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| **An Leas-phrìomh Mhinistear agus Ath**-**shlànachadh Cobhid**  **Deputy First Minister and Cabinet Secretary for Covid Recovery**  John Swinney MSP  T: 0300 244 4000  E: DFMCSCR@gov.scot |  |
| Rt Hon Jeremy Hunt MP  Chancellor of the Exchequer  HM Treasury  1 Horse Guards Road  London  SW1A 2HQ  «Address7» |  |

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March 2023

Dear Jeremy

**UK Government Spring Budget**

I fully recognise the challenging economic context that we both wrestle with, and the continuing pressures caused by inflation, the impact of Brexit and Russia’s illegal war in Ukraine. However, cost of living rises are putting a huge strain on households, many of whom are struggling to cope, and the outlook remains very concerning. The [Resolution Foundation](https://www.resolutionfoundation.org/press-releases/uk-households-just-halfway-through-two-year-cost-of-living-crisis-with-incomes-set-to-fall-by-2100/) estimates that typical incomes among non-pensioner households will fall by 4% in 2023-24 in real terms, compared to 3% in 2022-23.

The Scottish Government is doing what it can with its limited powers to ensure people receive the help they need. However, given the constraints of devolution, it is vital that the UK Government uses its full range of reserved powers to address these economic challenges and support people and businesses through this difficult time.

When I met with the Chief Secretary to the Treasury in Edinburgh last month I raised some of our expectations for the UK Budget. I am setting these out in more detail here and would urge you to act on them.

Overall budget settlement and continuing inflationary pressures

In your Autumn Statement, you announced Barnett funding increases in 2023‑24 and 2024‑25. While welcome, these are not sufficient for Scotland’s needs and are likely to be offset completely by lower projected Barnett funding in 2025‑26 and 2026‑27. At the end of this period, the Scottish block grant is expected to be lower in real terms than it was in 2021‑22. This is an extremely challenging fiscal situation. I have had to take difficult decisions in order to help to those most impacted by the cost of living crisis while tackling budget pressures caused by rising inflation and economic uncertainty, but significant pressures remain in the year ahead. It is vital that the Spring Budget provides additional funding for devolved governments to enable us to support people, provide fair public sector pay increases and invest in the public services and infrastructure that will deliver economic growth.

Managing in-year pressures and budget volatility is challenging for the Scottish Government given the limited flexibility to borrow and the need to balance the budget within fixed nominal limits which are eroded by inflation over time. Additional flexibilities would allow the Scottish Government to mobilise and deploy funding in the most effective and efficient way to support our citizens. I urge you to ensure that the Scottish Government and Parliament have the necessary fiscal flexibility to manage the risks we face within our devolved responsibilities, and to support economic recovery.

Public sector pay

I note the recent development on 22 February where UK Government departments made their formal 2023-24 pay submissions to eight public sector pay review bodies, indicating that only a 3.5% pay rise is affordable under current HM Treasury allocations. The Spring Budget must deliver additional funding across the UK to fund higher public sector pay awards. This increased funding would relieve the funding pressures we face and enable the Scottish Government to respond further to the cost of living crisis through fair pay increases for the public sector.

Capital investment

Disappointingly, the UK Autumn Statement delivered a 3% real terms cut to our capital grant for 2023-24 in the face of increasing costs - placing significant additional pressure on our capital programme. I urge you to use the Spring Budget to rectify this to allow our capital programmes to continue at the required pace and give a boost to the industry at this challenging time.

Cost of living and support with energy bills

Scotland is an energy rich nation, with significant renewable energy resource, yet fuel poverty is increasing. We estimate that the planned increase in the Energy Price Guarantee to £3,000 and ending of the £400 Energy Bills Support Scheme would result in an additional 120,000 fuel-poor households in Scotland compared to this winter. The recent price cap announcement by Ofgem still means that people are having to choose between heating and eating. It is essential that the UK Government reverses its plan to increase the Energy Price Guarantee from April and extends its support for domestic customers, given the Scottish Government does not yet hold all the powers to address the issue of high energy costs at source. I have consistently called upon the UK Government to provide additional support for vulnerable households with their energy costs, funded through taxing windfall gains rather than passing the cost on to taxpayers, which has regrettably not been forthcoming.

