



The Scottish Parliament
Pàrlamaid na h-Alba

Official Report

DEVOLUTION (FURTHER POWERS) COMMITTEE

Tuesday 2 December 2014

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DEVOLUTION (FURTHER POWERS) COMMITTEE
4th Meeting 2014, Session 4

CONVENER

*Bruce Crawford (Stirling) (SNP)

DEPUTY CONVENER

*Lewis Macdonald (North East Scotland) (Lab)

COMMITTEE MEMBERS

Linda Fabiani (East Kilbride) (SNP)
*Rob Gibson (Caithness, Sutherland and Ross) (SNP)
*Annabel Goldie (West Scotland) (Con)
*Alison Johnstone (Lothian) (Green)
Stewart Maxwell (West Scotland) (SNP)
*Mark McDonald (Aberdeen Donside) (SNP)
*Stuart McMillan (West Scotland) (SNP)
Tavish Scott (Shetland Islands) (LD)
*Drew Smith (Glasgow) (Lab)

*attended

THE FOLLOWING ALSO PARTICIPATED:

Jenny Bates (Smith Commission)
Patrick Harvie (Glasgow) (Green)
Bill Kidd (Glasgow Anniesland) (SNP) (Committee Substitute)
Lord Smith of Kelvin (Smith Commission)

CLERK TO THE COMMITTEE

Stephen Imrie

LOCATION

The Robert Burns Room (CR1)

Scottish Parliament Devolution (Further Powers) Committee

Tuesday 2 December 2014

[The Convener opened the meeting at 09:00]

Interests

The Convener (Bruce Crawford): We have a number of apologies this morning, from Linda Fabiani, Tavish Scott and Stewart Maxwell. Bill Kidd will substitute for Linda Fabiani.

I warmly welcome Alison Johnstone to the committee and say a grateful thank you to Patrick Harvie for his contribution and all his valued interventions during the course of the Scottish Independence Referendum Bill and the early work that we have been involved in. We are very grateful. I know that he is here today as an observer.

In that vein, I also thank Annabelle Ewing for her contribution during her time on the Referendum (Scotland) Bill Committee and at the beginning of the Devolution (Further Powers) Committee.

Mark McDonald has joined us as well, of course. I welcome him and Alison Johnstone. *[Interruption.]* That was not my phone going off.

The first agenda item is declarations of interest by new members of the committee. I invite Alison Johnstone to declare any interests that are relevant to the work of the committee.

Alison Johnstone (Lothian) (Green): I have no interests to declare.

The Convener: Thank you very much. I invite Mark McDonald to do likewise.

Mark McDonald (Aberdeen Donside) (SNP): I have no relevant interests to declare, convener.

The Convener: Thank you very much.

Smith Commission for Further Devolution of Powers to the Scottish Parliament

09:01

The Convener: We move on swiftly to agenda item 2, which is on the Smith commission.

I warmly welcome Lord Smith of Kelvin and thank him for agreeing to come to this committee first before any other committees. I know that he has taken up lots of media opportunities since the announcement last week, but this is his first committee appearance anywhere since the publication of the commission's report.

I also welcome Jenny Bates, the head of the secretariat of the Smith commission, who is here to assist Lord Smith in giving evidence.

Before I invite Lord Smith to make any opening remarks and to present his report to us, I remind the committee that his role has been as a mediator and chair of the Smith commission and that, ultimately, it was for the political parties to agree any deal that was done. I ask everyone present to remember that when it comes to questions.

After Lord Smith's remarks, I will ask a very general question; Lewis Macdonald will then do the same. We will then look at each major area to ensure that we use our time properly. We will probably deal with tax, welfare then constitutional issues, so that we keep everything together. I ask members to stick to that structure and to try not to jump ahead. Obviously, they should catch my eye if they feel that they need to do so.

Our time with Lord Smith is pretty limited—he has other commitments, which is totally understandable. If members can keep their questions brief—I will try to do the same—we can probably make more progress.

Do you wish to make any comments, Lord Smith? Then, we can open it up to questions.

Lord Smith: I have an opening statement to make, if I may.

The Convener: Sure. Go ahead.

Lord Smith: Thank you very much for your invitation to join you today and for the opportunity to make a brief opening statement.

Let me begin by thanking Parliament, which has supported our work throughout. We have benefited from the secondment of excellent parliamentary staff to our secretariat. The Parliament also hosted our talks on a number of occasions, most notably our public session at which we heard from civic leaders. I have

personally valued the counsel of the Presiding Officer throughout the process.

