



The Scottish Parliament
Pàrlamaid na h-Alba

DEVOLUTION (FURTHER POWERS) COMMITTEE

AGENDA

6th Meeting, 2014 (Session 4)

Thursday 11 December 2014

The Committee will meet at 10.00 am in the David Livingstone Room (CR6).

1. **The Smith Commission:** The Committee will take evidence from—

Professor David Bell, Professor of Economics, University of Stirling;

Professor David Heald, Professor of Accountancy, University of Aberdeen Business School;

Professor Nicola McEwen, Associate Director, ESRC Centre on Constitutional Change;

Professor Charlie Jeffery, Professor of Politics, University of Edinburgh;

Professor Michael Keating, Professor of Politics, University of Aberdeen.

Clerk to the Devolution (Further Powers) Committee
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The papers for this meeting are as follows—

Agenda item 1

Written submissions of evidence

DFP/S4/14/6/1

PRIVATE PAPER

DFP/S4/14/6/2 (P)

Devolution (Further Powers) Committee

Academic Evidence Session - Suggested Areas of Questioning

Background

This paper provides the written evidence that has been submitted by witnesses at the evidence session on 11 December 2014. Written evidence has been received from:

- Professor David Heald
- Professor Charlie Jeffery
- Professor Michael Keating
- Professor Nicola McEwen, and
- Professor David Bell

Members should note that Professor Heald's evidence is in the form of two separate papers that he had previously provided as written evidence to the Finance Committee. The written evidence was provided to the Finance Committee for their meetings on 25 June 2014 and 5 November 2014.

**Clerking Team
Devolution (Further Powers) Committee
5 December 2014**

WRITTEN SUBMISSION TO FINANCE COMMITTEE – 25 JUNE 2014**WRITTEN SUBMISSION FROM PROFESSOR DAVID HEALD¹****THE BARNETT FORMULA WITHIN THE DEVOLVED FINANCING SYSTEM****Introduction**

1. I have a longstanding interest in the public finances of Scotland: in 1976 I proposed what later became the tartan tax; in 1980 I named the Barnett formula when knowledge of its existence first came into the public domain; in 1990 I contributed to the debates stimulated by the Scottish Constitutional Convention; and in 2008 I supported the Canadian-style tax-points transfer that was included in the Calman Commission Report. This personal background is relevant to the exposition below on the issues that must be addressed if extended taxation powers are to be successfully operated by a devolved Scottish Parliament. My invitation to give evidence to the Committee explicitly asked me to address the Barnett formula: there is no discussion here of Independence as there would no longer be grants from the UK Government.

2. The Referendum constitutes a critical juncture in Scottish public finances, even if the result is No. The status quo of 1999 is rarely defended, with party competition on the No side on how far-reaching tax proposals can now be. Expectations have been aroused inside Scotland for a 'better devolution deal', while – temporarily in my view – the voices outside Scotland that denounce its 'excessive privileges' are relatively subdued. Squaring the circle between 'better deal' and 'worse deal' will prove difficult, particularly in relation to (a) the practical operation of devolved tax powers, and (b) the grant system. It must also be remembered that Wales and Northern Ireland are important players, both in terms of looking enviously at Scotland and in terms of wishing to emulate Scottish constitutional and financial arrangements.

How Barnett Works

3. What is remarkable is how much misunderstanding and/or misrepresentation there is of the Barnett formula, and how that has gone uncorrected because of inadequate transparency. It is an adjustment formula, not a needs formula as is sometimes claimed. Changes in expenditure in England on services that are devolved to Scotland lead to changes – positive or negative – in the Scotland Departmental Expenditure Limit (DEL), after weighting for population ratios and comparability percentages. Because the expenditure base per capita is higher than in England and increments are equal amounts per capita, increases in public expenditure will lead to (slow) convergence towards England per capita expenditure = 100. If expenditure falls, there would be divergence. There has been much less convergence since 1979-80 than would be predicted given the mathematical

¹ Professor of Accountancy at the University of Aberdeen.

properties of the formula (Heald, 1994): this is primarily a result of Scotland's *relative* population fall, but also of other factors discussed in Heald and McLeod (2005).²

4. There have been three emphatic advantages for Scotland. The first is the expenditure-switching discretion, originally of the Secretary of State for Scotland before 1999 and of Scottish Ministers since then. The second is the protection that this adjustment mechanism gives to policy discretion within Scotland. Unlike for UK departments responsible for England, central departments like the Treasury and Cabinet Office cannot probe the detail and disallow 'undesirable-in-their-eyes' expenditure. The practical advantage to the Treasury is that a mechanical formula has allowed the expenditures of Scotland, Wales and Northern Ireland to be settled, very quickly, after decisions have been taken on the much larger English programmes. Third, the existence of the formula protected the budgets of the Devolved Administrations from Treasury 'raids', perhaps conducted without public disclosure.³

5. On the basis of what is in the public domain, my assessment is that the Treasury has generally abided by the spirit and letter of the funding rules.⁴ Heald and McLeod (2002) set out how Barnett could be modified, in ways that might assuage concerns expressed in Wales and Northern Ireland. However, the Labour Government closed down debate on the topic at a time when public spending was increasing rapidly and modifications could have been done relatively painlessly. Criticisms of within-England distribution have been channelled against the Barnett formula, though that has no direct relevance.

6. Table 1 summarises the operation of the Barnett formula since the 2010 UK general election, with reference to the present year (2014-15). It reinforces two points. First, the Barnett formula is deeply embedded within the UK public expenditure system over which the Treasury has unchallenged power. The CSR2010 baseline for the 2014-15 Scotland DEL (£28,245 million) evolved through UK spending announcements to the 2014-15 Revised budget, net of depreciation (£28,683 million). Cumulatively the net Barnett formula consequentials (plus £113 million) were a modest component of this transition. For 2014-15, the Barnett reduction in SR2010 (£508 million) was more than offset by positive consequentials from subsequent spending announcements.

7. A much larger effect on the total DEL came from Machinery of Government changes and Baseline transfers (plus £367 million). Moreover, there is a £607 million reduction from the 2014-15 DEL (as at June 2013), reversing 'temporary' Barnett consequentials and one-offs, to reach the SR2013 baseline for 2015-16 (£27,920

² These included formula by-pass in the 1980s (usually beneficial to the then Territorial Departments), the transfer of functions, and classification and accounting changes.

³ See the *Herald* report on 3 January 2014 headed 'Thatcher minister wanted to secretly cut millions from Scotland's funding – Papers reveal row centred on saving cash and political fall-out' (Settle, 2014). The occasion was the release of documents at the National Archives under the 30-year rule.

⁴ The documented exceptions are now relatively old, relating to the treatment of the Olympics and to the implementation costs of the Carter Review of Prisons. The latest *Statement of Funding Policy* (Treasury 2010) is located at: http://webarchive.nationalarchives.gov.uk/+http://www.hm-treasury.gov.uk/d/sr2010_fundingpolicy.pdf. This was not updated at Spending Review 2013, contrary to customary practice, possibly on the argument that SR2013 (covering only 2015-16) was an extension of CSR2010.

million). There is no provision in the Statement of Funding Policy for such a step, nor a distinction there between ‘temporary’ and ‘permanent’ consequentials. Table 1 reinforces the point that the Treasury has much discretion. There is a transparency deficit that is undesirable now and – unless removed – would make major devolved taxes unworkable.

Table 1: 2014-15 as Illustration of evolution of Scotland DEL from CSR2010 to Budget 2014

	£ million	
	2014-15	2015-16
Baseline for CSR2010	28,245	
Cumulative Barnett consequential	113	
Machinery of Government changes and Baseline transfers	367	
Budget regime changes	12	
Forth Replacement Crossing prepayments	(52)	
Rounding error	(2)	
Revised budget, net of depreciation (March 2014)	28,683	
Revised 2014-15 budget, net of depreciation (June 2013)		28,527
SR2010 baseline adjustment		(607)
SR2013 baseline		27,920

Source: Successive Scottish Government responses to Freedom of Information requests

8. Second, the feast of Barnett consequentials in the early and mid 2000s reflected a surge in spending on health and education in England. Large reductions since June 2010 to English programmes were partially offset by large increases in health. During the period June 2010 to March 2014, there were ten UK spending announcements.⁵ The effect on the Scotland DEL clearly depends on UK Government decisions about whether comparable or non-comparable programmes will be cut.

9. Despite all the criticism, from within Scotland about the so-called ‘Barnett squeeze’ and from outside Scotland of its higher per capita expenditure, the system has survived for more than 30 years because:

- a) There has been no compelling support for an alternative, particularly a UK-wide needs assessment;
- b) The expenditure-based financing system, with broad expenditure-switching powers, is congruent with the reality of the UK public expenditure system; the 16% of the population living in the Devolved Administrations were sufficiently

⁵ These ten UK spending announcements were: June 2010 Budget; CSR 2010; 2011 Budget; Autumn Statement 2011; 2012 Budget; Autumn Statement 2012; 2013 Budget; SR2013; Autumn Statement 2013; and 2014 Budget.

marginal to UK political debates for some spending legacies and policy deviancy to be tolerated at Westminster and Whitehall; and

- c) Since 1997, there has always been a Scottish MP of Cabinet rank at the Treasury and this has protected Scotland's political clout. There is generalised hostility to the Barnett formula in Whitehall and Westminster, on the basis of what is perceived as excessive levels of public expenditure in Scotland and Northern Ireland.⁶

The Implications of Extra Tax Powers

10. The continued lack of transparency post-devolution was tolerated in the context of much more money flowing down the Barnett pipeline in the early and mid-2000s. A pre-condition of the exercise of significant tax powers is that there is full transparency about the funding system. Otherwise, the tax powers will become unusable, subjected to mockery, vulnerable to gaming by the UK Government, and to disintegration of the administrative infrastructure for assessment and collection. Heald and Geaughan (1997) voiced fears of such a fate for the tartan tax, though – in the event – non-use owed much to unabsorbable increases in Barnett funding that went partly into the build-up of End-Year Flexibility.