The Cabinet Secretary for Net Zero, Energy and Transport and I recently wrote to the Secretary of State for Energy Security and Net Zero about the changes to available support for non-domestic users. We raised concerns that the reduced funding envelope for the Energy Bills Discount Scheme will mean that many vulnerable non-domestic users will continue to struggle with their energy costs. It is critical that businesses in Scotland receive the support they need to allow them to operate with confidence without the uncertainty aligned to high energy costs. Many of our key public service providers such as local authorities and the healthcare sector are also facing considerable pressure at the moment and should be considered for additional support.

Stakeholders with high energy usage are concerned that they will not be covered by the UK Government’s definition of energy and trade intensive industries and we would like reassurance that they will be included. Additionally, we are concerned that there will be insufficient support for users of alternative fuels, who are more likely to be located in rural areas. Many rural businesses who rely upon heating oil and alternative fuels are already having to contend with higher costs of doing business than those in more central areas. It is therefore essential that they receive an adequate level of support to help with their energy costs.

Social security

I welcome the uprating of State Pensions and benefits by 10.1% to take effect from April 2023. The Scottish Government took similar action to uprate all devolved benefits by 10.1% from April 2023, building on our previous 6% uprating in April 2022, as well as increasing the Scottish Child Payment by 25% over last year. For families in poverty the still rising cost of essentials such as food, utilities and vital household goods remains too high and they are facing hardship. Once again, I urge you to reinstate the uplift to Universal Credit, increase it to £25-per-week and extend it to means-tested legacy benefits, as well as ending the benefit cap and the two-child limit. This would do much to lift families out of poverty, as highlighted by the report of the [Commissioner for Human Rights of the Council of Europe](https://search.coe.int/commissioner/Pages/result_details.aspx?ObjectId=0900001680a952a5#_Toc119660039). In addition, I urge you to follow the Scottish Government’s lead and urgently develop and implement a comprehensive benefit take-up strategy to help put money into the pockets of households most in need.

Taxation

Whilst the Scottish Government is doing all we can with our limited powers, the UK Government’s reserved tax levers are crucial to economic recovery. The tourism and hospitality sectors play an important role in Scotland’s economy and many businesses are still struggling to recover to pre-pandemic levels due to the impact of the cost crisis. A reduced rate of VAT is a consistent ask from those sectors, and I would urge you to consider this and all other reserved tax levers that can help provide support and certainty for their future. Extending the super-deduction, or introducing equivalent capital allowance incentives would help further by giving businesses the certainty to invest and grow.

The cultural sector also continues to face significant challenges, and so the UK Government must reconsider plans to decrease the levels of tax relief for theatres, orchestras, museums and galleries from 1 April 2023 to help protect these organisations that contribute so much to society.

Climate change

I am aware that you will soon be responding to Mission Zero, the report of the Independent Review of Net Zero and ask that you share your response with the devolved governments in advance. I welcome the report’s emphasis on seizing the economic opportunity offered by net zero, and the need for early action to reap these benefits, for which the Scottish Government has long been pressing. This includes providing a clear, accelerated and streamlined Carbon Capture Utilisation and Storage (CCUS) roadmap to 2030, which ties into a longstanding ask from the Scottish Government to confirm the position of the Scottish Cluster including ACORN. The Prime Minister has acknowledged the strength of the Scottish Cluster proposition, and said that the UK Government looks forward to its continued participation in the CCUS programme: it is vital that the UK Government now confirms Track 2 will be awarded in 2023 if we are to meet Scotland’s and the UK’s net zero targets. We also agree with the report’s recommendations on low-carbon heat, which support our aim of decarbonising a million homes by 2030 and to develop a 10-year delivery roadmap for the scaling up of hydrogen production. In responding to this review, it is vital that you work with the devolved governments and that all co-benefits of mitigation policy action are realised.