On appointment to my role, my first act was to visit the Parliament to listen to the debate on the referendum, so it is fitting that another visit is one of my last acts.

I wanted to take the opportunity to make a short opening statement to make four very brief points.

First, we achieved cross-party agreement. It was tough and intense at times and I feared that we might not get there, but we did, and all five parties signed up. That in itself is important and I pay tribute to the nominees for that. The agreement is their agreement; I just helped them to get there.

Secondly, we had a fortunate starting position. Almost all the parties entered the talks having already undertaken their own analysis and discussion. They had already reached important conclusions on how the powers of the Parliament should be strengthened. Without that work, I have no doubt that it would have been much more difficult, if not impossible, to reach a conclusion in the limited timescale that we had.

Thirdly, we had some great support. I was backed by an exceptional secretariat, drawn from the Scottish Government, the Scottish Parliament and the United Kingdom Government. The secretariat was supported by both Governments, who provided analysis and advice all the way through the process to ensure that the agreement could be delivered and would work. I am pleased to be joined today by Jenny Bates, who led the secretariat throughout the process.

Finally, I will say a few words about my role. My job was straightforward: to convene and chair cross-party talks. I had no voice in the debate and I have offered no view on the outcome. I entered the process politically unaligned and without a clear view on the constitutional debate, and I would like to leave it that way. It is not for me to provide a commentary on or an interpretation of the agreement or an analysis of its impact, and I do not believe that it would be right for me to do so even today. The weight of the appointment has never been lost on me. It followed what I consider to be one of the most extraordinary political events of my lifetime: the referendum. I never for a moment expected the agreement to satisfy everyone, as that would be impossible. Some people strongly believe that the agreement does not go far enough and some believe that it goes too far, and I respect and understand both those positions. My object was to chair a process that was well run and fair and that resulted in a package of new powers to strengthen the Parliament. I believe that we have achieved that.

I would be delighted to take questions.

The Convener: Thank you very much for your opening statement—I am grateful for it.

Many people have recognised that one of the cleverest decisions that the late Donald Dewar made in negotiating the Scotland Act 1998 was to tackle the issue of what powers would come to the Scottish Parliament by reversing the question and asking his then Cabinet colleagues to justify what would be reserved. That is why the act has a list of reserved powers rather than devolved ones. If something is not listed in the act, it is devolved.

What was the nature of the approach that you and the commission followed? Did you start with the premise that, unless a power could be justifiably reserved, it should be devolved, or did you assume that all matters should remain reserved unless all parties present at the commission and the UK Government could agree that they could be devolved? Arguably, the latter approach would always result in fewer powers for Scotland, so it would be useful to understand your approach.

Lord Smith: It was almost a hybrid of those. As I mentioned, I came to Parliament to meet the leaders of all the parties and I asked them to nominate two people from their parties. I said that one of them ought to be an MSP, because I wanted to reach deep into the parties rather than have gurus, if you like, as we might have reached agreement with them but then had to get political backing. I said that, within two weeks, I wanted the parties to give me their position on what powers should be devolved. I did not say that those should be maximised and I did not ask what should be reserved—I asked about the powers that should be devolved. Because we had the reports by Lord Strathclyde and Ming Campbell and various other papers from the parties, within two weeks all five parties produced their thoughts on what it would be right to devolve. Therefore, when we got to our first plenary meeting, we all knew what the various positions round the table were. From there, I tried to get some sort of common ground between the parties. That is how I went about it.

The Convener: I want to dig a wee bit further on the process and how it was set out. Was the working principle behind the overall package the UK pooling and sharing model, as described by the Westminster party leaders in their statement on the vow, in relation to areas such as welfare and social security, or was the principle that we should maximise autonomy?

Lord Smith: As I have said, at the very first meeting we agreed seven principles—well, we subsequently agreed that we had agreed them. We wanted

“a substantial and cohesive package of powers, enabling the delivery of outcomes that are meaningful to the people of Scotland”;

we wanted to

“strengthen the Scottish devolution settlement and the Scottish Parliament within the UK (including the Parliament’s levels of financial accountability)”;

and we wanted

“a durable but responsive democratic constitutional settlement, which maintains Scotland’s place in the UK”.

