



The Scottish Parliament
Pàrlamaid na h-Alba

ECONOMY, ENERGY AND TOURISM COMMITTEE

AGENDA

4th Meeting, 2014 (Session 4)

Wednesday 19 February 2014

The Committee will meet at 9.30 am in Committee Room 1.

1. **Decision on taking business in private:** The Committee will decide whether to take item 4 and all future reviews of evidence in private.
2. **Inquiry into Scotland's Economic Future Post-2014:** The Committee will take evidence from—

Rt. Hon Danny Alexander MP, Chief Secretary to the Treasury, and Stephen Farrington, Deputy Director, Economics of Scotland and the UK, HM Treasury, UK Government;


and then from—

Nicola Sturgeon, Deputy First Minister and Cabinet Secretary for Infrastructure, Investment and Cities, John Swinney, Cabinet Secretary for Finance, Employment and Sustainable Growth, Dr Gary Gillespie, Deputy Director, Office of the Chief Economic Adviser, Dr Graeme Roy, Head of the Office of the Chief Economic Adviser, and Martin McDermott, Policy Adviser, Elections and Constitution Division, Scottish Government.

3. **Deep Sea Mining Bill (UK Parliament legislation):** The Committee will consider the legislative consent memorandum lodged by the Cabinet Secretary for Finance, Employment and Sustainable Growth (LCM(S4)29.1).
4. **Inquiry into Scotland's Economic Future Post-2014:** The Committee will review the evidence heard at today's meeting and discuss any follow-up actions.

EET/S4/14/4/A

Stephen Imrie
Clerk to the Economy, Energy and Tourism Committee
Room T2.60
The Scottish Parliament
Edinburgh
Tel: 0131 348 5207
Email: stephen.imrie@scottish.parliament.uk

Agenda item 2		EET/S4/14/4/1
14 February 2014		

Economy, Energy & Tourism Committee
Scotland's Economic Future Post-2014:
UK Government and Scottish Government
Background Briefing

This briefing provides an overview of the debate between the UK Government and Scottish Government on key economic issues post-2014. It also draws on some additional publications and commentators which have contributed to the debate. The key areas covered by the briefing include the monetary framework, the fiscal framework (including taxation, public spending and net debt/borrowing), economic growth and equality.

Note that the briefing provides an overview of some of the key issues debated, but does not try to offer comprehensive coverage.

Monetary framework

The outcome of the Referendum will determine whether or not Scotland must design its own monetary framework. A key part of this framework would be the currency adopted by an independent Scotland.

Currency union option

The Scottish Government's Fiscal Commission undertook an [Assessment of Key Currency Options](#) (2013) including retaining Sterling in the context of a formal monetary union, adopting the Euro or establishing a Scottish currency. Both the Fiscal Commission and the Scottish Government are in agreement that, given the economic integration between Scotland and the rest of the UK, an independent Scotland would wish to continue to use Sterling in a formal monetary union.

At the end of last month, Mark Carney the Governor of the Bank of England spoke of the benefits of a currency union in eliminating transaction costs, promoting investment, reducing borrowing costs and promoting integration. However, he stated:

“Set against these benefits are the potentially large costs of giving up an independent monetary policy tailored to the needs of the region and a flexible exchange rate that can help absorb shocks.” [\(2014\)](#)

He went on to explain that the success of the currency area “hinges on whether its features mitigate the costs of losing the flexibility that comes from an independent monetary policy” (2014). He also advanced the case for shared fiscal arrangements within a currency area, while recognising that this would require some ceding of national sovereignty.

The Chancellor of the Exchequer, George Osborne, delivered a [speech in Edinburgh on Thursday 13th February 2014](#) picking up ‘where the Governor’s speech left off’. He appears to rule out a formal monetary union between an independent Scotland and the rest of the UK:

‘First of all, the Scottish government say “it’s as much Scotland’s pound as the rest of the UK’s”. They are like an angry party to a messy divorce. But the pound isn’t an asset to be divided up between the two countries after break-up as if it were a CD collection...A vote to leave the UK is also a vote to leave these unions and those transfers and those monetary arrangements. That’s part of the choice that people in Scotland are being asked to make. There’s no legal reason why the rest of the UK would need to share its currency with Scotland.’

Referring to [advice from the Treasury's Permanent Secretary](#) (the Treasury’s most senior civil servant), the Chancellor advises against a currency union for the following reasons:

1. The Scottish Government has left open the option to leave a currency union. However, according to the Treasury, ‘successful currency unions are based on the near universal belief that they are irreversible’;
2. The size of Scotland’s banking sector relative to its national income means “there is a very real risk that the continuing UK would end up bearing most of the liquidity and solvency risk which it creates”;
3. ‘Asymmetry’ leading a real possibility that the continuing UK has to ‘bail-out’ Scotland in the event of a financial or fiscal crisis. However assistance could not be reciprocated: ‘it is inconceivable that a small economy could bail-out an economy nearly ten times its size’;
4. An independent Scotland’s fiscal policy would become ‘increasingly misaligned’ from a continuing UK’s. Such divergence would eventually put “intolerable pressure on the currency union’.

