



ADVISORY GROUP ON ECONOMIC RECOVERY (SCOTTISH GOVERNMENT CALL FOR VIEWS)

Issued 5 June 2020

ICAEW welcomes the opportunity to provide evidence to the Scottish Government's **Advisory Group on Economic Recovery**, which opened a call for views on 18 May 2020.

We believe there are four areas the Scottish Government should include in its action plan for recovery and sustainable growth in the Scottish economy:

- Design devolved taxes to encourage enterprise
- Support infrastructure investment
- Encourage businesses to take action climate risk
- Skills

These are explored in this written evidence. We would welcome the opportunity to discuss our ideas with the Advisory Group.

This response of 5 June 2020 has been prepared by the ICAEW Corporate Finance and Tax Faculties, along with the Business and Industrial Strategy team. Recognised internationally as a source of expertise on corporate finance and tax issues, ICAEW Faculties are responsible for ICAEW policy on technical issues in their areas of expertise, including submissions to consultations. The ICAEW Business and Industrial Strategy team is key to putting the voices of Chartered Accountants across all regions and nations at the heart of policy making.

ICAEW is a world-leading professional body established under a Royal Charter to serve the public interest. In pursuit of its vision of a world of strong economies, ICAEW works with governments, regulators and businesses and it leads, connects, supports and regulates more than 150,000 chartered accountant members in over 160 countries. Our members work for and advise businesses across Scotland. ICAEW members work in all types of private and public organisations, including public practice firms, and are trained to provide clarity and rigour and apply the highest professional, technical and ethical standards.

© ICAEW 2020

All rights reserved.

This document may be reproduced without specific permission, in whole or part, free of charge and in any format or medium, subject to the conditions that:

- it is appropriately attributed, replicated accurately and is not used in a misleading context;
 - the source of the extract or document is acknowledged and the title and ICAEW reference number are quoted.
- Where third-party copyright material has been identified application for permission must be made to the copyright holder.

For more information, please contact: representations@icaew.com

ICAEW Members in Scotland (IMS) provides a local network for members. Through our volunteer groups we offer support, help and advice to members across Scotland along with a programme of professional development and business networking events.

KEY POINTS

1. The call for views was open for evidence for a two-week period and our comments below are therefore initial reflections that do not reflect detailed discussion in our technical committees. We would welcome the opportunity to participate further in the Advisory Group's work.

ECONOMIC LANDSCAPE

ICAEW's quarterly **Business Confidence Monitor (BCM)** is based on 1,000 interviews conducted with ICAEW members, covering a range of economic sectors, regions and company sizes. In the BCM for Q1 2020 (published in February 2020, before the coronavirus outbreak), it found overall business confidence returning to positive territory in the first quarter of 2020, after being at its lowest level for a decade at the end of 2019.

UK-wide findings:

- Confidence Index rises to +1.3 (from -20.6 last quarter), at least partly due to the general election. Underlying economic fundamentals remain challenging.
- GDP may experience a small bounce in Q1, but growth is likely to remain subdued through 2020.
- Domestic sales and exports are slowing compared to previous years, and this is leading directly into a duller picture for profits growth.
- Capital investment remains low due to continuing uncertainty - including over future trade deals, with plans for the year ahead still very weak.
- Slow growth in investment continues to hurt productivity performance.
- Concerns over regulations remain the most commonly cited challenge and will be a factor to watch during this year's trade negotiations.

Scotland findings:

- 2.2% growth in domestic sales (as an annual percentage change), in the bottom third of all UK regions
- 1.2.% growth in export sales (as an annual percentage change), the lowest of all UK regions
- When asked "How would you describe your confidence in the economic prospects facing your organisation over the next 12 months, compared to the previous months?", Scottish business confidence registered at -2, up from -11 in Q4 2019, in the lower half of all UK regions

On 22 May 2020, **ICAEW and its partner Oxford Economics published a report** which examines the differing impacts of the coronavirus pandemic on the UK regions and forecasts the likely impacts between 2020-2025. These forecasts focus on regional coronavirus vulnerability, and the potential impact of the 'levelling up' policy goal.

Scotland findings:

- Although Scottish Gross Value Added (GVA) is set to contract by a slightly smaller percentage than the overall UK in 2020, the Scottish economy may underperform the UK from 2021 onwards.
- Despite a strong 2021 rebound, the number of jobs in the Scottish economy is still likely to be slightly lower in that year than it was in 2019, at 2.79m compared with 2.82m.

- Scotland has a similar industrial structure to the UK but does rely more heavily on the hospitality sector, which has suffered badly this year. It does score better on many other metrics, however.

These findings help to set the scene for ICAEW's public policy stance. The ideas set out below are expressed with the aim of giving the Scottish economy the best chance of economic recovery.

DESIGN DEVOLVED TAXES TO ENCOURAGE ENTERPRISE

Aim for certain, simple and competitive taxes

2. We start with tax in this written evidence as this is one of the levers closest in control for the Scottish Government to influence the economy. As the Scottish Government seeks to develop devolved elements of the tax system and potentially considers new taxes, it is essential that that these are designed in a way that fosters rather than holds back economic growth and opportunity.
3. We recommend that the Scottish tax system and any new tax policy measures the Advisory Group considers are tested against a benchmark like our **Ten Tenets for a Better Tax System**.
4. Once the transitional period following EU exit ends, the UK will have control over VAT, one of the largest sources of government revenue. Were VAT to be included in devolved powers, these considerations about the design of the tax system will be particularly pertinent. Considering them now could help equip the Scottish Government to most effective as the devolved tax system develops.