We said that the agreement should

“not be conditional on the conclusion of other political negotiations elsewhere in the UK”,

which is an issue that may come up later in questioning. We said that, as the powers move, the agreement should “not cause detriment” one way or the other and it should

“cause neither the UK Government nor the Scottish Government to gain or lose financially”

simply because we are devolving power. It should also be “implementable”. Those were the principles that we worked to.

The Convener: Thank you very much. It is helpful to understand that at the beginning.

Lewis Macdonald (North East Scotland) (Lab): I have read very carefully the foreword to the report and your other comments about the work of the commission. Clearly a number of imperatives were operating on you and I would be interested in your comments on them, particularly the requirement on the one hand to achieve a consensus, with agreement among the parties, and, on the other hand, to define a coherent set of proposals. There is also the work that you initiated and did yourself to make sure that other voices were heard in the commission’s work. How did you balance those imperatives and choose how you would ensure that they were all reflected in the work of the commission?

Lord Smith: This theme will come across all the time: I did not choose anything; there were 10 people around the table and they were making the decisions. I was just bringing my skills as a chairman to make sure that people met somewhere, and I do not mean on the lowest common denominator; I mean on the powers that people could agree are useful for Scotland.

As well as getting initial submissions from the five parties, we encouraged the public to write in. We got more than 18,000 e-mails. Even if you take out the slightly scurrilous ones, there was a lot of information in there that the politicians had to take into consideration. I also wrote to 129 civic organisations—from trade unions to third sector, voluntary and business organisations—and other interested people, and 407 of them replied. There are more civic organisations out there than even I had realised.

The submissions that came in from those people were of a very high quality. Within days of receiving them, we had them up on the website so that the process was transparent. We shared them immediately with all five parties. We were informed hugely by what we learned.

You probably know that I also went walkabout in Scotland. I went from the Borders, which was easy for me, around Scotland to Aberdeen, Inverness, Dundee, Stirling and Glasgow and so on, and I met quite a number of people. They were not getting preferential treatment; I simply wanted to hear the word on the street and the mood music, to add to the submissions that were coming in. We based the report on the submissions, which helped to inform our discussion and to supplement the five submissions that had come in from the political parties.

Lewis Macdonald: I fully acknowledge that the coherence of the proposals is not ultimately your responsibility, but I was interested in the efforts that you made. As you say, you travelled the country and encouraged and went out and sought submissions. I want to understand the means by which you ensured that the responses were not just fed in but were reflected in the discussions among the parties.

Lord Smith: We had two meetings—or a meeting split into two—at Holyrood and a number of civic society people came in. The five parties were able to address them and to ask them to explain what they were saying more carefully.

We made sure that we looked at all the themes that came out of the e-mails from civic society and we talked about those openly around the table.

Lewis Macdonald: That is very helpful. You have said that concluding the report required some parties to move further along the devolution route than they might have wanted and that others had to accept an outcome that fell short of their ultimate ambitions. Since you stood up on Thursday morning, do you feel that the parties have accepted the outcome of the commission and supported it in the spirit in which you presented the report?

09:15

Lord Smith: I think that they have accepted it. Obviously, I have read what has been said by people since then. I respect the position of people who take one particular point of view. If you believe in independence, you are still going to believe in independence. People’s political convictions have not changed. If they want full independence, with all the powers here, I absolutely understand that. However, for the purposes of this commission—which I would now like to be called an agreement, by the way, as

commissions tend to last for a couple of years and take evidence from people and so on, whereas we took 10 weeks—all five parties were happy for me to stand up and say that we had arrived at an agreement among all parties, and that is unprecedented; it has not been done before. Calman did not work that way, and the original settlement did not work that way. All five parties signed up to this agreement; but, of course, they have their own political convictions outside that.

Mark McDonald: I have a question that might help us to segue into the taxation element. I will pick up on the commission's seven principles, and particularly principles 5 and 6, which are that the proposals should

"not cause detriment to the UK as a whole nor to any of its constituent parts"

and that they should

"cause neither the UK Government nor the Scottish Government to gain or lose financially simply as a consequence of devolving a specific power".

The question of detriment could be said to be subjective in some ways. For example, we have seen the recent response from the UK Labour Party on air passenger duty, which involved it writing a letter to the Chancellor of the Exchequer that implied that there could be detriment as a result of devolving that duty. What analysis was applied to those principles from outwith the commission's members to inform the conclusions that were arrived at?