11. There are undoubted advantages when democratically elected bodies have some of their expenditure covered by tax revenues under their control. However, this is easier to say than to sustain in a highly centralised political system such as the United Kingdom. Raising 'own revenues' cannot legitimately mean receiving the revenues generated in a sub-national jurisdiction through the application of a centrally-set tax rate to a centrally-prescribed tax base. This creates no political accountability: they are 'assigned revenues', even if not labelled as such. Moreover, without some form of revenue equalisation, there will be large variations in revenues per capita across jurisdictions, and substantial year-to-year revenue volatility. To count as own revenues, there has to be at least sub-national control of the tax rate, possibly within prescribed limits: these can legitimately be labelled as 'own tax revenues'. Otherwise, there will be shifts in the location of fiscal risks (eg revenue oscillations) and policy risks (eg UK government changes to the tax structure to the detriment of sub-national revenues) in ways which are damaging to public expenditure management and to political accountability. Arguably the worst of all worlds is when devolved tax powers are not usable: it will not take long before the talk of 'enhanced accountability' is discredited. Therefore, the design of the grants system and the adopted rules about devolved borrowing and saving become decisive. Otherwise, the Barnett formula system's high level of predictability of capacity to spend will be lost, without off-setting benefits. Since 1999 this predictability has been enhanced by periodic Spending Reviews every two or three years, rather than the pre-1998 system of annual Public Expenditure White Papers.

12. Four observations about political context are highly relevant:

⁶ Commentary on spending differentials per head usually refers to the territorial analysis tables in the annual *Public Expenditure: Statistical Analyses* (Treasury 2013). However, these figures include UK Government expenditure in Scotland and are influenced by other factors than the Barnett formula. Heald (1994, pp. 170) called for the regular publication of 'English equivalent expenditure' (ie that expenditure that drives Barnett increases or decreases). Twenty years later this has still not happened.

- a) The Devolved Administrations wish to spend more per head than does the UK Government in England, in part reflecting historical legacies and in part divergent views about the size and scope of the public sector;
- b) A striking feature of the last 30 years has been the weakening of local government across Great Britain,⁷ in terms of loss of functions and of discretion in local taxation. The arguments for own tax-raising no longer seem to be applied to local authorities, from which much financial discretion has been removed either by legislation or grant design;
- c) Notwithstanding (a) above, much contemporary discussion relates to the possibility of taxes being lower than in England, particularly but not exclusively in relation to Corporation Tax and Airport Passenger Duty. Tax-varying powers would be more difficult to operate in Wales because of population proximity to the border with England, and Northern Ireland has the complication of a 220-mile land border with Ireland. Moreover, while Scotland and England are economically quite similar in terms of prosperity, both Wales and Northern Ireland have much lower taxable capacities, meaning that whether there is tax-base equalisation becomes salient in the way it does not for Scotland alone. The Government of Ireland Act 1920 system of financing for the Stormont Parliament disintegrated because of 'parity'. If Northern Ireland broadly followed UK taxes, then some of its resource shortfall would be non-transparently funded by Westminster; and
- d) Claims that lower tax rates would be self-financing through higher economic growth should always be treated with suspicion.

13. If more extensive taxation powers are not to be mere window-dressing at substantial cost (ie parity is always maintained but the tax infrastructure must always be in place), the following issues must be addressed:

- a) The administrative infrastructure must work to a very high standard and there must be effective enforcement of, for example, tax residence rules for Scottish taxpayers;⁸
- b) Changes are required to the way in which the UK Government sets taxation policy. Many of these would be beneficial to the United Kingdom (Heald, 2012), but that is no guarantee that they will be forthcoming. Specifically, the discretionary timing of the UK Budget just before the beginning of the tax year on 6 April, will create difficulties for the Scottish Government which has to notify HMRC of the Calman tax rate by 30 November of the preceding year,⁹

⁷ The circumstances of Northern Ireland are different, as the removal of powers in 1973 was connected to the Troubles. Reorganisation and centralisation of key functions followed the 1970 report of the (Macrory) Review Body on Local Government in Northern Ireland.

⁸ Alarmingly, the HMRC will not give priority to verifying taxpayer declarations of residence between the countries of the United Kingdom; further work would be rechargeable to the Scottish Government (Scottish Government and HM Revenue & Customs, 2013, para 3.14). This is critically important because (a) unlike the tartan tax, the Calman tax has no upper limit on liability; and (b) some of the highest-income Scottish taxpayers may have homes in more than one UK country.

⁹ See Appendix B of Scottish Government and HM Revenue & Customs (2013). It stretches credulity to believe that this tax decision could be kept confidential for long after this date.

without knowledge of what will happen to UK-wide tax thresholds and tax bands or to tax rates for those UK residents who are not Scottish taxpayers. The potential for game-playing by the UK Government is self-evident;

- c) The grant system, which could be a Barnett-type adjustment mechanism or based on a needs assessment, must be transparent and accessible. There must be no appearance or fact of the grant being reduced as punishment for an increase or decrease in a devolved tax rate relevant to that applying in England (or the rest of the United Kingdom, as appropriate).¹⁰ This provision is vital because a perceived constraint on the Scottish Government using the tartan tax power in a downwards direction during the expenditure feast of the early and mid-2000s was the fear that the Treasury would then open up the Barnett formula, not necessarily making those steps public;
- d) For tax powers to work, there must be explicit reporting on an annual basis, with standardised updates whenever there are changes, so that devolved finances can be followed in real time; and
- e) The relationship between the devolved taxation system and social security is critical, both in terms of system functioning and political credibility.

Beyond the Barnett Formula?

14. Fantasy numbers have become pervasive in the Referendum debate, with the impression being given that austerity can be forgotten. Two frightening numbers appear in Institute for Fiscal Studies briefings on UK public finances. First, at the end of 2013-14, only 49% of planned austerity had been done. Second, real-terms age-adjusted per capita NHS expenditure in England is projected to fall by 9.1% from 2010-11 to 2018-19, despite the 'protection' it has so far received.

15. There has been no published UK-wide needs assessment since 1979, in which year was published the 1978 exercise that predated the intended implementation of the Scotland Act 1978 and the Wales Act 1978. Some internal exercises within the UK Government have never been published. At devolution in 1999, it seemed inevitable that, sooner or later, there would be an official exercise, though circumstances led to that not happening. If there were to be one post-Referendum, the main alternatives are an Australian-type detailed needs assessment (which would be comprehensive and expensive) or a simplified one (which would use a limited number of needs indicators). The other question is whether such an exercise would be buried inside the recesses of government (eg Treasury-led, with or without Devolved Administration participation), or conducted at distance from governments by some public body (eg a UK-wide Territorial Exchequer Board).

16. One of the by-products of the Holtham Commission Report on devolution finance in Wales is the proposal by two of its three members that the Scotland budget should be cut by £4 billion (Holtham and Miles, 2010). This calculation is based on applying their 'simple' needs assessment formula across the United Kingdom: on that basis, Wales is underfunded whereas Scotland and Northern

¹⁰ Some grant designs might have grant dependent on local tax effort: however, the issue here relates to 'off-system' changes to the grant made by the UK Government.

Ireland are overfunded. The calculated needs indexes (England = 100) were Wales (115), Scotland (105) and Northern Ireland (121) (Independent Commission for Funding & Finance for Wales, 2009). It is clear that there would have to be transitional arrangements should a new needs assessment generate such numbers. Without a formal needs assessment, one option that might appeal to a UK Government would be to fund the Devolved Administrations on the basis of the distribution formulae in use for internal distribution within England. This would embody UK priorities for England in terms of the scale and scope of public service provision, as well as importing into devolved funding the political fixes made for England. A second-round effect is likely to be that the UK Government would make reference to the implied needs weights embodied in lower-level distribution formulae used within each of the Devolved Administrations. This would possibly lead to pressure to mimic internally the needs formula underlying the block grant. In a political climate of low trust in official numbers, the scope for potential conflict is obvious: between the UK Government and the Devolved Administrations; between the Devolved Administrations themselves; and between prosperous and less prosperous parts of the devolved countries about 'pass-through' and the extent of internal equalisation.

17. More devolved taxes will mean that the block grant is smaller but its role will remain critical. If such a system is to work, there must be explicit constitutional architecture with far-reaching implications for the rest of the United Kingdom. For example: the UK budgetary timetable must be pulled forward; there has to be less opportunity for political theatre on the part of UK Chancellors of the Exchequer, necessitating constraints on Treasury power; and rules of engagement have to be devised that protect the UK Government and Devolved Administrations from gaming, probably in the form of internal fiscal rules. The Scottish Government would have to be ready for extremely tough financial negotiations.

Conclusion

18. Paradoxically, to make devolution finance work better it is not the Devolved Parliaments/Assemblies/Governments that must change most but the UK Parliament and Government. Otherwise the income tax powers are likely to lead to parity, as any change by a Devolved Administration is vulnerable to countering – whether on thresholds, bands and rates – by the UK Government. Within the context of the United Kingdom's membership of the European Union, which imposes constraints on Corporation Tax and VAT, income tax is the appropriate basis for the main devolved tax. However, without appropriate constitutional machinery on intergovernmental financial relations, it would be possible for a UK Government to subvert the financial arrangements, for example, by significantly reducing income tax rates in England while increasing VAT.