Consider consistency

5. A particular question the Advisory Group might consider are whether and where the Scottish Government should aim for consistency with the rest of the UK in taxes that are devolved and where that defeats the policy object.
6. For example, one question is whether it is sensible that we have three different forms of general anti-abuse rules across the UK. This seems rather disjointed and unhelpful to taxpayers who value certainty. In this case we understand there may be intended to be a differential policy objective, but it would be worth examining whether that objective is being met.

Engage with business

7. In doing that, and in developing tax policy more generally it is vital that a broader set of stakeholders are included in engagement than those proposed by the Scottish Government in 2019 in its consultation on the policy framework for devolved taxes. For example, the other chartered institutes of accountants and tax advisers should be included as well as other professional bodies and stakeholders that are affected by the legislation. Investment decisions can be affected by tax policy hence it is vital that a broader business representation is included.
8. How the government consults on tax is also important. If it wants to be able to use consultation responses to help improve tax policymaking, then those consulted need to be able to make general comments as well as answer specific questions, unlike the online response forms we've seen used recently.

Reform non-domestic rates

9. The non-domestic rates system is broken. A significant part of the cost base for some sectors of the economy and a fixed cost that does not flex with business success, non-domestic rates can disincentivise otherwise productive investment decisions. The system needs reform. Our report **Business Rates: maintain, demolish, rebuild or refurbish** explores the issues and looks at potential solutions.

SUPPORT INFRASTRUCTURE INVESTMENT

10. High quality infrastructure and energy technology brings multiple benefits to business. Government has a key role in supporting its development. Establishment of the new Scottish National Investment Bank is a positive step to help ensure long-term funding flows to Scottish businesses. There will be a role for this institution to ensure proportionate regional and sector support to reduce the risk of recovery being concentrated in parts of Scotland, much as the British Business Bank aims to do, including by engaging with, and attracting, local business and professional communities.
11. The Scottish National Investment Bank will also have a key role in replacing European Investment Bank funding. That supported £2bn of projects in Scotland between 2016 and 2018 and the Scottish Government will need to consider the scale of funding necessary to replace this. Smart policy making can help supplement public investment with incremental private funds. We submitted written evidence to HM Treasury and the Infrastructure & Projects Authority's Infrastructure Finance Review ([REP 59/19](#)), which will also be pertinent to the Advisory Group. In that evidence we recommended that:

Finance innovation has the power to transform infrastructure investment in the UK

- An Infrastructure Growth Fund and pooled investment funds would facilitate investment.
- New public-private partnership contractual models are needed now.
- Approved peer-to-peer networks would enable citizens to invest directly.
- The UK should utilise its world-leading professional expertise in infrastructure finance.

Public investment is an enabler

- A new Investment Bank to replace the EIB as an anchor investor.
- The British Business Bank should support business to deliver infrastructure projects.
- Direct investment by city-regions and local authorities would engage communities.
- Local industrial strategies must make improving infrastructure a top priority.
- Centres of excellence are needed to support investment decisions and in managing risk.

Capital is available, but it needs to be unlocked

- Long-term pricing would provide certainty to investors, taxpayers and consumers.
- Tax and other incentives need to be gauged carefully, but then should be stable.
- Reforming balance sheet treatment requirements would remove contracting hurdles.
- Regulatory asset base and concession arrangements could be used more widely.
- Early-stage risks need to be tackled to draw in more seed capital.

ENCOURAGE BUSINESSES TO TAKE ACTION ON CLIMATE RISK

12. We understand that achieving a green recovery is a core objective for the Advisory Group. Effective climate action relies on businesses making decisions that put people and planet first. Crucially, to put natural capital at the heart of their thinking, businesses need robust systems that provide decision useful information to management and meaningful disclosures to stakeholders.
13. These routes could help to build capacity within businesses to generate this information:
 - Government should consider how business owners and their advisors, including SMEs, will 'see' climate as an issue relevant to them and how it can reach them.

- Financial Institutions: with an increase in regulation from the PRA it's likely the implications of this will be passed on to businesses
 - Governance – in particular internal auditors, audit chairs, non-executives and directors will likely be more conscious of climate risk and how it affects their organisations.
 - Biodiversity loss – this is a similar sort of issue to climate but making it more visible is difficult.
14. We can expect early action from BEIS to extend sustainability reporting, following 2019's Green Finance Strategy and efforts in the EU to extend the non-financial reporting directive. But government efforts also need to be focused on broader capacity building so companies can act meaningfully.

SKILLS

15. As mentioned in [ICAEW Representation 77/19 Treasury Select Committee: Regional Imbalances in the UK Economy](#), skills are paramount to economic growth and so economic recovery through increasing productivity and improving workers' quality of life.
16. Having an appropriately skilled workforce locally attracts inward investment, and increases productivity, an important driver of business growth
17. Members that took part in the Scottish events from this consultation felt that home-grown talent was key for this. A more sustainable method of funding free universities away from reliance on international students was suggested by these members in order to free up more spaces for 'home grown' talent to stay in Scotland to study- which in turn would drive localised economic and social development. This is now particularly pertinent when viewed in the lens of COVID-19 and the potential difficulties in attracting international students.
18. Scotland was however named best in class in this consultation with regards to universities' strategic commitment to enterprise and entrepreneurship. With high levels of graduate start-ups, we urge the continuation of support for these sorts of activities given the positive economic benefits of strong entrepreneurial skills- particularly crucial given the importance of innovative thinking for businesses to react to the current pandemic.