I urge you to use your reserved tax levers to help both governments reach net zero. This includes issues with existing taxes, such as addressing the discrepancy in VAT treatment of existing land and buildings in contrast to the advantageous zero-rating of new build construction. This will help incentivise retrofitting of existing structures, revitalise our towns and cities, and reduce carbon emissions.

I understand that the UK Government is also working to understand the impacts of the measures taken by the US Government’s Inflation Reduction Act and equivalent EU measures and I ask that you continue to share this analysis, including at a Scotland level. I urge you to carefully consider the implications for UK’s journey to net zero and make us aware in advance of any measures you are considering taking forward in response.

In 2023-24 we will be investing a further £50 million from our 10-year Just Transition Fund, for North East Scotland and Moray. This will more than double the 2022-23 allocation, helping to diversify regional economies away from carbon-intensive industries and capitalise on the opportunities that transition to net zero can bring, such as jobs and prosperity. The Scottish Government, alongside unions and industry, has called on the UK Government to match this fund, but we have not yet received a positive response. Once again, I repeat that call and urge you to include this in the Budget.

Migration

Changes are required to the immigration system to address the acute labour market shortages faced by businesses and the public sector and the Scottish Government has consistently called for an overhaul of immigration fees and processes. The UK Government must accept the Migration Advisory Committee’s recommendation to deliver a migration pilot for rural areas, as set out in the Scottish Government’s Rural Visa Pilot proposal. We are keen to work with you to develop and deliver such a proposal in partnership with local authorities and employers, to address the urgent need for targeted migration solutions to benefit Scotland’s remote, rural and island communities.

Scotland must be able to attract and retain talented people to study and workhere without excessive barriers. I am very concerned at suggestions the UK Government may reduce the number of international students who can work in the UK after graduating and the amount of time they can stay. This would be detrimental to both our Universities and the Scottish economy and I call on you to rule this out. It is also important that all visa applications are processed promptly to ensure that Scotland remains an attractive destination for international students and graduates.

Horizon Europe

I am concerned that £1.6 billion of funding originally allocated by the UK Government to facilitate association to EU Programmes has been claimed back by the Treasury, risking future access to Horizon Europe. This is in direct contradiction to the UK Government’s previous commitment to invest these funds into research and innovation. It is vital that the UK Government opens discussions on re-joining Horizon as soon as possible and provides assurance to the sector that it will mitigate this loss of funding and the wider damage caused by Brexit, which has been a disaster for universities, students and the research community.

Levelling Up funding

The Scottish Government is opposed to UK Ministers making spending decisions in wholly devolved policy areas facilitated by the UK Internal Market Act, which the Scottish Parliament voted against. Funding should be allocated in the usual way via Barnett consequentials to respect devolution and the priorities of Scotland.

I recently wrote to the Secretary of State for Levelling Up, Housing and Communities, to propose closer working on regional economic development, building on the constructive approach taken by both our governments to Green Freeports and the City Region and Growth Deals. We look forward to further discussions on this but, in the meantime, make the case for the remaining Levelling Up fund money that is due to Scotland to be transferred directly to the Scottish Government. This would enable us to allocate it in line with the priorities in our National Strategy for Economic Transformation and the recommendations in our Regional Economic Policy Review.

This principle extends to the UK Shared Prosperty Fund, and Scotland’s share of this ought to be routed through the Scottish Government to allow strategic interventions to be made that reduce economic disparity within and between regions. Scotland’s allocation of £212 million over three years remains far below the £549 million that would equal EU funding, calculated and published in the Bell Report in November 2020. Future arrangements must meet the promise to fully replace EU funding lost as a result of Brexit.

This Budget provides an opportunity to take meaningful action to address the current economic challenges. This must include investing in our valuable public services, enabling economic growth and providing the support that people and businesses need at this difficult time.

I am copying this letter to the Rt Hon John Glen MP, Chief Secretary to the Treasury.

**JOHN SWINNEY**