The Chancellor’s speech and his Permanent Secretary’s letter summarise the key points from the Treasury’s [Scotland Analysis: Assessment of a sterling currency union](#) published on the same day.

The Scottish Government’s submission to the Committee, sent the following day (14th February), responds to the Chancellor/Treasury’s four points (see Annex G of the submission). In short, it argues that a whole range of reforms to the financial sector, both nationally and internationally, have been

introduced since the 2008/09 crash making any need for bank bailouts less likely. As such, there would be minimal risk to taxpayers in the continuing UK from Scottish banks. Indeed the response goes on to argue that an independent Scotland would be less exposed to risks from its financial sector than the whole of the UK, stating that ‘the size of the Scottish financial services sector as a proportion of the overall onshore Scottish economy is 8.0% – similar to the UK – and smaller than the UK at 6.7% when a geographical share of oil and gas output is included’.

The Scottish Government also uses its submission to reiterate its belief that political unions are not a requirement for successful monetary unions, pointing to the Belgium and Luxembourg union which existed until 2002. The Scottish Government agrees that aggregate borrowing and debt levels would have to be agreed between partners in a monetary union; however, on the matter of fiscal flexibility it believes there are many examples, even within unified states, that demonstrate national/regional variations in taxation levels without any accompanying currency pressures.

Furthermore, the Scottish Government also highlights its belief that a monetary union would benefit the people of a continuing UK as well as those in Scotland. According to the SG:

- Scotland is a key trading partner for the rest of the UK, which exports more to Scotland than to Brazil, South Africa, Turkey, Russia, India, South Korea, China and Japan put together.
- Scottish oil and gas production would boost the Sterling Area’s exports by £30 billion
- Scotland and the UK are better suited to monetary union than the Eurozone economies (pointing to very similar productivity and output per capita rates)

In a previous Treasury Scotland Analysis publication on [Currency and monetary policy](#) the UK Government suggests that independence will lead to a weakening of economic integration, and questions the economic rationale for the UK to agree to a monetary union. It also states that Bank of England would continue to play an important stability role in a monetary union and this may include providing lender of last resort facilities to the financial sector. However, it states:

“The UK’s interest would be to minimise these risks through a well designed fiscal framework and clear conditions for financial stability interventions. An independent Scottish state would need to agree to a negotiated set of constraints on economic and fiscal policy. In practice this would be likely to include rigorous oversight of Scotland’s economic and fiscal plans by the UK authorities.” (2013)

There are reports that the First Minister Alex Salmond has warned that an independent Scotland could walk away from its share of the UK's national debt if the UK Government rejects its terms for a monetary union (FT [2014](#) and [Scotsman 2014](#)). The National Institute of Economic and Social Research's Angus Armstrong and Monique Ebell believe 'there is a reasonable claim that an independent Scotland would be entitled to a population share of its assets (including sterling and the Bank of England) and liabilities (debt)' (my parenthesis). Nevertheless, the Permanent Secretary to the Treasury offers a different view:

"...you can expect the Scottish Government to threaten not to take on its share of the United Kingdom's debt. I do not believe this is a credible threat. First, the sooner an independent Scotland established economic credibility, the better it would be for its economic performance. An extensive wrangle about its share of the debt would increase uncertainty and hence its funding costs. Secondly, the debt is one of a number of issues which would have to be settled post independence, where the new Scottish state would require the cooperation of the international community including the continuing UK"

Other currency options

On the other hand, some have also suggested that establishing a new Scottish Currency would have economic benefits. For example, research by the National Institute for Economic and Social Research (NIESR) on [Scotland's Currency Options](#) (2013) suggests that there may be a case for introducing a new Scottish currency to give an independent Scotland an extra degree of policy freedom to support the financial system if necessary. Writing for the Jimmy Reid Foundation, Jim Cuthbert argues ([2013](#)) that the UK is not an optimal currency area and suggests that there would be benefits to an independent Scotland ultimately having its own currency.

While Professor John Kay agrees that using Sterling is the most sensible option, he believes that the most likely outcome would be the establishment of a new Scottish currency:

"Monetary union with the rest of the UK is the most sensible course – and the one the Scottish government proposes. But in the context of the troubles of the eurozone, the Treasury and Bank of England might be expected to seek extensive control of both Scottish fiscal policy and banking supervision. Yet with Scotland representing only 8.5 per cent of the monetary union, it is hard to imagine them conceding many such rights back to Scotland. While Mr Salmond insists that there is no currency plan B, Scotland would have no negotiating power without one and the rational plan B – a Scottish pound pegged to sterling – is also the likely outcome." ([2013](#))

Fiscal policy

Taxation, public spending and borrowing and debt post-2014 are dealt with in turn below.