Lord Smith: I will ask Jenny Bates to speak about that in a moment, but I can say that, every time we spoke about devolving a particular power, we did quite a bit of research. We asked the UK Government and the Scottish Government in particular to provide research to us. I well remember that on one occasion the UK Government sent 330 pages and, not to be outdone, the Scottish Government sent a bigger document with, by the way, a slightly different analysis and conclusion—all based on empirical evidence, of course.

Incidentally, the evidence was coming from the UK and Scottish Governments, and members of parties that are in those Governments were getting that information directly. We said to the UK Government and the Scottish Government that Labour and the Greens were being disadvantaged by that and asked that copies of the information be provided to them as well. Both Governments agreed to that, which meant that all the information was given to all the parties around the table.

When we considered what would be detrimental—of course there is subjectivity in that—we looked carefully at whether there would be detriment to either Government and whether

either Government would gain or lose financially as a result of the proposals.

Jenny Bates (Smith Commission): Given that the parties had all submitted proposals to the commission, we ensured that the analysis and the evidence from both Governments covered every proposal that had been put to the commission, so that we had information on every proposal for a devolved power. Some material that we received from civic organisations had evidence attached to it, so some people sent us evidence and analysis, as well as views about which powers should be devolved. That was factored into the discussions, so that we ensured that every decision that the parties looked at was based on some understanding of the impacts of operating powers.

Mark McDonald: Did any recommendations come out before the final report on the basis of the principles or on the basis of input?

Lord Smith: The short answer is yes. I have been reading blow-by-blow accounts in *The Herald* and *The Scotsman* and so on about exactly what happened inside the room, and I do not want to go into that. There were proposals that we felt could have caused detriment and proposals that looked as if they might be unworkable. We had to consider the practicalities and the implementability of a lot of these things. We felt that we could not go forward with some things.

Mark McDonald: Was that quite late in the process? The media reports have spoken about there being draft conclusions that were revised following input from outside the commission.

Lord Smith: We had nine plenary meetings and there were nine drafts. Things were changing all the time.

By the way, the hands that were shown shredding a copy of the report in the *Sunday Herald* are not my hands. Mine are quite stubby, and the fingers in the photograph were impressively long and elegant.

Rob Gibson (Caithness, Sutherland and Ross) (SNP): Good morning, Lord Smith. One of your four opening points was that you got support, analysis and advice from the Scottish Government and the UK Government. You said that, ultimately, the five parties made the agreement, but the advice from the Scottish and UK Governments must have weighed heavily in some instances. How did the parties' views weigh against the Governments' advice, particularly in the final draft of the report?

Lord Smith: First, I pay tribute to the quality of the people who were sitting round the table. People might smile, but I genuinely mean that. I have had a long career in the private and public sectors, and the 10 people sitting round the table

were high-quality people. I believe that they took their own positions on a lot of things. I am sure that they were being fed advice from superiors—can I call them that?—in their various parties, but they were listening to arguments, taking part in discussions and arriving at conclusions, I believe, from their own thoughts as much as through being informed by the Scottish Government, the UK Government or anyone else out there. They were amazingly robust in the discussions.

Rob Gibson: I will leave it there.

The Convener: I guess that, whether you had said “seniors” or “superiors”, both words would have got you into trouble. [*Laughter.*]

Lord Smith: I am new to politics, convener—and, by the way, I am going to remain new to politics.

The Convener: Before we move on to taxation issues, Drew Smith has a question.

Drew Smith (Glasgow) (Lab): I have two questions, convener, but I will ask them together in the interest of saving time, if that is okay.

Good morning, Lord Smith, and welcome to the committee. You mentioned some of the reports that we have seen in the media since the commission’s report was published. You were clear while the commission was sitting that you wanted a degree of confidentiality and that you thought that that was important to the process. I suppose that, once such things start, it becomes inevitable that, if one version of events goes out, a differing view will be put. Do you want to express a view on that?

To what extent did the pressure of time that hung over the process help you to drive towards consensus? Is it the case that, if the time pressure had not been there, you might not have been able to achieve as much as you did, or was it a difficulty throughout?

Lord Smith: Will you remind me of your first question?

Drew Smith: It was about confidentiality—

Lord Smith: People talking after the event.

Drew Smith: Yes.

Lord Smith: I have already alluded to that. I absolutely respect people’s political opinions, and they have to speak to their people outside. I know that the negotiations that I was party to and which I chaired were conducted in a good spirit. They got heated from time to time, but there was humour as well, and all five parties agreed to what we wrote down, line by line. They all bought into that.