19. An important point to stress is that such reforms could also bring benefits for much of England, within which economic imbalances are severe. This can be seen in controversies about whether London and the wider South East is a fiscal ATM for other parts of the United Kingdom or whether its dominance sucks life out of elsewhere. The economic imbalances within England and the dominant size of England within the United Kingdom greatly complicate fiscal decentralisation and influence the ensuing political controversies.

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WRITTEN SUBMISSION TO FINANCE COMMITTEE – 5 NOVEMBER 2014

Memorandum by Professor David Heald¹¹ to the Finance Committee of the
Scottish Parliament

THE FUTURE FINANCING OF THE SCOTTISH PARLIAMENT

INTRODUCTION

1. The Committee's invitation to submit evidence lists six questions that witnesses should address. Each of these is considered in sections below. As these questions mostly refer to devolved taxes, this 'Introduction' places those in the broader political, constitutional and economic context. In June 2014 I provided both written and oral evidence (Heald, 2014b) to the Committee and, except where essential, I will not repeat such material.
2. The Scottish Independence Referendum provides the context for these discussions. Clearly momentum has built up that 'something dramatic' must be seen to be done, otherwise disenchantment is a likely response. A political auction has developed as to whose taxation proposals are the most far-reaching. Two cautions are vital: first, that some of the taxation issues are highly technical and poorly understood; and, second, that there are conflicting political objectives – making 'a New Union' (Jones, 2014) that will be durable, and demonstrating that nothing short of Independence will work.
3. Several issues are analytically distinct but in practice become interconnected:
 - a) **Whether all parts of the United Kingdom have access to the UK resource pool and can make claims based on territorial needs.** As well as the case for decentralisation within a state based on democratic accountability, decentralisation can be argued as a way of reducing the size of the state, by way of tax competition. The standard public finance argument is that redistribution is more effective when undertaken at the highest available level of government, but this runs into difficulty if political preferences about redistribution diverge across the state.

¹¹ Professor of Accountancy at the University of Aberdeen.

- b) **Which level of government decides the size of the state.**¹² Both sides of the Referendum debate seemed to want to spend more. On the Yes side, this would be financed by the growth and productivity gains it was claimed Independence would bring. On the No side, there was inadequate recognition of the United Kingdom's existing fiscal deficit and of the present UK Government's plans to reduce 'public service spending' to its lowest level since 1948 (Johnson, 2014b). I have been an advocate of (partial) income tax devolution since 1976 (Heald, 1976), but recognise there are limits on the extent to which Scotland could levy personal tax higher than elsewhere in the United Kingdom. Decisions made at Westminster remain profoundly important for Scotland, whether there is sharing of the income tax base or if Scotland's income tax is standalone. The UK Government will not allow Scotland (or Wales or Northern Ireland) to erode its own tax base and the Treasury will have retaliatory instruments.
- c) **Whether the devolved finance system remains expenditure-based or whether there is a significant move to make it more revenue-based.** If a system is expenditure-based, judgements – implicit or explicit – are taken as to the level of spending in each jurisdiction that the collectivity will support. If a system is revenue-based, the level of public spending will depend on the taxable capacity of jurisdictions, with implications for the standards of public services and for internal migration. This is best seen as a spectrum rather a dichotomy. A UK-specific difficulty is that England represents 84% of the UK population and 87% of the GB population. At the first modern census in 1801, England accounted for 74% of the GB population. This dominance of England, likely to increase through time, makes it difficult to design

¹² The controversy during the Referendum campaign about the future of the National Health Service (NHS) was confused. Since 2010, there have been strongly positive Barnett formula consequentials from increases in health spending in England, alongside large negative consequentials from other programmes. The Scottish Government has used its expenditure-switching discretion, for example, to mitigate the effects on local government services. Although the Scottish Government exercises legislative and political control over the NHS in Scotland, the overall level of funding for public services in Scotland is primarily determined by UK decisions.

conventional federalism-type financial relationships within the United Kingdom.

- d) **Where the fiscal risks sit.** The United Kingdom is of sufficient size that it pools risks more effectively than Scotland could alone, for example in relation to economic activity in, and tax payments from, the oil and financial sectors. On a strict revenue basis for devolution financing, Scotland would be exposed to fiscal risks, while lacking the policy instruments to manage such risks. This is a caution against assuming that devolution is necessarily enhanced by taking on all taxation powers that would have come with Independence.
4. In relation to what a good tax system would look like, there are marked differences between ‘expert’ and ‘popular’ views (Lim *et al*, 2013). These create difficulties for policymakers because popular views place little weight on neutrality (a key concern of reports such as Mirrlees (2011)) and tend to focus on single taxes rather than the effects of the tax system as a whole.

QUESTION 1: WHAT GENERAL PRINCIPLES SHOULD APPLY TO THE DEVOLUTION OF FURTHER FINANCIAL POWERS TO THE SCOTTISH PARLIAMENT?

5. There is extensive discussion of relevant criteria in the report of the Expert Group to the Calman Commission (Muscatelli, 2008).
6. **On the issue of devolved taxation**, the particular points I wish to stress for this meeting are:
- a) That the use of devolved tax powers, whether relating to tax rate or tax base, must be credible. Otherwise substantial administrative and compliance costs will be incurred, only for devolved Scottish taxes to remain identical to UK ones. There were specific reasons¹³ why the tartan tax was never used: the power became effectively unusable when the Scottish Government took the unannounced decision in 2007 to let the 10-month HMRC readiness period to lapse (Scotland Office, 2010).

¹³ So much money came down the Barnett pipeline during the 2000s as consequential from increased health and education expenditure in England that all three Devolved Administrations built up End-Year-Flexibility; and Scottish Ministers were advised that use of the downwards variation of tartan tax would lead to the Treasury challenging the level of the block grant.

- b) That what matters is ‘fiscal accountability at the margin’ (ie the ability to vary taxes) (Blow *et al*, 1996) and not the proportion of expenditure financed by taxes levied in Scotland if those decisions are not taken by the Scottish Parliament (ie revenues generated in Scotland on the basis of UK decisions). Raising 54% of revenues (*Guardian*, 2014) does not improve accountability or enhance discretion if powers to vary do not exist or are not usable.
- c) That tax devolution (or the assignment of tax revenues) means that extensive borrowing powers are required in order to manage year-on-year fluctuations in revenues (see response to Question 4).
- d) That consideration should be given to how powers made available to Scotland might later be extended to Wales and Northern Ireland, perhaps in modified form. This may not seem important in Scotland in the aftermath of the Referendum, but the durability of arrangements is more likely when all three countries have stakes in the arrangements.¹⁴
- e) That while the United Kingdom remains a member of the European Union (EU), there are legal constraints on within-Member-State variation that affect both VAT and Corporation Tax.¹⁵
- f) That there should be no detriment to other parts of the United Kingdom. This is easier to state as a general principle than to operationalise. Examples are tax incentives to induce re-location of high income individuals over internal borders or to divert air passengers. As international examples of tax arbitrage demonstrate, the dangers of a ‘race to the bottom’ should not be underestimated. This should rule out devolution of those taxes where the only motivation for securing them is to reduce/abolish them.
- g) That urgent attention is required to local government taxation: there has been no council tax revaluation since 1991 and this is the seventh year of council tax freeze. Revaluation may be feared as politically toxic and council tax freezes

¹⁴ Scotland tends to be sufficiently close to the UK average that tax base equalisation is likely to be unnecessary. That is not the case for Wales and Northern Ireland.

¹⁵ Readings of these constraints differ, but the likelihood that such powers would end up in the European Court of Justice is one of several reasons for caution.

may be politically popular, but this combination undermines claims that the Scottish Parliament itself needs more fiscal powers to be accountable.

7. On the issue of assignment of tax revenues:

h) That the assignment of tax revenues (eg the Scottish Parliament receives some percentage of VAT revenues attributed to Scotland) is different from having devolved taxes where the Scottish Parliament has control over the tax rate and (perhaps) tax base. There might be some advantages in terms of political narrative (ie countering the view that the block grant is a subsidy from Westminster) but whether there is a genuine stake in VAT revenue growth in Scotland would depend on how the equalisation mechanisms work.

8. On the issue of borrowing:

i) That greater reliance on devolved taxation and/or assigned revenues inevitably means that the income of the Scottish Parliament will be less predictable: for example, consider how it would have been affected by the 2008 recession and the present tax-poor economic recovery.

j) That there will have to be ‘internal fiscal rules’ that constrain borrowing to offset cyclical fluctuations and for capital purposes so that the UK Government can meet its international obligations, in particular to the EU.

9. For arrangements to work, in the sense that new powers are usable and that they command consent in Scotland and in other parts of the United Kingdom, there must be full transparency of the funding arrangements (Heald, 2014b).

QUESTION 2: WHAT FURTHER FINANCIAL POWERS SHOULD BE DEVOLVED TO THE SCOTTISH PARLIAMENT AND WHY?

10. My strong preference would have been for the Calman income tax powers contained in the *Scotland Act 2012* to be used. This would have been a gradualist step, during which implementation issues could have been resolved. This power is sometimes represented as being ‘much bigger’ than the tartan tax, but that is primarily because the first 10p of yield substitutes for the reduction in UK income tax for Scottish taxpayers. The genuine difference is that the Calman tax applies to the higher and additional rate bands, whereas the tartan tax only applied to the basic rate band.