Taxation

The Fiscal Commission Working Group published their report [Principles for a Modern and Efficient Tax System in an Independent Scotland](#) (2013) suggesting that independence offers an opportunity to re-examine the tax system and design one that is more robust and efficient following the principles of simplicity, neutrality, stability and flexibility. Recommendations and examples to consider include:

- The use of a select few targeted tax reliefs
- The use of modern technology to lower the burden of administration and compliance
- Linking the tax and welfare systems so the system can be used to tackle inequality effectively

Indeed, in the White Paper on independence, the Scottish Government proposes to simplify the tax system to reduce compliance costs, streamline reliefs and help to reduce tax avoidance. The Scottish Government also notes the opportunity to better link the welfare and tax system. It highlights a number of priorities for building a taxation system focussing on economic growth including reducing Air Passenger Duty by 50 per cent and reducing corporation tax by up to three percentage points ([2013](#)).

In their report [Taxing an Independent Scotland](#) (2013), the Institute for Fiscal Studies (IFS) expressed a similar view to that of the Fiscal Commission on the opportunity for reform offered by independence. However, while recognising that the Scotland has made some different choices in the areas of taxation already devolved, the IFS noted that “the Scottish Parliament has eschewed more fundamental reform of these taxes.”

The IFS also point out new challenges would arise as a result of the creation of a tax border between Scotland and the rest of the UK, ranging from cross-border shopping in the context of indirect taxes to tax competition in the direct tax system. Tax competition between Scotland and the rest of the UK could leave both areas raising less revenue than if there is co-operation to set rates at what would be best collectively ([2013](#)). Dr Andrew Goudie highlights that within a Sterling monetary union the UK Government might seek an Agreement to set limitations on the ability of an independent Scotland to engage in tax competition in pursuit of advantage (2013)¹.

If there is a No vote at the Referendum then there may well be a debate about whether more tax powers should be devolved. The Prime Minister David Cameron has indicated that he is prepared to devolve more powers in this situation (BBC [2012](#)). The issue of further devolution in the event of a No

¹ p.49 Scotland’s Future: the economics of constitutional change, edited by Andrew Goudie 2013

vote is currently being considered by groups such as the Scottish Labour Devolution Commission and the Scottish Conservative Strathclyde Commission.

Public spending and the fiscal framework

In the White Paper on independence the Scottish Government argues that, despite being in deficit, Scotland has been in a stronger position in relation to public finances, relative to the UK and states that there will be no requirement for an independent Scotland to raise the general rate of taxation to fund existing levels of spending ([2013](#)).

However, a number of studies have highlighted some factors which may lead to public finance pressures in an independent Scotland. The IFS states that an independent Scotland might want to maintain a stronger fiscal position than the UK, both in order to gain credibility in the financial markets and as preparation for the longer-term fiscal challenges of an ageing population and the eventual inevitable decline of North Sea revenues ([2013](#)). For example, the IFS report on [Government spending on benefits and state pensions in Scotland: current patterns and future issues](#) stated that higher spending on health and social care suggests that demographic change will place a greater burden on Scotland's public finances than it will on Great Britain as a whole (2013).

The IFS report on [Fiscal sustainability of an independent Scotland](#) examined the long-run fiscal pressures that an independent Scotland would face. It concludes that a significant further fiscal tightening would be required in Scotland, on top of that already announced by the UK Government. Its basic model estimates that, without policy action, Scotland would require a permanent tax increase or spending cut equal to 4.1% of Scottish national income to be implemented in 2021-22, to put Scottish public sector debt on course to reach 40% of national income by 2062-63 (2013). Professor David Bell has also warned of a long period of adjustment in an independent Scotland meaning either more taxes or less spending (Scotsman [2014](#)).

In its [reports](#), the Fiscal Commission Working Group puts forward a number of recommendations in relation to public spending and the fiscal framework in an independent Scotland, including:

- The establishment of a short-term stabilisation fund to manage year on year changes in oil and gas tax revenue immediately following independence.
- The establishment of a long-term savings fund immediately following independence to ensure that a proportion of the wealth generated from the taxation of Scottish oil and gas production can be invested for future generations.
- That public finances and the borrowing requirement are planned on the basis of a cautious forecast for oil and gas revenue.