I am sure that people have political ambitions beyond that, and there might be people in parties

who felt that they had gone too far, but that is what we agreed at the time, and I have not heard any of the parties turn round and say that they thought the process was wrong. They all say that it was well conducted and I believe that they all stand by the outcomes. I am not particularly disappointed by anything that has been said, and I respect people’s right to speak.

I think that the timing worked in our favour. Had I been given two years to do the work—by the way, I would not have taken the job in that case—we would have had all sorts of additional analysis and so on. The subjects have been talked about in great detail. We have had the Menzies Campbell report, the Strathclyde report, the Scotland Act 2012, the Christie commission report and various other things. Lots of things have been written. The parties were able to come up with reasoned arguments within two weeks because the material was there. I always feel that, if people are allowed another three months, they will take another three months.

Did we manage to do enough analysis? Let me tell you, there was a cottage industry in the civil service south of the border and up here with people producing information. If we needed to know about a particular tax or welfare provision, we got experts in the Department for Work and Pensions, the Treasury or the Scottish Government to produce information for us quickly.

This stuff is implementable; I know that it is. We have argued it through. Some of the detail might not be there, but we know that it is implementable, because we did sufficient research.

There are those who say that we did not have enough time. I reject that. We had enough time and we have arrived at a conclusion. There are those who said, “You’ll never get five parties to agree.” We got five parties to agree, whatever is being said outside now, so I am relaxed about the process.

The Convener: I would like us to move into the more general area of taxation now.

Alison Johnstone: I will explore the rationale for where the boundary was drawn between taxes devolved and taxes reserved in a couple of cases. How did the commission agree that receipts from the first 10 percentage points of VAT should go to the Scottish Government’s budget?

Lord Smith: We looked at assignment because VAT cannot be devolved. VAT is controlled by the European Union and it cannot be split. Scotland cannot have a VAT rate relative to the rest of the UK, so the VAT rate has to be set somewhere. We had to decide how much of that could be assigned, and there were discussions about whether there could be a 15 per cent rate, which is the minimum rate in Europe.

We discussed the subject. There were arguments about the volatility of tax receipts and about how far we should go with such things. If a lot of money is raised in one area—we are talking about something like £9 billion in VAT receipts in Scotland—the question is where the line should be drawn.

Eventually, we came out with a figure of 50 per cent of the rate. Please note that that is 50 per cent not of the receipts but of the rate, and that was fixed at 10 per cent. If Scotland prospers as a country, the receipts from that 10 per cent will grow. If something happens to Scotland's economy, the receipts will go down. If, for example, there is more cutting by the UK Government, that should not directly affect receipts, because the receipts from the 10 per cent VAT rate will come out of the block grant and will stand alone.

That is riding on the Scottish economy, and with power comes responsibility. That part will fund a big chunk of welfare spending and other spending in Scotland. Why 10 per cent and not 9 or 15 per cent? I wish that you had been inside the room to take part in the discussion, but that is where we came out. Patrick Harvie is looking embarrassed now, and rightly so.

Alison Johnstone: If we look at corporation tax—

The Convener: I am sorry, but could I seek clarity on that issue before we move on to corporation tax? I understand that the VAT package involves an assigned revenue. Is it therefore the case that, as in the past, if there is an assigned revenue, there is also a reduction in the block grant at the same level? If so, will there be a net benefit? I need a bit of clarity, because I am not sure about that.

Lord Smith: At the time of transfer, there should be no benefit and no loss, but a direct deduction from the block grant is involved. Jenny Bates, our Treasury expert, is nodding. When the money is passed over, there is no plus or minus. It comes straight off the block grant and is raised against the economy as 10 points on VAT.

The Convener: After the first year and the first implementation, will there be no yearly adjustment?

09:30

Jenny Bates: The way to think about is that something that is funded by the block grant is being switched for something that depends on what happens to VAT revenues. In the past, the change over time would be a function of what happened to the block grant. In the future, the change to revenues will be a function of what

happens to VAT revenues. They normally grow a bit over time, based on inflation in the economy—the nominal figure usually goes up. Lord Smith is making the point that variability in that income will be a function of what happens in the economy. As consumption goes up, we get more VAT revenues; if consumption goes down, we get less in VAT revenues.

The Convener: The main question that I asked was whether the block grant will be adjusted. If VAT income increases, will the block grant be reduced in the annual settlement to reflect that?

