of formal business cases which will determine a project’s success in securing funding through the competition.

The closing date for Stage 1 bids was 29 July 2005 and 96 bids were received. Assessment of all but 9 of these bids has been carried out and, to date, the Minister has approved 24 applications to be invited to proceed to the next round of the competition. We expect to be in receipt of the first fully worked up Stage 2 bids by 31 March 2006 with the rest coming forward by the closing date of 31 August.

In July 2005, approval was given for the use of £6 million from the EGF to assist in the delivery of the wider efficient government agenda, as a number of demands had arisen relating to the delivery of the policy, as distinct from Efficient Government projects.

One such demand was the activity of the Performance and Innovation Unit (PIU) which was funded as a project from the EGF and received £1 million at the ABR. As the full demand for funding for these and other efficient government project funding was unknown at this time, £8.8m (balance of £5m relating to policy delivery costs and £3.8m other EGF projects) was transferred to Central Unallocated Provision (CUP) for use at Spring Budget Revision or later in the timetable of the Fund.

Payment of EGF monies to successful projects will be made via the partnership’s Lead Bidder. Most of the projects approved to proceed to Stage 2 of the competition have appointed a local authority in this role and payment of grant to these partnerships will be made annually through the redetermination adjustments to the Revenue Support Grant (RSG). It should be noted, therefore, that most of the EGF expenditure in future years will be handled via CUP movements and transfers to other Departmental baselines.

Increase in Operating Costs of Agencies and NDPBs (£70m)

Finally, it is worth highlighting that all of the increases in Agency and NDPB budgets have been found from within existing portfolio budgets and are simply a reallocation of existing resources. No additional resources have been given to portfolios to meet these particular increases. Some examples (excluding the Environment & Rural Affairs and Accountant in Bankruptcy examples explained above) of the reasons for these increases follow:

49.1 Scottish Higher Education Funding Council (£16.6m) – Post Graduate Certificate in Education: Transfer from Education Department in respect of additional funds to take account of the need to train additional teachers to meet the Partnership Agreement commitments on teacher numbers and class sizes in 2007. Clinical Academics: Transfer from Health
of the need to train additional teachers to meet the Partnership Agreement commitments on
teacher numbers and class sizes in 2007. Clinical Academics: Transfer from Health
Department to cover the Health Department's share of increased costs for Scotland's 350
clinical academics for 2005-06.

49.2 Scottish Enterprise (£14.5m) – change in payment mechanism to use SEn as the body
to pay out enterprise grants. Some examples include: Small business start up fund: Funding
to develop a scheme to attract marginal players to start up in business, where lack of finance
constitutes a barrier, and providing small grants targeted at 18-30 year olds; Capital for
Finnieston Bridge: Take up of End Year Flexibility to provide an injection of capital funding
towards the construction costs of the Finnieston Bridge project; Lithgows Landcatch:
Transfer from ERAD for the reimbursement of investment capital costs incurred by SEn in
providing financial assistance to Landcatch Natural Selection (LNS), a smart science
aquaculture company; and West Lothian Action Plan: Final element of 4 year funding. The
funding is part of the total £6m commitment to the area given by the Executive in the wake of
the Motorola closure. SEn Edinburgh & Lothians is administering the funding on behalf of
the West Lothian Economic Partnership.

49.3 VisitScotland (£7m) – The increase results from an internal portfolio transfer of £2m
from Other Arts to cover costs associated with the development of the new integrated
VisitScotland tourism network and £5m from Enterprise Transport and Lifelong Learning
Department for marketing and quality assurance.

49.4 Scottish Further Education Funding Council (£6.6m) – Further Education/School
Review: To meet the Executive’s Partnership Agreement commitment to enable 14-16 year
olds to develop vocational skills and improve their employment prospects by allowing them
to undertake courses in further education colleges as part of the school based curriculum.

49.5 Highlands & Islands Enterprise (£3.5m) – Many elements make up the total, but the
major ones are: Take up of End Year Flexibility (EYF) to provide additional capital
expenditure for the Inverness MediCentre and the Western Isles Enterprise Connected
Communities broadband service; and also transfers from within Enterprise portfolio to
Scottish Community Household Renewables Initiative to assist HIE in administering an
advisory service and grant scheme for communities interested in developing renewable
energy projects.

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