In line with some of these recommendations, in the White Paper on independence the Scottish Government proposes that Scotland sets up an Energy Fund to ensure that future generations benefit from oil and gas reserves (2013). However, in its Scotland Analysis paper on [Macroeconomic and fiscal performance](#) the UK Government highlights that, based on forecasts of Scotland's fiscal position in 2016-17 by the Centre for Public Policy for Regions, for an independent Scotland to start an oil fund in 2016-17 from a balanced budget, additional fiscal consolidation of 5.1 per cent of GDP would be needed. The paper goes on to state that as part of the UK, Scotland achieves many of the benefits of an oil fund: the UK's integrated fiscal model provides a very stable level of Scottish expenditure, without the need for Scotland to run the onshore fiscal position required for an oil fund (2013).

Borrowing and debt

In its [First Report](#), the Fiscal Commission Working Group highlighted that there are no agreed international rules on the division of assets or liabilities in the context of state succession or independence, and there is a lack of clear precedent or consensus. The Group highlights three hypothetical options for managing and servicing Scotland's national debt:

1. Transferring a proportion of UK gilts to the Scottish Government immediately post-independence.
2. Paying an agreed share of debt interest on outstanding debt until maturity then repays the principal, with any new debt issued separately by the Scottish Government.
3. As above, but with the issue of sterling bonds jointly by both Governments (2013).

Under independence, the Scottish Government has stated that it is prepared to negotiate taking on a proportionate share of the UK national debt as long as it receives a proportionate share of assets. The White Paper gives two methods by which Scotland's share of debt might be calculated: apportionment by reference to the historic fiscal balance of public spending and taxation since 1980/81 (the earliest year for which figures are available) or a population share. Under either method an independent Scotland would have a debt to GDP ratio smaller than the rest of the UK's (2013). The White Paper also indicates that the Scottish Government does not envisage that a proportion of UK debt would be legally transferred to Scotland on independence. Instead Scotland would service the share of the debt allocated to Scotland (2013).

A number of other publications have also considered the different ways that the share of debt that Scotland would take on under independence could be both calculated and serviced. For example, NIESR suggest an oil for debt swap to reduce the initial debt burden (2013).

An issue related to the share of debt that an independent Scotland might take on is the cost of borrowing. Commentators have stated that taking on a share of the UK debt would be important for Scotland in building up credibility in the

financial markets. For example Professor Ronald MacDonald warned that if an independent Scotland did not take on its share of UK debt then Scotland would be “paying an even bigger premium on our debt than we would be if we were financing or willing to accept the debt levels which most people agree would be Scotland’s share” (Scotsman [2014](#)).

A NIESR publication considers the wider factors influencing the costs of borrowing that an independent Scotland could face. It finds that if Scotland continues using sterling, it may face additional interest rate costs of between 0.72% to 1.65% above the UK borrowing costs for 10 year debt ([2013](#)). A further publication suggests that:

“If Scotland were to find itself with high debt and interest rates, and in the throes of an already painful austerity drive, and were to face a further adverse shock, then markets might question the commitment to remaining in the monetary union.” (2014)²

It should be noted that the UK Government has committed to in all circumstances honour the debt issued by the UK Government in the event of independence ([2014](#)). It also stated that:

“the full spectrum of assets and liabilities – past, future and contingent – would need to be considered in negotiations between the continuing UK and Scottish Governments, on a case-by-case basis” (2014).

Economic growth

The Scottish Government is critical of the current economic policies for the whole of the UK – stating that they are often heavily determined by the interests of London and the South East of England – not tailored to Scotland’s needs ([2013](#)). The Scottish Government publication [Scotland’s Economy: the case for independence](#) highlights the policy levers which an independent Scotland could use to tackle income inequality, create rewarding employment, counterbalance the gravitational pull towards London and stimulate growth in key sectors (2013). A further publication looking at [Economic Policy Choices in an Independent Scotland](#) suggests that policies under independence could include, among others:

- Boosting competitiveness through the design of a more efficient tax system and the use of carefully targeted tax measures, such as a reduction in corporation tax and the effective use of tax reliefs and allowances to support Scottish businesses
- Using Scotland's new global status to develop growth sectors and growth companies, widen the export base, attract investment, and support local firms to move into new and emerging markets
- Providing the infrastructure required for rural areas to fully participate in economic life through improved communications technology

² p. R19 Scotland: Currency Options and Public Debt in the National Institute Economic Review No. 227

- Creating a genuine partnership approach to developing, and taking forward, economic policy – involving the public, private and third sectors alongside employers and employees (2013).