Lord Smith: If variable activity goes up, the Scottish Government keeps the increase. That will rise and fall on economic activity: if more VAT is paid, the Scottish Government will keep the income from 10 points of that.

The Convener: So there will be no adjustment to the block grant. It is useful to get that clarified. That is different from how the assignment process normally works.

I am sorry for interrupting Alison Johnstone.

Lord Smith: I think that the question was on corporation tax.

Stuart McMillan (West Scotland) (SNP): Can I ask a question?

The Convener: Is it on VAT?

Stuart McMillan: Yes.

The Convener: Sure.

Stuart McMillan: This may be a hypothetical question, but in the process did you look ahead to any potential policy changes? I am not suggesting any particular changes, but if the Government decided to change the VAT rate or how VAT is implemented or, further down the line, to remove VAT from a particular area, how would that affect Scotland and Scotland's revenues?

Jenny Bates: This process is about the devolution of a power, rather than how the power is operated. That was a common principle across the commission's work: we looked at whether a power should be devolved, rather than the policy choices that might be made once that power was devolved. That was the general way that we went about our work.

As Lord Smith said, the way that VAT assignment would work is that, given that Scotland would take the first 10p and the rest would go to the UK, if the UK rate changed from 20p, the change would not directly affect the amount of revenue that Scotland would receive. As we said, what does affect the revenue that Scotland would receive is the nature of the economy in Scotland: whether it is growing faster or slower.

Lord Smith: Stuart McMillan's question is also a technical one about what would happen if someone decided that children's shoes—or whatever it happens to be—should no longer attract VAT or should attract VAT.

Jenny Bates: There are two points to make in relation to that. First, as the committee will be aware, VAT is a Europe-wide tax and decisions about it are taken at the European level. Changes to VAT would need to be decided at EU level; that is how the policy would be made.

Secondly, if there was a change to the base, in either direction, in terms of the things that are or are not taxed, that would affect the revenue that is received.

Stuart McMillan: Has a mechanism been built in regarding the consultation that the Scottish Government could have with the UK Government if VAT was removed from an item?

The Convener: That is about the detail of how the Governments operate the system in future.

Lord Smith: We have said very strongly in our report that consultation between Governments must be improved. I said that in the four items that I raised, but we also have comments in the report about the fact that the Scottish voice must be listened to. I am certain that that will be picked up.

The Convener: Alison Johnstone, I am sorry—

Lord Smith: Yes, corporation tax.

The Convener: We go back to corporation tax.

Alison Johnstone: How was agreement reached to devolve APD while a decision was made to reserve corporation tax? You could apply similar arguments to the impact that both might have. If APD is devolved we might see a race to the bottom; the same argument has been used time and again in discussions about corporation tax. I would like to better understand how those decisions were reached.

Lord Smith: This is where the input from civic Scotland and others was very important. There was overwhelming demand for something to be done about APD, which came from several different areas. Businesses said that moving from a hub down to London, for example, to do business makes business life in Scotland very expensive, which disadvantages us, and they asked whether something could be done about that and whether we could have the power to at least think about that. There was also a huge voice from people in tourism, who said, "We're being disadvantaged—here's an opportunity."

I am not speaking out of school, but I imagine that the Greens might well take the view that they would like us to have control over APD because

they are concerned about CO₂ emissions and so on. What happens to powers when they are devolved is entirely a matter for the politicians who will exercise those powers. Many people wanted the power over APD to come to Scotland; I did not hear many arguments against that happening.

The position on corporation tax was different. Corporation tax is an interesting lever, but a large number of organisations in civic Scotland, including the Scottish Trades Union Congress, employers organisations such as the Confederation of British Industry, and even the Institute of Chartered Accountants of Scotland—of which I am a member and which cannot be attacked for lacking objectivity—said that we should not tinker with corporation tax, because that would lead to strange behaviours and, in the end, we would regret it. That was the message from the trade union side, employers and disinterested observers who understand tax. There was a very strong view that we should not interfere with corporation tax, never mind what the politicians around the table were saying.

There has been talk of the possible devolution of the power over corporation tax to Northern Ireland. We were aware of rumours to that effect. It is in such situations that a chair steps into his own. I said that we should remember that our discussions were not conditional on the conclusion of political negotiations elsewhere in the UK and that we needed to consider what was right for Scotland. I said that, if it was right for us to devolve corporation tax, we should talk about that and how it would happen, but if it was not right to do so, we should ignore what was happening elsewhere. The fact that someone somewhere else might be getting a bag of sweets was not a reason for us to get one; we needed to ask why we wanted that bag of sweets. We talked about the issue at great length and eventually decided that power over corporation tax was not something that it would be in the interests of Scotland to have.