11. At this juncture, it is useful to introduce some numbers. Scotland's mid-year 2014 population was 5,327,700, of which 4,416,021 (83%) were 16 or over. The electoral register for the 2014 Referendum contained 4,285,323 voters, estimated to be 97% of those eligible. The latest year for which data are available for Scottish income taxpayers is 2011-12 (HMRC, 2014a), so there is a lag but not one likely to be significant in the present context. There were 2.64 million Scottish income taxpayers paying £11.3 billion total tax. Taxpayers (217,000) with total incomes of £50,000 and above paid £5.018 billion total tax: thus, 8.22% of taxpayers paid 44.41% of total tax. Taxpayers with total incomes of £100,000 and above (42,000) paid £2.548 billion: thus 1.59% of taxpayers paid 22.55% of total tax. This concentration of yield indicates (a) that declarations on residence in Scotland acquire a significance they have never had before (the maximum additional tax payable/savable under the maximum tartan tax variation was modest)¹⁶; and (b) hints at the constraints on Scottish tax policy. One other source of constraint is that, like the tartan tax, the Calman tax would only apply to non-savings income, excluding savings and dividends because of the administrative complexity involved.
12. The rhetoric that surrounded the Referendum has been taken by many commentators to mean that it constituted a critical juncture in relation to taxation powers. There has been a clamour for full income tax devolution, without fundamental issues being addressed. These are illustrated below, on the assumption that UK income tax would not be levied on Scottish residents:
- a) This is likely to cause a flash point at Westminster regarding the role of Scottish MPs in voting for a UK budget containing income tax measures applicable to the residents of England, Wales and Northern Ireland. The implications for government formation have been publicly debated since the Referendum.

¹⁶ At the maximum +3p variation in 2014-15, the maximum annual charge from the (now lapsed) tartan tax would have been £956. Doubling that for a household consisting of two higher rate taxpayers does not reach a total at which actual or declared change of residence from Scotland to other parts of the United Kingdom would have seemed likely.

- b) If income tax were to be fully devolved, that raises the question of whether Capital Gains Tax should also be devolved. These are closely related personal taxes and there are inevitably opportunities to convert income into more lightly taxed capital gains: such conversion would erode the Scottish tax base and benefit the UK tax base.
- c) For the reasons discussed under Question 3 below, Corporation Tax is not suitable for devolution. Given that Corporation Tax rates are falling internationally, relative to the taxation of earnings (particularly when National Insurance is added), there are taxation incentives for the self-employed to incorporate, for example, by using personal service companies. These are widespread in the oil services sector, constituting another leakage from the Scottish tax base.

13. Four matters concern me greatly:

- a) If the UK Treasury does not have a financial stake in the Scottish income tax base, I would expect both malicious actions (eroding that base through other tax measures) and malign neglect (inadequate attention being paid to interactions with other tax measures and inadequate enforcement from HMRC in the entirely new situation where determination of Scottish residence matters).
- b) The potential loss of access to the expertise and economies of scale of HMRC. Over recent years HMRC has received much criticism about its performance, but at least part of its perceived failures relate to the internationalisation of business and the way in which tax avoidance exploits complexity yet acts as a driver for more complexity.
- c) Whereas the Calman Commission took 14 months from appointment to the publication of its final report, the Smith Commission is expected to deliver on a much more complex agenda within 10 weeks in the build-up to a UK General Election campaign.¹⁷
- d) So much effort having gone into devising new financial powers, political parties go into the 2016 Scottish Parliament election promising not to use them.

¹⁷ The Holtham Commission took 24 months and the Mirrlees Review 31 months.

QUESTION 3: WHAT FURTHER FINANCIAL POWERS SHOULD NOT BE DEVOLVED TO THE SCOTTISH PARLIAMENT AND WHY?

14. The criteria for determining which taxes are suitable for devolution were discussed in the Muscatelli (2008) and Calman (2009) Reports. In relation to the large revenue generators:
- a) Corporation Tax should not be devolved because, *inter alia*: (i) EU legal cases are likely which will consume time and resources, whatever the outcome; (ii) recent high-profile instances of avoidance show how vulnerable this form of taxation has become despite the OECD's efforts in its Base Erosion and Profit Shifting project (OECD, 2014); (iii) this would create economic distortions within the United Kingdom; and (iv) the UK Government would use other financial levers against a Scottish Government that reduced its Corporation Tax below the UK level.
 - b) VAT should not be devolved because, *inter alia*: (i) EU treaties forbid VAT variation within a member state; and (ii) this would create new avoidance and evasion possibilities when the VAT 'tax gap' is estimated to be 10.9% in 2012-13 (HMRC, 2014b). It would be possible to fully or partially assign VAT revenues as a substitute for part of the block grant, but that would increase revenue volatility and increase the importance of damping and smoothing mechanisms (see Question 5 below).
 - c) National Insurance should not be devolved because, *inter alia*: (i) though economists correctly regard this as a second income tax, psychologically the public links it to pensions and other welfare benefits provided at the UK level; (ii) this would lose the pooling benefits over the UK population as a whole; and (iii) this would further complicate policy attempts at the UK level to address the future role of National Insurance.
 - d) Oil tax revenues should not be devolved because, *inter alia*: (i) of their future volatility in relation to oil prices, production costs and output; and (ii) of these natural resource rents being part of the pool of UK resources.

QUESTION 4: TO WHAT EXTENT COULD THE SCOTTISH GOVERNMENT BE CONSTRAINED IN HOW IT USES NEW TAX POWERS GIVEN THE INTERACTION WITH FISCAL DECISIONS AT A UK LEVEL?

15. Paradoxically, to make devolution finance work better, it is not the Devolved Parliaments/Assemblies/Governments that must change most, but the UK Parliament and Government. UK Budgets are treated as political theatre, where the obligation on the Chancellor of the Exchequer is to pull some rabbit out of the hat in order to catch Opposition parties off guard. The Budgets that attract the most instantaneous praise are often the ones that do the most damage. The predictable result is that UK tax policy has become incoherent (Johnson, 2014a). Reforms that would benefit the UK Parliament itself would be to bring the Budget forward to November and to establish a Tax and Spending Committee which would take on the budget review function that the wide-ranging responsibilities of the Treasury Committee lead it to neglect (Heald, 2014a). Otherwise income tax powers are likely to lead to parity, as any change by a Devolved Administration is vulnerable to countering – whether on thresholds, bands, or rates – by the UK Government. Without appropriate constitutional machinery on intergovernmental financial relations, it would be possible for a UK Government to subvert the financial arrangements, for example, by significantly reducing income tax rates in England while increasing National Insurance and VAT.
16. It is necessary to distinguish between what are (a) constitutional/legal constraints and (b) those that come from the same political parties operating at UK, national and local government levels. Parties have played a highly centralising role, with UK-based parties concerned that actions at sub-national level will be used against them in UK elections. For the ‘New Union’ to work, UK politicians will have to learn to think in constitutional terms (possibly a German-style debt brake: Lodge and Wegrich (2014)), and to develop a harder skin about differential priorities at different tiers of government and jurisdictions.
17. The long-term direction of travel of UK policy has been greater integration of taxes and benefits, yet devolving income tax while holding most social security at the UK level will involve a partial change of direction in the Devolved

Administrations. There are some welfare payments where there is a strong case for devolution because of the connections to devolved service functions: housing benefit is an obvious example. There is a public attachment to UK-wide benefit levels (eg the state pension) even though it is widely known that its purchasing power varies markedly. The interactions of tax thresholds, tax bands and tax rates, on the one hand, with tax credits and the welfare system (including Universal Credit), on the other, raise issues outside my expertise. What appeared to be the case in the Scottish Referendum is that both sides favoured a more generous social safety net than the UK Government. If that view survives beyond the Referendum campaign, there will be difficult issues of policy design and funding.

QUESTION 5: WHAT ARE THE IMPLICATIONS OF FURTHER FISCAL DEVOLUTION FOR THE BLOCK GRANT?

18. Having a Referendum was bound to put pressure on the Barnett formula in the event of a ‘No’ vote. ‘The Vow’ (Cameron *et al*, 2014) on the front page of the *Daily Record* on Tuesday 16th September included the three leaders’ commitment to ‘the continuation of the Barnett allocation of resources’. Although this sounds definitive, the actual meaning is ambiguous. Does it mean one or more of the following:

- a) That the Barnett name will be kept;
- b) That the population-based adjustment mechanism will continue, whether or not in combination with needs assessment; and/or
- c) That Scotland’s per capita public expenditure, which has consistently been above UK=100, will maintain this relative position?¹⁸

19. The Barnett formula receives a bad press, some justified but much showing little understanding of how the United Kingdom operates. Indeed, it can be argued that the population-adjustment mechanism of Barnett, and of its Goschen predecessor

¹⁸ The Treasury has consistently refused to publish spending data on services in England that would be devolved according to each of the three schemes of devolution. The comparative figures which are regularly cited are those for identifiable expenditure, published annually in *Public Expenditure: Statistical Analyses* (Treasury, 2014) which include much non-devolved expenditure, particularly in relation to social security. The Barnett formula should produce long-term convergence on England = 100 provided that nominal expenditure is increasing. However, this has not happened for a variety of reasons, the most important being the falling relative population of Scotland (see Heald and McLeod, 2002).