However, there have also been concerns raised about the impact that independence might have on businesses, in particular in relation to trade. For example, the Scotland Analysis paper published by the UK Government on the [Business and Microeconomic Framework](#) suggests that, in the event of independence, the introduction of an international border would almost certainly have a negative impact on trade. It also states that small companies with little cross-border experience are likely to be hampered most by the creation of barriers to trade and added bureaucracy. It also highlights that different regulatory and tax systems are likely to diverge over time, increasing the barriers to trade on both sides of the border and increasing the cost of compliance for firms who have to comply with two different systems. It concludes that the size and scale of the UK market brings opportunities to trade, move jobs, collaborate to develop new and future technologies, travel and communicate with each other efficiently and benefit from economies of scale (2013). A subsequent Scotland Analysis paper on [Macroeconomic and Fiscal Performance](#) suggests that policy divergence would be expected to trigger a “border effect” reducing flows of trade, labour and capital between Scotland and the continuing UK and leading to reduced levels of real income in the Scottish economy. It goes on to state that an independent Scotland could look to new markets to offset these effects but it is not clear whether this would be able to compensate for the effect on trade flows with the continuing UK (2013).

In relation to the scale of any “border effect” that might be observed, Professor Peter McGregor and Professor Kim Swales highlight:

“It is difficult to know what role the introduction of a more substantial border between Scotland and the RUK would imply for trade. Scotland and England have the same currency and speak the same language, so this barrier might be very low, and it seems inconceivable that any government of an independent Scotland would not wish to encourage trade with the rest of the UK. Also, as we have outlined, Scotland already has a distinctive set of legal and administrative arrangements. If these institutional differences are generally the source of the negative effects of borders on trade, perhaps the relatively small step to independence will have a small impact on Scotland.” (2013)³

Equality

In the White Paper on independence the Scottish Government states:

“Under the Westminster system Scotland is also locked into one of the most unequal economic models in the developed world: since 1975 income inequality among working-age people has increased faster in the UK than in any other country in the OECD. The increasing

³ p.171 Scotland’s Future: the economics of constitutional change, edited by Andrew Goudie 2013

geographical imbalance concentrates jobs, population growth and investment in London and the South East of England, but no action has been taken to address this by successive Westminster governments” (2013).

The Scottish Government states that independence will allow it to have more effective levers to tackle income inequality. Suggested developments for an independent Scotland include:

- Exploring mechanisms to formalise the relationship between Government, employer associations and employee associations.
- Using fiscal incentives to provide employer investment in training and development (2013).

Research by Dr David Comerford and David Eiser at the University of Stirling looks at which policy levers are most effective at tackling inequality. They find that the fiscal policy levers which the Scottish Government already (or will soon) have access to are relatively blunt tools with which to address inequality. They also find that further devolution of income tax (at least to include the ability to vary rates differentially, but potentially also to vary thresholds as well), as proposed by the proponents of Devo-More and DevoPlus, would provide the Scottish Government an opportunity to more effectively use fiscal policy to influence income distribution. But full control over low income and out of work welfare benefits would provide other important levers with which to influence inequality. However, the results presented show that it is difficult for a small open economy to implement substantially different redistributive policy from that of its close partners. Therefore, even with full autonomy for tax and benefit policy, the Scottish Government might need to look beyond fiscal policy and redistribution to achieve the substantial reductions in inequality that it desires (2014). Another publication by Professor David Bell and David Eiser at the University of Stirling finds that there are limits to the extent to which a small open economy can mitigate inequality given that many drivers are linked to global trends in technology, trade and family formation practices (2013).

Scherie Nicol and Greig Liddell
SPICe Research
17 February 2014

Note: Committee briefing papers are provided by SPICe for the use of Scottish Parliament committees and clerking staff. They provide focused information or respond to specific questions or areas of interest to committees and are not intended to offer comprehensive coverage of a subject area.

ECONOMY, ENERGY AND TOURISM COMMITTEE

4th Meeting, 2014 (Session 4), Wednesday, 19 February 2014

LEGISLATIVE CONSENT MEMORANDUM – AMENDMENTS TO THE DEEP SEA MINING (TEMPORARY PROVISIONS) ACT 1981

Note by the Clerk

Background

1. This Legislative Consent Motion (LCM) was laid in Parliament in January 2014. The Parliamentary Bureau referred the LCM to this Committee on 28 January. The Delegated Powers and Law Reform Committee has previously considered this LCM and found the powers conferred on the Scottish Ministers to be acceptable.

Procedure for dealing with legislative consent memorandums

2. Chapter 9B of the Standing Orders sets out the procedures for consideration of an LCM. An LCM must (a) summarise the UK Bill and its policy intentions; (b) specify the extent to which the Bill makes provision to alter the competence of the Scottish Ministers, and (c) outline whether the Scottish Government intends to lodge a motion recommending that the Scottish Parliament gives its consent to the provision, along with the reasons behind this decision.