The Convener: Just for the record, was a view sought from HM Treasury or the Chancellor of the Exchequer's office when you discussed the Northern Ireland situation?

Lord Smith: We sought views from the Scottish Government, the UK Government, the Treasury, the Business, Innovation and Skills Committee, the Office of Gas and Electricity Markets, and the Department of Energy and Climate Change. We spoke to a whole range of people about what was possible and what their views were, but the views that we signed up to were our views.

The Convener: Was that the case specifically on corporation tax?

Lord Smith: Absolutely. That decision was made inside the room.

The Convener: Three other members have indicated that they have questions. I am keeping an eye on the time, because we need to rattle on a bit.

Bill Kidd (Glasgow Anniesland) (SNP): Thank you for all the work that you and your commission have carried out, Lord Smith.

I have a question about the suggested increase in borrowing powers, on which I am by no means an expert; Ms Bates might be the right person to ask. The fiscal baseline that is envisioned will undoubtedly include the Barnett formula as well as variations in taxation that might be made by the Scottish Parliament. In enacting the proposed powers, would the Scottish Parliament or the Scottish Government be left in a position of relative advantage or relative disadvantage? I know that you say that there should not be any advantage or disadvantage, but given that an element of the situation is the fact that agreement still has to be reached on the Barnett formula, how do you see the borrowing powers being used to support capital infrastructure projects?

Jenny Bates: The report recommends that borrowing powers should be increased substantially in agreement with the UK Government. The detail of the borrowing powers will be sorted out as part of the implementation of the Smith commission. What happens to those additional borrowing powers is ultimately a decision for a future Scottish Parliament. It is a bit difficult to say, sitting here, what the effect of that would be. A future Parliament will need to decide how it wants to exercise and use those powers.

Bill Kidd is right about the Barnett formula. The report is very clear that the Barnett formula will continue to operate for the block grant. Under these proposals, the block grant would continue to operate and the Barnett formula would continue to be the mechanism that determined the block grant.

Lewis Macdonald: To follow up on that question, did you take evidence, as a commission, on how the Barnett formula would be updated in view of the changes included in the agreement? If so, is that evidence relevant to the work that the Governments will clearly have to do in the next few months?

Jenny Bates: There was a fairly strong consensus around the table that the Barnett formula would remain, and that is what the commission has agreed. We did not look in a lot of detail at how it would be changed or amended. The commission has just said that it is something that should continue to operate.

Rob Gibson: Lord Smith, the National Union of Students Scotland has welcomed—as I do—the proposed powers for the Scottish Government to set rates and thresholds for income tax raised from non-dividend and non-savings income. However, we are concerned that the exclusion of dividend and savings income from the reach of the new powers will mean that the Scottish Parliament is unable to exercise its own tax policy, as NUS Scotland says, “where it matters most”. I am interested to know how you came up with that formula.

Lord Smith: I go back to the powers that the Scottish Government has at the moment, or will have after the 2012 act comes in. It takes about three years for these things to bite, as you will have gathered.

Even with the 2012 act, the Scottish Government will have the ability to vary tax rates by 10 percentage points. There are three tax rates: 20 per cent; 40 per cent; and 45 per cent. The Scottish Government will be able to vary those rates, but in lockstep. If you want to increase your 45 per cent to 50 per cent, your 40 per cent has to go up to 45 per cent and your 20 has to go up to 25. If you want to take five off, your 20 goes down to 15, your 40 goes down to 35 and your 45 has to come down to 40.

In our agreement—as I like to keep calling it, because it is much more powerful, and I expect the people around this table to ensure that this agreement finally finds its way into the statute book—changes are not in lockstep. You can increase rates and bands and reduce rates and bands. You could raise this rate, reduce that rate and keep that one where it is. There is a huge amount of power and leverage, which, by the way, amounts to £6.8 billion of income. The responsibility for how you go about that will now rest with the Scottish Parliament, but I think that that gives huge income.

We were concerned about starting to interfere with savings, dividend income and interest income. There is a huge industry in Scotland and a lot of people’s pensions are dependent on these issues. If we start to create differences across borders in areas such as pensions, we are taking a very big step that could lead to a lot of confusion.