(Mitchell, 2003), has played a significant role in sustaining the United Kingdom as a multinational state. As well as the advantage to the Treasury (ie not having to become involved in detailed negotiations with the three territories and (now) Devolved Administrations), the formula avoids the Treasury intervening in expenditure priorities. Given the population predominance of England, UK policy is often perceived as English policy and non-English needs would be perceived through those eyes (eg by extending English needs assessment formulae). The existence of the territorial blocks has allowed expenditure-switching, originally by Secretaries of State in the UK Cabinet and later by the elected governments of Scotland, Wales and Northern Ireland. Those arguing for a needs assessment tend to (a) underestimate the complexity and sensitivity of such an exercise,¹⁹ and (b) fail to recognise how a built-up calculation might constrain devolved policy-making. The most telling criticisms of the Barnett formula are that (i) there has been a failure by UK Governments to explain the rationale and explore alternatives, and (ii) the 2000s' period of unprecedented public expenditure growth was not used to recalibrate the formula (Heald and McLeod, 2002). Barnett is now blamed for perceived injustices that have nothing directly to do with Barnett, such as the treatment of the North East of England by within-England distribution formulae.

20. If the devolution finance system was strictly revenue-based, the Scottish Parliament would have its budget determined by the revenue yield of its own taxes and the revenue yield in Scotland of UK taxes. There would be no grants from the UK Government: there would have to be extensive borrowing powers to cope with volatility, otherwise fiscal decisions would become strongly pro-cyclical. The transfer of tax bases from the UK Parliament to the Scottish Parliament will be accompanied by compensating reductions in the block grant. As with the Calman 10-points income tax transfer, there will be complicated issues of how

¹⁹ One of the by-products of the Holtham Commission on devolution finance in Wales was the proposal by two of its three members that the Scotland budget should be cut by £4 billion (Holtham and Miles, 2010). Outside Scotland, it is widely assumed that the Scottish Parliament is over-funded.

that is indexed in the future. The view that this makes the block grant less important is mistaken:

- a) How this adjustment is done is profoundly important and introduces complexities to a previously simple calculation.
- b) Even when there is no explicit needs assessment, the size of the block grant indicates the level of Scottish spending that the UK Government is willing to underwrite.
- c) Securing transparency of the calculations acquires more salience because Scottish Ministers have to move tax resolutions to restore the revenue loss, or to exceed or go below that. Under the Calman tax, MSPs would demand assurance that the Treasury has not made changes to the block grant as a consequence of the Scottish income tax being higher or lower than 10p. The same issue will apply in the case of beyond-Calman income tax devolution.

QUESTION 6: WHAT ARE THE IMPLICATIONS OF FURTHER FINANCIAL POWERS FOR THE ROLE OF REVENUE SCOTLAND?

21. I would expect the role of Revenue Scotland to grow through time, but the maintenance of an effective relationship with HMRC in relation to income tax is the foremost organisational issue. Devolved taxes will require a bedding-in period, during which there will be those looking for administrative failures or cases of egregious tax avoidance.

CONCLUSION

22. I understand that the Scottish Parliament wishes to seize the present momentum to achieve an extension of its powers that would either not otherwise be possible or only possible over a long timescale. Nevertheless, I urge the Parliament to tread carefully. Those who wish to maximise devolved taxes should clarify whether they believe:

- a) public expenditure in Scotland is too high, too low, or just about right.
- b) whether their tax devolution proposals are expected to lead to the overall level of taxation in Scotland being higher, lower, or about the same as in other parts of the United Kingdom.

Aberdeen, 29 October 2014

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WRITTEN SUBMISSION FROM PROFESSOR CHARLIE JEFFERY**Implementing Smith****CHARLIE JEFFERY****Centre on Constitutional Change, University of Edinburgh****ESRC Future of the UK and Scotland Programme**

The Smith Commission report was a compromise of often quite divergent positions that was crafted at speed. Already it has been criticised from a number of directions, including from within parties represented in the process (though not, generally, from those directly involved in the process).

Those party-political criticisms have been various and divergent, including: concerns that the report undermines the notion of pooling of risk across the UK that some see as important; concerns that the report falls short of the extent of additional devolution implied by 'The Vow'; and concerns that additional devolution to Scotland is unfair without balancing measures in Wales and, in particular, England.

This diversity of response to the report (alongside other, more positive views) contrasts with the certainty with which the recommendations in the Smith report are put. These recommendations in most cases are put definitively; they 'will be' implemented.

They may be, but there are significant hurdles on the way. There are numerous technical difficulties in the implementation both of fiscal devolution and welfare devolution, which my colleagues David Bell and Nicola McEwen have addressed elsewhere. There are also perhaps more philosophical challenges around the scope to establish the Scottish Parliament as an indissoluble institution. There are also a number of procedural challenges.

A draft Bill is expected to be introduced to the House of Commons by late January 2015. This may (as initially suggested by Gordon Brown on 8 September 2014) achieve a second reading and with it a substantive debate before the UK Parliament session ends prior to the general election on 7 May. It will clearly not have received full scrutiny in the Commons before the next UK election, nor in the House of Lords. Nor will it have received full scrutiny in the Scottish Parliament, which, following the precedent of the 2012 Scotland Act and wider conventions around legislative consent, will need to give its approval to the Bill before it can be enacted.

Many commentators are suggesting that the outcome of the next UK election is the most unpredictable in living memory. That said any ensuing UK Government is likely to include one or more of the pro-Union parties that contributed members to the Smith Commission, and so is likely to wish to take forward any Bill on additional devolution for Scotland. The SNP, a further contributor to the Smith Commission, may also have some say in determining the composition of the next UK Government.

The party-political criticisms of Smith of course have been expressed precisely by figures in these parties: Labour on risk-pooling and perceived unfairness to Wales; the SNP on under-fulfilment of The Vow; and the Conservatives on the need for

balancing actions in England. Our public attitudes research conducted both before and after the referendum suggests that the criticisms of the SNP and the Conservatives have considerable traction in public opinion in Scotland and England respectively. There are also some echoes in Scottish opinion of Labour concerns about risk-pooling.

These concerns and their public resonance are likely to be reflected in parliamentary scrutiny and debate, though likely pulling in different directions in Westminster and Holyrood. There may be calls at Westminster to restrict the extent of fiscal or welfare devolution in the interest of pooling risk. There may equally be calls at Westminster - echoing the Prime Minister's initial intervention on 19 September - to make progress on Smith and on English Votes on English Laws co-dependent. The Command Paper on reform in England expected in the next days, and the process of pursuing reform it foresees, may cast some light on this.

Any changes to the substance or spirit of the Smith proposals arising from such debate at Westminster may not find favour in the Scottish Parliament, where there are likely to be pressures from within the majority party to seek power additional to those proposed by Smith. There is scope for divergence between the views of the two parliaments on the implementation of Smith. Lord Smith's confident 'will be' formulations may prove more difficult to implement than he may have expected.

WRITTEN SUBMISISON FROM PROFESSOR MICHAEL KEATING**Memo for Scottish Parliament Devolution (Further Powers) Committee****The Smith Report**

Michael Keating, Professor of Politics, University of Aberdeen and Director of ESRC Centre on Constitutional Change

3 December 2014

1. General Approach

- 1.1. The Smith proposals should be judged according to whether they give the Scottish Parliament the powers needed to foster growth and social cohesion. By this criterion they are inadequate.
- 1.2. The main reason is that they do not stem from a mature consideration of Scotland's needs but from a pledge made by the pro-union parties in a moment of panic towards the end of the referendum campaign. This included an unrealistic timetable, which precluded in-depth consideration, public debate and civic engagement. The process was dominated by bargaining among political parties. The pro-union parties started from their own previous proposals, which were in many respects flawed, while the SNP had not worked out what its priorities were for a reformed union and so asked for too much.
- 1.3. These problems were compounded by the approach to negotiations, which was to take items piecemeal, even to the point of considering bits of existing policies, rather than focusing on broad policy fields.

2. Taxes

- 2.1. There is an excessive focus on income tax, which was reflected in the negotiations and the media coverage of the report. The concession is a significant one but:
 - 2.1.1. The tax base and threshold are reserved;
 - 2.1.2. Investment income, capital gains and inheritance, which are forms of income, are reserved;

- 2.1.3. National insurance is reserved;
 - 2.1.4. This leaves limited discretion over basic rates (which have not been raised since the 1970s) and the higher rate (where the argument among the parties is about 50% versus 45%);
 - 2.1.5. Income tax is no longer the reliable, buoyant revenue-raiser it was, given the growth of low wages and raising of the tax threshold.
- 2.2. Policy discretion requires a broad range of taxes.
- 2.3. Assignment of VAT does broaden the tax base (although not the discretion) and will reduce reliance on income tax. One might ask why it was assigned on the basis of receipts rather than population, which could have allowed the principle to be extended more easily across the UK.

3. Welfare

- 3.1. Proposals for devolution of welfare are piecemeal and lack coherence.
- 3.2. The Labour Party in particular has long resisted the devolution of welfare on the grounds that social entitlements should be uniform across the state. The pro-union parties, however, have never spelt out just what should be uniform and what can vary. In practice, there is considerable variation already.
- 3.3. There is a need to think about taxation, welfare and labour market policy together and at multiple levels. There is no recognition of this.
- 3.4. Universal Credit is locked in as a UK programme, which precludes discussion of possible adaptations to Scotland. The delay in rolling it out could have given an opportunity for a deeper examination before proceeding.
- 3.5. There is a provision apparently designed to allow Scotland to repeal the 'bedroom tax', which indicates a concern with immediate short-term problems rather than a deeper consideration of welfare.