3. Once lodged, the Parliamentary Bureau refers the LCM to the relevant lead committee; that committee is required to consider the LCM and report its views to the Parliament. A motion is then taken by the Parliament

4. It is usual practice for the Parliament to have expressed a view on an LCM in time for the final amending stage in the House in which the Bill was introduced, i.e. report stage in the Commons or third reading in the Lords.

Views of the Delegated Powers and Law Reform Committee

5. The Delegated Powers and Law Reform Committee published its [report](#) on this LCM on 5 February. An extract from that Committee's report can be found at Annexe B.

Recommendation

6. **The Committee is invited to agree:**

- **whether to recommend that the Parliament approve the draft motion contained in the Legislative Consent Memorandum in Annexe A; and**
- **to delegate to the Convener and Clerk the production of a short, factual report detailing the Committee's considerations and arranging for the report's publication.**

ANNEXE A**LEGISLATIVE CONSENT MEMORANDUM****AMENDMENTS TO THE DEEP SEA MINING (TEMPORARY PROVISIONS) ACT 1981****Draft Legislative Consent Motion**

1. The draft motion, which will be lodged by the Cabinet Secretary for Finance, Employment and Sustainable Growth, is:

“That the Parliament agrees that the relevant provisions of the Deep Sea Mining Private Members Bill introduced to the House of Commons on 19 June 2013, relating to the amendment of the [Deep Sea Mining \(Temporary Provisions\) Act 1981](#), so far as these matters fall within the legislative competence of the Scottish Parliament or alter the executive competence of Scottish Ministers, should be considered by the UK Parliament.”

Background

2. This motion has been lodged by John Swinney, Cabinet Secretary for Finance, Employment and Sustainable Growth under Rule 9.B.3.1(c)(i) of the Parliament’s Standing Orders. The Deep Sea Mining Bill was introduced to the House of Commons 19 June 2013 and amended to extend to Scotland on 15 January 2014. The latest version of the Bill can be found at: <http://services.parliament.uk/bills/2013-14/deepseamining.html>

3. The Deep Sea Mining Bill (“the Bill”), a Private Member’s Bill by Sheryll Murray MP, seeks to amend the Deep Sea Mining (Temporary Provisions) Act 1981 (“the 1981 Act”). The 1981 Act which pre-dates the United Nations Convention on the Law of the Sea (“UNCLOS”), partially implements Part XI of UNCLOS. The 1981 Act requires to be amended to become fully compliant and this is the purpose of the Deep Sea Mining Bill.

4. Part XI of UNCLOS and the 1981 Act concern deep sea mining in that part of marine environment defined as “the Area” in UNCLOS, namely the seabed, ocean floor and subsoil thereof, beyond the limits of national jurisdiction. It accordingly concerns activities beyond our fishing limits and Scottish waters.

5. Deep sea mining is, generally a devolved matter although as the Bill seeks to amend the 1981 Act to provide that all types of minerals may be mined where this may include coal or gas it would, in those cases, be a reserved matter.

6. Amending the Bill offers potential growth opportunity for Scottish companies. Companies wishing to mine the sea bed for minerals need to be licensed under national law. Access to the international resource is governed by the International Sea Bed Authority (“the ISA”), established under UNCLOS

7. The 1981 Act sets down the licensing regime in the UK concerning deep sea mining in “the Area”. Under UNCLOS a person may apply to their national authority (or “State Party”) for a licence to carry out deep sea mining in a specific region of ‘the Area’. The State Party, upon issuing a licence, then sponsors their application to the ISA for a contract to mine that region.

8. The Bill when presented in the House of Commons extended only to England, Wales and Northern Ireland. The 1981 Act extends to the whole of the UK. There have been exchanges and discussions between the Foreign and Commonwealth Office and the Scottish Government which have concluded that the Bill should be extended to Scotland and amendments to that effect have been tabled in the UK Parliament.

Content of the Bill

9. The updates to the 1981 Act implement in full UNCLOS to include widening the scope of mineable material covered by the Act, which currently only apply to polymetallic nodules, to all types of minerals, no matter their form (ie solid, liquid or gaseous form).

10. The Deep Sea Mining Bill will amend the 1981 Act to:

- Give effect to Part XI of UNCLOS providing that companies wishing to undertake deep sea mining must enter into a contract with the ISA before exploring or exploiting the mineral resources of the deep sea bed.
- Extend coverage of the 1981 Act from hard mineral resource to mineral resources of any form.
- Authorise, in Scotland, the exploration and exploitation for the mineral resource in a specified part of the Area.
- The Bill once amended will apply to UK nationals, Scottish firms or bodies incorporated under UK law and residents of any part of the UK and which could also be extended by Order to persons outside the UK (the Channel Islands, the Isle of Man or any colony).

Provisions which relate to Scotland

The following paragraphs describe the specific provisions for which consent is sought.

