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Patricia Ferguson, MP
Scottish Affairs Committee
House of Commons

30/01/2025

Re: additional evidence for committee inquiry session, 29/01/2025

Dear Ms Ferguson,

Following up on my appearance at the committee on 29/01/2025, I wanted to provide some supplementary information which might be of interest in relation to questions about whether interest should be charged on borrowing to cover negative forecast errors.

I stand by my answer, but there are two further points worth making.

1. I highlighted how the 3-year gap between the tax year in question and reconciliations between forecasts and outturns mean that the Scottish Govt, in effect, does have an interest free loan for negative reconciliations – for that first 3 years. That also means though that the Scottish Govt is, in effect, giving the UK government an interest free loan for 3 years when forecasts initially under-estimate the Scottish net income tax revenue position and there is a positive net reconciliation.

2. Once the reconciliation payment becomes due, interest is payable if the Scottish Govt borrows to offset a negative reconciliation. If it uses a positive reconciliation payment to reduce capital borrowing, for example, it also benefits from not incurring the interest on that borrowing. If it uses a positive reconciliation to pay into reserves though to draw down over a few years, it doesn't earn interest on the money in those reserves. Arguably there is a case that there should be symmetrical treatment of borrowing and saving. When the Scottish Govt puts money into reserves it reduces the net cash requirement of the UK government, saving the UK government some interest. Given the Scotland reserve has grown out of the Budget Exchange system for Whitehall departments, and HMT doesn't pay interest on Budget Exchange if Whitehall departments carry forward a bit of their budget, the UK government would likely push back on this suggestion citing symmetry between the Scottish Government and Whitehall departments. But while Whitehall departments do not earn interest on money carried forward via Budget Exchange, the UK government as a whole does. So, considering things on a governmental (rather than departmental) basis, that is not a strong argument for not paying interest to the Scottish Government on its reserves.

I hope this is helpful.

Best wishes

David Phillips

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