4. Barnett

- 4.1. The Barnett Formula is to remain the basis for distributing the remaining block grant.
- 4.2. It is difficult to discuss taxation without also addressing this.
- 4.3. The rationale given by the parties for keeping Barnett is that it is necessary to stabilize revenues and to equalize in accordance to need. Yet Barnett is not an equalization mechanism – it is notable that in its Scotland Analysis papers the Treasury never made this

claim. The Labour Party did (Scottish Labour Party, *Powers for a Purpose. Strengthening Accountability and Empowering People*, 2013, p.37, 'An equitable system of grant distribution – to Scotland, and indeed Wales and Northern Ireland – is a key aspect in the UK's social union.')

5. The UK dimension

- 5.1. The parties have attempted to resolve the issue of Scotland in advance of addressing the territorial constitution of the UK as a whole.
- 5.2. This will prove impossible politically, since already there are reactions elsewhere in the UK seeking to link Smith to reform of Barnett and English Votes for English Laws.
- 5.3. There are proposals for a constitutional convention for the UK or a federal constitution. This could not be done without reopening the Scottish settlement.

6. Local taxation

- 6.1. The proposed commission of inquiry on local taxation in Scotland could have at least as much impact. It opens up new possibilities for taxation in Scotland, including more progressive property taxation and land-value taxation. If local authorities are able to raise more of their own revenue, the Scottish Government need raise less. If the Scottish Parliament is to control the rates and gain the revenues from income tax, a local income tax makes less sense, as both levels would be competing for the same tax share and the tax base for public services in Scotland would be excessively narrow.

7. External Affairs

- 7.1. This is not a matter to which the Smith Commission gave much attention but it is part of the wider agenda.
- 7.2. 'Paradiplomacy', the involvement of sub-state governments in international affairs, is part of the normal practice in federal systems.
- 7.3. This often stems from the external projection of competences that are devolved domestically. In the Belgian formula, it is expressed as *foro interno, in foro externo*.
- 7.4. Paradiplomacy is also used to promote economic development; for policy learning; to assert national aspirations; and to give moral leadership.
- 7.5. Constitutional provisions vary, being most extensive in Belgium.

- 7.6. The Scottish Government proposes a greater role for Scotland. There are two aspects:
- 7.6.1. The promotion externally of devolved competences, which extends the devolution principle;
 - 7.6.2. The securing of Scottish interests in reserved matters, which is more difficult.
- 7.7. The Scottish Government proposes that Scotland be able to sign international treaties. This is allowed in Belgium, subject to the treaties not conflicting with Belgian foreign policy objectives. The principle could be extended to Scotland, although comparative experience suggests that whether an agreement is formally called a treaty, as opposed to an understanding, concordat or whatever is not particularly important.

8. The European Union

- 8.1. The European Union poses other issues, since it is both external and domestic.
- 8.2. The Scottish Government (like other sub-state governments) seeks more 'direct' influence in Europe. This is problematic since only national governments are directly represented in the key institutions of the Council of the EU and the European Council and in the nomination of the Commission.
- 8.3. More important is indirect influence, through participation in member state delegations to the Council of the EU and via European networks.
- 8.4. There has been a big emphasis on Scotland's representation in the delegation to the Council of the EU and rights to lead delegations. This is a high-profile activity and there may be a case for clarifying Scotland's rights here. On the other hand, Scottish ministers must speak for the UK as a whole and cannot dissent from the common line, so this is not direct Scottish representation.
- 8.5. More important is influencing the EU policy process at all stages. It is crucial to be aware of proposals pending in the Commission and the consultative mechanisms and to be prepared with an argument. Influence is maximized by making a positive contribution, not by lobbying for one's own interests.
- 8.6. It is important to have networks of people in the Brussels institutions, and for Scottish civil servants to be familiar with Brussels. Scottish civil society and education should also be familiarized with Europe.
- 8.7. The matter of the role of devolved territories in EU treaty change raises issues of a different nature. In so far as these affect the competences of the devolved assemblies, there is an argument for

stronger rules analogous to the convention that their powers should not be changed without their own assent. This could, for example, provide for treaty changes to approved by the devolved legislatures, with a special provision needed to over-ride their objections. This in turn could ensure that they are fully involved in the negotiations about treaty change.

WRITTEN SUBMISSION FROM PROFESSOR NICOLA MCEWEN

The Smith Commission Report: A focus on welfare



Evidence to Devolution (Further Powers) Committee

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This paper outlines some of the issues that may emerge from the recommendations of the Smith Commission on the devolution and administration of social security. It begins with a general observation on the changing nature of the devolution settlement, the scope of the recommendations on welfare devolution and flexibility, and the challenges of increased policy interdependence.

1. General Observation

One of the strengths of the original devolution settlement was its emphasis upon defining the powers of the Scottish Parliament by setting out in specific reservations (Scotland Act, 1998, schedule 5) those areas where it could not legislate. The Scotland Act 2012 and in particular the Smith recommendations may herald a departure from that reserved powers model. Their focus has been on identifying new powers to be devolved, rather than redefining what is reserved. This may produce a settlement that is more restrictive than it would otherwise be.

The emerging devolution settlement is also more complicated. It will increase the powers of the Scottish Parliament and simultaneously increase the interdependence between these powers and the policies of the UK government, notably on taxation, economic policy, welfare and energy. The Smith commission recognised this increased complexity in its call for the “reform” and “scaling up” of intergovernmental machinery “as a matter of urgency”, including new bilateral arrangements. Revising IGR doesn’t require legislation, but it would require a cultural change in the relationship between the UK and Scottish Governments, new forums for coordination, potential implications for IGR involving Wales and Northern Ireland, and further challenges to the Scottish Parliament’s capacity to scrutinise policy decision-making.

2. Forms of Welfare Devolution

The UK government’s Command Paper outlined three approaches to devolving welfare, which allow for variable degrees of political autonomy:

Model 1: devolving a portion of the spending associated with a particular benefit, alongside the power to either vary the rate and rules of the benefit, replace it with a completely separate benefit, or to reallocate that funding to another area;

Model 2: devolving a proportion of the expenditure on a specific welfare service delivered to claimants in Scotland, alongside a statutory responsibility to deliver that service in Scotland, potentially with some flexibility over the scale of provision;

Model 3: powers to ‘top up’ benefits above the level set by the UK Government.

The recommendations in the Smith Report seem to incorporate all three models.

3. Devolved Benefits

The Smith Report recommended devolving Attendance Allowance, Carer’s Allowance, Industrial Injuries and Severe Disablement Allowance, Winter Fuel Payments and a range of small benefits which, together, accounted for around 6% of social security spend in Scotland in 2012/13. The report also recommended the devolution of Disability Living Allowance/Personal Independence Payments which, assuming it includes DLA/PIP for all age categories, is a more substantial benefit amounting to £1.45bn in 2012/13, or 8.2% of Scottish welfare spend. Around 86% of Scottish welfare spending, including pensions, child and family benefits, tax credits and work-related benefits, will remain reserved to Westminster after the new settlement is implemented.

The Report indicates that the Scottish Parliament will have ‘complete autonomy’ in determining the structure and value of these benefits. This would imply conformity with Model 1 above, but that may not be clear until legislation and subsequent agreement on how the block grant is to be adjusted.

The Smith Report suggests it is for the Scottish Parliament to determine whether it agrees a delivery partnership with DWP. A delivery partnership may be cost-effective, especially in light of the relatively modest transfer of social security spend, but it is likely to mean that the autonomy which could be exercised over these benefits would be less than ‘complete’, curtailing the scope for distinctive policy development.

4. Universal Credit

Universal Credit will remain reserved, with policy development, administration and delivery the responsibility of DWP. Within this reserved framework, the Scottish Government will have an opportunity to alter some delivery arrangements, and the Scottish Parliament will have the power to vary a range of housing cost elements, including ‘varying’ the under-occupancy charge and local housing allowance rates, eligible rent and deductions for non-payment. This conforms to Model 2 above, incorporating some opportunities for modest policy innovation but ruling out others. The limits set on the power to vary housing elements will depend on a mix of statutory obligations, bureaucratic and financial constraints, with all costs to be met by the Scottish Government.

5. Employment Provision

The Smith report recommends some form of devolution over employment programmes to support the employability of unemployed people. It is not clear whether the recommendation conforms to model 1 or 2. Para 57 refers to the parliament being given ‘all powers’ over such support programmes on completion of current contracts. It then goes on to define this as ‘the power to decide how it operates these core employment support services’. Operational control over services does not necessarily imply legislative control. It is unclear, for example,

whether the parliament would have the power, should it choose, to deliver these services through public or third sector bodies instead of the existing contracting arrangements or to completely redesign employment support programmes. Delivery of employment programmes will require close cooperation with Job Centre Plus, which is to remain reserved.

6. New/Top-up Benefits

The Smith Report includes the power ‘to create new benefits in areas of devolved responsibility’. It is not clear what this means, since the provision of ‘assistance for social security purposes to or in respect of individuals by way of benefits’ (Scotland Act, schedule 5, Head F) will remain reserved matters, save for those specific exceptions identified above. I assume it reinforces the Scottish Parliament’s power to replace those benefits which have, or will be, devolved with new alternative benefits aimed at a similar purpose.

The Report also includes provision to make discretionary payments to supplement any UK social security benefit. This power would be constrained by available finance, as well as the capacity for DWP or HMRC to incorporate these additional payments within their processing and delivery systems for welfare benefits or tax credits. It is not clear whether these systems would have the capacity to distinguish and process claims on the basis of distinct Scottish entitlements.