Clause 2 of the Bill - extent, commencement and short title

11. Policy Intent: The Scottish Government is seeking to update the regulatory framework to extend the functions of the Scottish Ministers by providing that they are the competent authority for considering Scottish applications to mine a wider range of minerals than is currently the case.

12. Background: The existing functions under the 1981 Act which were exercisable by the Secretary of State were transferred so as to be exercisable by the Scottish Ministers within devolved competence by virtue of section 53 of the Scotland Act 1998 instead of by the Secretary of State. Subject to the agreement of the

Parliament on the LCM, the Bill will be amended to extend to Scotland to provide that the Scottish Ministers are to exercise the functions of the Secretary of State that are being added to or modified by the Bill so far as the exercise of those functions would be within devolved competence (within the meaning of the Scotland Act 1998).

13. If the Bill were not extended to Scotland then the legislation applying to Scottish companies with an interest in deep sea mining would be out of step with international law. Furthermore, if that was the case then Scottish companies would only be able to apply for licenses to mine from the sea bed only those minerals which are in a solid form, and not such minerals in gaseous or liquid states.

14. Modernising the legislation will provide international agreement to avoid conflict over deep sea mining areas; and extend coverage of the scheme from hard mineral resource to mineral resources of any description (ie solid, liquid or gas).

Schedule to the Bill – amendments to the Deep Sea Mining (Temporary Provisions) Act 1981

15. Policy intent: the Bill seeks to ensure that companies seeking to exploit all types of mineral resources of the deep sea bed in the Area obtain licences from the Secretary of State, or where it is within the devolved competence of the Scottish Ministers, authorising that activity which is also regulated by the ISA in line with UNCLOS.

16. Background: Companies wishing to mine the sea bed for minerals in the Area need to be licensed under national law - the 1981 Act sets down the licensing regime. The Act partially implements UNCLOS, but requires amendment to become fully compliant. Under UNCLOS a person may apply to their national authority (or “State Party”) for a licence to carry out deep sea mining. The State Party, upon issuing a licence, then sponsors their application to the ISA for a contract to mine that part of the Area. In order for the 1981 Act to be made compliant with UNCLOS across the UK. Amendments to the Bill have been tabled extending its application to Scotland, in order to:

- Ensure that exploration and exploitation deep sea mining licences are only valid if there is a contract between the ISA and the Licensee.
- Ensure that exploring or exploiting minerals requires an exploration or exploitation licence which states the type of mineral to be explored or exploited and the area of the deep sea bed that is to be explored or, as the case may be, exploited.
- Provide that the Scottish Ministers may on payment of a fee grant a exploration or exploitation licence.
- Provide that the Scottish Ministers may grant a licence subject to such terms and conditions as they think fit, including the protection of the environment, health and safety, treatment of minerals, disposal of waste requiring plans or samples.
- Provide that where the Secretary of State or the Scottish Ministers have granted an exploration licence then they may not grant an exploitation licence in relation to any part of the licensed area to which the exploration licence has been granted or to any of the mineral resources

to which that licence relates unless the exploitation licence is granted to the holder of the exploration licence, or with that person's written consent.

- Provide that, where required, the Scottish Ministers may vary or revoke any exploration or exploitation licence.
- Provide that the enforcement of decisions of the Seabed Disputes Chamber of the International Tribunal for the Law of the Sea ("the Tribunal") may be registered in the Court of Session for enforcement and applies the Arbitration (Scotland) Act 2010 to disputes between the ISA and contractors.
- Provide that if a person had a licence under the 1981 Act or held a contract issued by the ISA and if that person acted in pursuance of that licence or contract then the provisions of Part 4 of the Marine (Scotland) Act 2010 or Part 4 of the Marine and Coastal Access Act 2009 should not apply to that activity. The 1981 Act, as unamended, provides such an exclusion in relation to Part 2 of the Food and Environment Protection Act 1985 and that exclusion remains in place under the Bill. This avoids the person from having to comply with two (or more) licensing regimes.

Consultation

17. Given that this is a non-contentious technical change to better implement existing Treaty obligation, detailed consultation with stakeholders has been thought unnecessary. The provisions are being taken forward by means of a Private Members Bill.

Financial implications

18. We would not anticipate a significant change following the new legislation coming into force. Agreeing to the LCM will result in the extent of the Bill applying to Scotland without the need to consider enacting our own legislation.

19. Amending the Bill offers potential growth opportunity for Scottish companies. Companies wishing to mine the sea bed for minerals need to be licensed under national law. We do not expect any practical consequences in the short term because of the extreme challenges involved in initiating a deep sea mining operation – our approach is sensible and pragmatic, agreeing to the changes but preserving the responsibilities devolved to us.

Conclusion

It is the view of the Scottish Government that it is in the interests of Scottish business and good governance that the relevant provisions outlined above which fall within the executive competence of Scottish Ministers or legislative competence of the Scottish Parliament, should be considered by the UK Parliament.

Scottish Government

January 2014

ANNEXE B**EXTRACT FROM THE REPORT BY THE DELEGATED POWERS AND LAW REFORM COMMITTEE****Paragraph 3(3)(b) of the Schedule to the Bill – power to prescribe the level of fee payable upon application for a licence**

Power conferred on: The Scottish Ministers
Exercised by: Regulations
Parliamentary Procedure: Negative

The Deep Sea Mining Bill amends the Deep Sea Mining (Temporary Provisions) Act 1981 (“the 1981 Act”) to bring UK law in line with provisions regulating mining on the deep sea bed under the United Nations Convention on the Law of the Sea (“the Convention”).

The Bill amends section 1 of the 1981 Act so that a person may not explore for or exploit mineral resources in the deep sea bed, unless they hold an exploration or exploitation licence. The licence must relate to mineral resources as described in the licence and to that area of the deep seabed. It is now possible for a licence to be given to explore for or exploit different mineral resources in the same area of the seabed.

The new definition of “mineral resource” includes liquid or gaseous minerals. The change is necessary because the 1981 Act covered only the mining of hard polymetallic minerals.

Section 2 of the 1981 Act, as amended by the Bill, sets out provisions relating to the granting of licences and the terms and conditions of any licence granted. The section confers power on the Scottish Ministers to prescribe, by regulations, the level of the fee payable upon application for a licence.

The power in the new section 2(2)(b) (inserted by paragraph 3(3)(b) of the Schedule to the Bill) enables the Scottish Ministers to make provision, by regulations, as to the level of fee to be charged upon an application for a licence.

Paragraph 3(4) of the Schedule – power to prescribe sums to be paid under a licence, and prescribe cases in which a transfer of a licence is permitted

Power conferred on: The Scottish Ministers
Exercised by: Regulations
Parliamentary Procedure: Negative

The Bill inserts a new subsection (3A) in section 2 of the 1981 Act. This provides that a licence may contain such terms and conditions as the Scottish Ministers think fit including, in particular, the terms and conditions set out in that subsection. This provision broadly replaces a similar provision in the 1981 Act, with the addition of several new terms and conditions which can be included in a licence. The terms and

conditions which may be included in a licence are set out in new subsection 3A(a) to (m).

Under sub-paragraph (l) the Scottish Ministers can include a provision in a licence, requiring payment to the Scottish Ministers of such sums as may be prescribed, at such times as may be prescribed. Under, sub-paragraph (m), Ministers can include a provision in a licence permitting the transfer of the licence in prescribed cases.

The powers in new section 2(3A)(l) and (m) are inserted by paragraph 3(4) of the Schedule to the Bill. Section 2(3A)(l) allows the Scottish Ministers to prescribe the nature and amount of any payments due under a licence and when those payments fall due. Section 2(3A)(m) confers power on the Scottish Ministers to prescribe the cases in which a licence can be transferred.

Paragraph 11 of the Schedule to the Bill – power to prescribe functions of inspectors

Power conferred on: The Scottish Ministers

Exercised by: Regulations

Parliamentary Procedure: Negative

Section 11 of the 1981 Act (as amended by the Bill) confers powers on the Scottish Ministers to appoint inspectors and prescribe their functions, in order to ensure compliance with the Act and the licences granted under it.

The power in section 11(1) (as amended by paragraph 11 to the Schedule of the Bill) enables the Scottish Ministers to prescribe the functions to be discharged by inspectors.

Paragraph 12 of the Schedule to the Bill – power to make regulations generally for carrying the 1981 Act into effect

Power conferred on: The Scottish Ministers

Exercised by: Regulations

Parliamentary Procedure: Negative

Section 12(2) as amended by paragraph 12 of the Schedule confers power on the Scottish Ministers to make regulations generally for carrying the 1981 Act into effect. In particular, regulations may make provision with respect to any matters mentioned in the Schedule to the 1981 Act. The Schedule includes matters relating to the form and content of licence applications, health and safety, prohibited methods of working, inspectors and the creation of offences under regulations.

The Ministers also have power to prescribe anything required or authorised to be prescribed under the Bill, in relation to an exploration or exploitation licence granted or to be granted by the Ministers (new section 12(2)(a)).

Equivalent powers are conferred on the Secretary of State, in new section 12(1).

The Committee reports that it finds powers conferred on the Scottish Ministers in paragraph 3(3)(b) and (4), and paragraphs 11 and 12, of the schedule to the Bill to be acceptable, and to be content that they are subject to the negative procedure.