7. Social Security Interdependences

The complexities of the social security system will remain after the introduction of the Smith reforms, creating interdependencies which will have to be managed to avoid new anomalies in the system.

The Benefit Cap: The UK Government’s Benefit Cap limits the total amount of benefit available to households to £500/week for couples or single parents with children at home, and £350/week for adults without dependent children. Among those benefits included within the cap are two to be devolved – Carer’s Allowance and Severe Disablement Allowance. These should be excluded from the cap for Scottish claimants. The Smith report also recommended that the Benefit Cap be adjusted to accommodate additional benefit payments, which should include discretionary payments.

Benefit interdependence: Entitlement to some benefits depends upon eligibility for others. If the eligibility criteria for devolved benefits are altered, it could affect entitlement to UK benefits. My reading of para.55 suggests that any additional benefit received by Scottish claimants as a result of devolved benefits or Scottish discretionary payments *should not* adversely affect entitlement to UK benefits or tax credits, but in practice the new complexities generated may be difficult to administer.

Conditionality and Sanctions: The merger of Job Centres with the Benefits Agency combined employment support with the process of claiming and receiving benefits. This includes provisions for conditionality, which make claims for Job Seekers Allowance and Employment Support Allowance conditional upon claimants’ willingness to seek work, with those deemed not to meet these conditions potentially facing financial sanctions. There is a close relationship between these conditionality rules and the employment support programmes which are to be devolved under Smith. This is likely to generate operational challenges, political difficulties, and accountability issues, given the concerns expressed by

the Scottish Government and Parliament about the DWP's conditionality and sanctions regime.

WRITTEN SUBMISSION FROM PROFESSOR DAVID BELL

The Draft Scottish Budget 2018-19

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Strategic Context

It is a pleasure to introduce the Draft 2018-19 Budget to the Scottish Parliament. This will be the first year in which the full proposals of the Smith Commission can be implemented. It has taken three years to put these proposals in place.

Thus, following the Scotland Act 2015, the Scottish Parliament is now able to set both the bands and rates of income tax; it can set Air Passenger Duty; it will receive a share of VAT revenues raised in Scotland. Together these measures will take Scotland's revenue raising capability to around £26 billion this financial year.

The potential costs and benefits to the Scottish budget of differences in macroeconomic performance have been amplified by the transfer of full income tax powers under the Scotland Act 2015 and their implementation in the current financial year. Any difference between Scottish and UK rates of tax revenue growth will have a larger consequence for the Scottish budget now than under the Scotland Act 2012 because the block grant adjustment has been increased in line with the increased revenue associated with the extended income tax powers.

The relative changes in the growth of tax revenues in Scotland and rUK since the introduction of the Scottish Rate of Income Tax (SRIT) have been small compared to the size of the Scottish Budget, and therefore easy to accommodate. The decision to hold SRIT at 10p has also maintained broad equality between the budgets that have been set under the Scotland Act 2012 and the outturn that could have been expected under the Barnett Formula.

VAT revenues will now be shared with the rest of the UK. Though common in other countries, this form of revenue allocation is relatively new to the UK. It does not significantly increase the accountability of the Scottish Parliament because the Parliament will have no control over the setting of the tax base (including exemptions such as food and children's clothing) or the rates of tax. Thus, it will not add significantly to the incentives for the Scottish Parliament to improve Scotland's economic performance.

Reductions in Air Passenger Duty might have given Scotland a competitive advantage in air travel. However, the change implemented by the UK Government in 2015, whereby children were exempt from the tax, has perhaps reduced the potential for competitive advantage. Whereas business air travellers are probably not very price sensitive, the holiday trade, which inevitably involves children, is more likely to respond to differences in the costs of air fares.

The Scotland Act 2015 has also given Scotland some control over some welfare spending. The new spending responsibilities are grouped in three main categories covering (1) disability benefits, (2) those benefits covered by the so-called Regulated Social Fund and (3) discretionary housing payments. The specific benefits are:

1. Attendance Allowance, Disability Living Allowance/PIP, Carer's Allowance Industrial Injuries Disablement Allowance and Severe Disablement Allowance.
2. Cold Weather Payment, Funeral Payment, Sure Start Maternity Grant and Winter Fuel Payment.
3. Discretionary Housing Payments

Transfer of these benefits will add around £2.5 billion to Scotland's spending power in 2018-19.

There is a recent precedent for the transfer of welfare powers from the UK government to local government (in the case of Scotland to the Scottish government). That was due to the "localisation" of council tax benefit which took place in 2013-14. One argument in favour of this change was that councils had previously no incentive to reduce claims for council tax benefit, since these would always be met by the Department for Work and Pensions.

The change to the administration of council tax benefit was effected by a transfer from the DWP Annually Managed Expenditure (AME) to local government funding which is drawn from the Departmental Expenditure Limit (DEL) budget. One important implication of this change is that, as part of DEL, council tax benefit now has to compete within local government budgets against other priorities.

A similar arrangement has been agreed with the UK Government for the transfer of the new welfare responsibilities to Scotland. This has created a substantial difficulty for the Barnett Formula (which operates only on DEL budgets) since these benefits remain part of AME expenditure at UK level. However, a solution has been found that is in a sense a variation on the Barnett Formula²⁰. The Scottish Government will receive a transfer into its DEL budget of an amount equivalent to 2018-19 DWP spending on the relevant benefits. In subsequent years, this component of its budget will be adjusted in line with *changes* in spending on the equivalent benefits in the rest of the UK, adjusted for "population at risk". (Some of these benefits are specific to particular groups within the population. Rather than adjust for overall changes in the population, as is the case for the Barnett formula, it has been agreed to reflect relative changes in the size of the populations that may be eligible for the benefits - the "population at risk")

This mechanism for transferring welfare benefits means that the existing AME spending in Scotland, which is largely used to fund public sector pensions, has not been affected by the transfer of fiscal powers to Scotland. The new welfare benefits will be dealt with through Scottish DEL.

This change will give the Scottish Government the incentive to use the additional resource to deliver better outcomes for welfare recipients, or the same outcomes at lower cost. Having these resources within the DEL budget does enable it to transfer resources to other priorities. For example, the delivery of free personal care might be made more effective by the effective integration of AA and DLA budgets with existing social care budgets at local government level.

It has taken some time, and considerable resource, to put in place the necessary infrastructure to deal with these changes in Scotland's fiscal powers. The changes involved were much more extensive than those needed under the Scotland Act 2012, which involved the creation of Revenue Scotland and payments of around £40 million to HMRC to implement the Scottish rate of income tax (SRIT). We do not yet have the final cost associated with the implementation of these new powers.

²⁰ See: [Powering Public Services](#), Local Government Association

Macroeconomic Context for the 2018-19 Budget

Since 2014-15, the performance of the Scottish economy has largely mirrored that of the UK as a whole. As a result, the growth in income tax revenues in Scotland has closely tracked that in the UK. The consequence is that the reduction in the Barnett block grant that accompanied the granting of limited income tax powers under the Scotland Act 2012 has almost exactly offset the revenues arising from SRIT (based on an SRIT of 10p), Land and Buildings Transactions Tax and Landfill Tax. *Thus far, the tax powers associated with Scotland Act 2012 have had no net effect on the Scottish Government's spending power.*

Nevertheless, due to the continuing pressure to reduce public sector borrowing, the block grant itself from Westminster has been under considerable strain. However, Scotland has been somewhat sheltered from this pressure by the UK Government's decision to protect real spending on health and education in England. The Scottish Government allocates more of its overall budget to health and education than does the UK Government. In the jargon of the Barnett Formula, spending on health and education is almost entirely "comparable" and thus a larger share of the Scottish Budget has been protected from spending cuts than that of the UK as a whole.

Our proposed budget for 2018-19 is set out in Table 1 below:

Table 1: Scottish Budget 2018-19, £m

Revenues	
Council Tax	2269
Business rates	2350
Land and Buildings Transactions Tax	749
Landfill Tax	101
Income tax	14418
VAT	5834
APD	364
Aggregates levy	55
Block grant	8159
CDEL	2772
RDEL	31526
- Of which: borrowing costs for PFI/ NDR	1200
- Of which: borrowing costs associated with Scotland Act 2012	38
- Of which: HMRC transfer	45
- Of which: devolved benefits	2542
Total DEL	34299
AME	7762
Total Scottish budget	42061

Assumptions

In this section we outline the detailed assumptions underpinning the draft budget.

Tax assumptions

Council Tax grows in line with OBR (Dec 2014) projections for Council Tax in Scotland. This assumes that the Council Tax freeze remains until 2015/16, after which the rates are increased annually in such a way as to raise revenues by 2% per annum. The tax base is assumed to grow by 0.7% per annum, from present.

LBTT and Landfill Tax receipts grow at the rate projected by the OBR (Dec 2014) for those taxes in Scotland.

All other taxes are assumed to grow at the same rate in Scotland as the OBR forecasts for the UK as a whole in its Dec 2014 projections. Income tax revenues are projected to grow 28% from 2013/14 to 2018/19 (having been revised down from 35% growth in March).

Block grant assumptions

Scotland's block grant in 2013/14 is assumed equal to Scotland's DEL budget minus revenues from council tax and business rates. Changes to this block grant in future years are calculated as follows:

OBR projections (Dec 2014) provide forecasts of DEL spending for current (RDEL) and capital (CDEL) spending at UK level over the period to 2019/20.

We assume that RDEL will be protected in real terms over the period to 2018-19 for health, schools and international development. We take spending on these items in 2013/14 and uprate nominal spending to maintain the real value of spend. The spending profiles of all other departments is assumed to be cut in such a way as to balance the OBR's forecast RDEL budget.

In each year, a Barnett consequential for Scotland is calculated by applying the relevant departmental comparability factor to the change in nominal spend. Scotland is allocated a population share of the consequential changes summed over all departments; population proportions are taken from ONS population projections.

Similarly, OBR projections for CDEL spending are combined with relevant departmental comparability factors to estimate the Barnett consequential associated with capital spending.

Taxes devolved in 2015/16 result in a one-off deduction to the block grant. The value of the estimated SRIT is assumed to be deducted from the block grant in 2016/17. We assume that the 'Indexed Deduction' method is used to determine the 'Block Grant Adjustment' in 2017/18 and 2018/19.

Revenues from other taxes (the remainder proportion of income tax, the share of VAT, APD and the Aggregates Levy) are assumed to be deducted from the block grant in 2018/19.

Devolved benefit spending

Expenditure associated with benefits devolved under the Smith proposals are estimated by taking outturn expenditure on these benefits in Scotland in 2013/14, and assuming that future spending grows on each of these benefits grows at the same rate as the DWP forecasts for the UK as a whole.

RDEL/ CDEL split

We assume that the Scottish Government increases its DEL budget in proportion to the CDEL element of its Barnett consequential. Thus our estimate of CDEL can be thought of as a lower bound estimate of the likely CDEL budget (the Scottish Government can vire RDEL into CDEL as it wishes, but has to seek the approval of HM Treasury to vire CDEL to RDEL). We also assume that the Scottish Government uses its borrowing powers under the Scotland Act 2012 to fund additional capital spend in 2015/16 – 2017/18, which effects interest payments in 2018/19.

Borrowing and other costs

The estimated cost associated with PFI/ NDR is taken from a SPICe research paper (Campbell and Aiton, April 2014). We also assume that the Scottish Government has borrowed £250m for capital investment in each of 2015/16, 2016/17 and 2017/18 in line with its Scotland Act powers, and that it faces a 5% rate of interest on this debt (covering principal and interest), in line with the estimate in the Scottish Government Draft Budget 2015/16, (p.157).

It is assumed the Scottish Government faces a one-off payment of £45m to the HMRC in respect of administration arrangements for devolved taxes²¹.

AME

Forecast AME expenditure on elements associated with Scotland's existing devolution settlement (largely pensions) are taken from the Draft Budget 2015/16, and assumed to grow at the same rate as UK AME spending excluding the debt interest component of AME. This may underestimate the growth rate of the Scottish Government's AME budget, given that it relates largely to pensions rather than welfare benefits.

In Appendix 1, we explore the implications of varying some of these assumptions described above, while in Appendix 2 we illustrate how forecast errors may lead to a significant borrowing requirement for the Scottish Parliament.

²¹ Based on the fact that The Second Annual Report on the Implementation of the Financial Provisions in the Scotland Act 2012 (Scottish Government, April 2014) identifies that HMRC costs for the implementation of the SRIT are likely in the order £35-£40m.

Appendix 1: Alternative Scenarios

In this section we explore the effects of changes to some of the key assumptions made above for the size of the Scottish budget. We present three scenarios that have varying degrees of plausibility and indicate the effects they would have on our central budget estimates in Table 2.

Scenario 1: No protection of health and education at UK level

We maintain the OBR assumptions for the path of RDEL, but assume that after 2015/16 these cuts are distributed evenly across UK spending departments. This results in a reduction in Scotland's block grant of some £2.5bn. The decision to ring-fence real spending in health and education at a UK level is highly favourable to the Scottish Government, generating increased revenue equivalent to the cost of the new welfare benefits that have been assigned to Scotland.

Scenario 2: A slower path to closing the UK deficit

The current UK Government aims for a budgetary tightening of 5% of GDP between 2013/14 and 2018/19. It expects TME to fall from 41% of GDP to 36% of GDP, with this adjustment virtually all coming from DEL.

In this scenario we assume a slower path to deficit reduction. Specifically, we assume that there is a fiscal tightening of 2% of GDP; spending on RDEL is assumed to fall from 18 to 16% of GDP, rather than under the status quo where RDEL is expected to fall from 18% to 13%. Not surprisingly, this results in an increase in Scotland's block grant of £1.5bn. The increase is perhaps not as great as might be expected. This is because of the core assumption that health and schools spending is protected; the additional RDEL spending is assumed to go to departments that are not currently protected, and these are associated with a smaller Barnett consequential than are health and schools.

Scenario 3: A more rapid growth of income tax revenues in Scotland

This scenario assumes that income tax revenues in Scotland grow at the rate forecast for the UK in the OBR's March 2014 forecast (as opposed to the December forecast). This results in Scottish income tax revenues being around £0.6bn higher by 2018/19, as noted previously. Note however that the Scottish Budget only benefits if this rate of growth is greater than the growth of UK income tax revenues overall. If higher Scottish revenue growth is matched by higher revenue growth in the UK, then the value of Scotland's Block Grant Adjustment simply grows more rapidly, and a larger deduction is made from Scotland's block grant when the rest of Scottish income tax is devolved in 2018/19.

In this scenario therefore, we assume that the SRIT grows between 2016/17 and 2018/19 at the rate forecast for UK income tax growth by the OBR in March 2014, whilst UK revenues grow at the rate forecast by the OBR in December 2014. This results in SRIT revenues growing from £4.8 - £5.35bn, while the value of the BGA grows from £4.8 - £5.3bn. Thus the Scottish Budget grows by some £50m in this scenario as opposed to the core scenario.

Of course, the remaining Scottish income tax revenues (those outside the SRIT) have also grown at a more rapid rate than those in rUK, but the higher SRIT in 2014/15 was deducted from the block grant

in that year, and the remaining tax revenues were deducted from the block grant in 2018/19. The only 'benefit' to the Scottish Budget of the higher income tax growth is the difference between the growth of the SRIT between 2016/17 and 2018/19 relative to the growth of the equivalent tax in rUK.

Scenario 4: Continuation of Council Tax freeze

Another scenario (not shown in the table) is to assume the Scottish Government maintains the Council Tax freeze into the next parliament. This would result in a reduction of Council Tax revenues of around £250m by 2018/19.

Table 2: Alternative Budget Scenarios

	Central Budget	No protection of health and education	Slower path to deficit elimination	Faster income tax growth
Revenues				
Council Tax	2269	2269	2269	2269
Business rates	2350	2350	2350	2350
Land and Buildings Transactions Tax	749	749	749	749
Landfill Tax	101	101	101	101
Income tax	14418	14418	14418	15070
VAT	5834	5834	5834	5834
APD	364	364	364	364
Aggregates levy	55	55	55	55
Block grant	8159	5053	9687	7557
CDEL	2772	2772	2772	2772
RDEL	28984	25879	30513	29034
- Of which: borrowing costs for PFI/NDR	1200	1200	1200	1200
- Of which: borrowing costs associated with Scotland Act	38	38	38	38
- Of which: HMRC transfer	45	45	45	45
- Of which: devolved benefits	2542	2542	2542	2542
Total DEL	34299	31193	35827	34349
AME	7762	7762	7762	7762
Total Scottish budget	42061	38956	43589	42111

Appendix 2: Forecast errors

Our main budget contains estimates of tax revenues in Scotland for 2018-19. These are, of course, subject to forecast error. Income tax revenues can only be known with certainty well after the end of the financial year. Yet, forecasts for income tax are of particular interest to the Scottish Government since this is the largest source of revenue for the Scottish Parliament.

Income tax forecasts have been particularly prone to error in recent years due to the unusual behaviour of the Scottish and UK local labour markets following the recession of 2008-09. In particular, the substantial increase in employment that has occurred since 2008-09 has mostly been in low-paid jobs (both employees and self-employed) which generate relatively small amounts income tax revenue given the generosity of the personal allowance.

This change was recognised by the Office of Budget Responsibility in December 2014. This led to a substantial downward revision in its average earnings forecast and consequent reduction in expected income tax revenues.

To illustrate the magnitude of the forecast errors we have conducted an experiment with our micro-simulation model. The experiment shows the difference between forecast income tax revenues for Scotland in 2018 based on the March 2014 OBR forecast compared with the December 2014 forecast. Table 3 below shows the OBR forecasts of average earnings made on these dates.

Table 3: Forecast growth in average earnings, March 2014 and December 2014:

	<i>Outturn</i>		<i>Forecast</i>					
<i>Year</i>	<i>2012</i>	<i>2013</i>	<i>2014</i>	<i>2015</i>	<i>2016</i>	<i>2017</i>	<i>2018</i>	<i>2019</i>
Forecast (%)								
Mar-14	2.0	1.5	2.5	3.2	3.6	3.7	3.8	
Dec-14		1.8	1.8	2.0	3.1	3.9	3.9	3.8

Source: Office of Budget Responsibility

Aggregated over the period 2014-15 to 2018-19, these seemingly small reductions in the average earnings forecast between March and December 2014 would have led to a reduction of more than £37 billion in income tax receipts at a UK level. For Scotland in 2018-19, our model suggests that the reduction in revenues would have been around £600 million: this is clearly a considerable sum. It is worth around one third of net council tax revenues in Scotland. It is also well in excess of the £300 million borrowing facility agreed under the Scotland Act 2012 to cover forecast errors associated with SRIT.