Rob Gibson: Just to follow that up, when there was a 50p tax rate under the previous Labour Administration, the highest earners were often able to avoid tax by receiving bonuses or non-dividend income. That means that the potential under income tax is restricted considerably in order to be able to raise that money, whether it is down south or here.

Lord Smith: We are talking anti-avoidance here. I am absolutely for anti-avoidance. The UK Government speaks strongly about that; a Scottish Government ought to be the same. I have no truck with people who avoid paying income tax.

Incidentally, I am much older than most people in this room and can tell you that, at one point when I was a young lad, people in the UK paid income tax at 83 per cent and tax at 98 per cent on what was charmingly called unearned income—savings, dividends and so on. Therefore, we have been in different regimes. I am not suggesting that those rates should apply in Scotland; I am just saying that they have happened in the past.

09:45

The Convener: I am watching the clock, and we need to move on to welfare.

Lord Smith: I am honestly not filibustering; I just talk too much.

The Convener: I would not let you filibuster anyway, so do not worry about it.

I think that Mark McDonald indicated earlier that he would like to ask about welfare.

Mark McDonald: Yes. I would like to ask a couple of questions about welfare. I will make them brief, convener.

Lord Smith, you have mentioned a number of times the input from civic Scotland. There was an overwhelming, almost universal call from civic society, charities and so on for full welfare powers to be devolved to Scotland. What was the bulwark against that that led to the conclusions in the commission's report?

Lord Smith: As you know, the universal credit system is a major new reform in the welfare system. The parties agreed that it would be quite difficult to break that asunder but that Scotland could have flexibilities around it, particularly in things such as the housing element.

You know that a lot of housing is already devolved, so the Scottish Government having the housing element of the universal credit made a lot of sense as there would be complementarity. There are quite different housing issues in Scotland compared with elsewhere in the UK. Housing payments could be increased or reduced, there could be flexibility around timing and so on. However, it was felt that to attack universal credit was not somewhere we could go in arriving at a consensus in the room.

Outside universal credit, around £2.5 billion of extra cost benefits are being fully devolved. They are things such as the disability living allowance and winter fuel payments—there is a whole list of

them in our report. Currently, £400 million of benefits are under the Scottish Government's control, so an extra £2.5 billion is quite an increase in that area.

Mark McDonald: To go back to the discussion that we had earlier, the reporting has suggested that universal credit was in a draft report and was dropped quite late in the process. Is that a fair reflection of what happened?

Lord Smith: The final report is the final report. I am not prepared to go into things blow by blow and into who said what to whom.

Mark McDonald: Okay. That is fine.

You mentioned and the report refers to the flexibility for Scotland to create new benefits. Obviously, that responsibility would have to be funded accordingly. The question around coherence is the same that we have just had in the taxation discussion. Without a panoply of tax options to create the funding to derive those new benefits, they would have to be funded through reductions elsewhere, the dropping of other benefits, or the use of income tax as the only instrument. Did the coherence element play any role in the discussions about creating new benefits but not necessarily having the broad tax power base to be able to fund them?

Lord Smith: The block grant is used in different ways, too—that is available. In fact, around half of the funding of the devolved powers would still be in the block grant and around half would be in directly raised funds, including the VAT assignment. Very roughly speaking, there is £6.8 billion from income tax, an existing £4 billion or so, and around £4.5 billion for VAT, which adds up to around £15 billion out of the £30 billion or so of spend. It is then up to the Government to make choices.

Mark McDonald: I have a final, very brief question.

Disability living allowance—or personal independence payment, as it will become—has been mooted for devolving to Scotland. Obviously, there are currently proposals for reductions in that budget and for changes to the criteria by which people can qualify for payments. Was that factored into the discussions when devolving that power and future projections were looked at?

Jenny Bates: The general principle was that the commission was looking at which powers to devolve and basing the discussions on the powers that were already available. The precise detail of how to proceed is something for the two Governments to look at as they implement the proposals. You are right to suggest that many policy areas are continuing to evolve and move

even as we speak and that they will continue to do so as the process of implementation takes hold.

Lord Smith: This is where Governments have to talk, and we have made the point very strongly that the Scottish voice needs to be heard.

The Convener: I call Stuart McMillan. As quickly as you can, please.

Stuart McMillan: Sure, convener.

Using as a baseline the fifth and sixth principles of the Smith commission's work—in other words, that the powers would “not cause detriment” and would

“cause neither the UK Government nor the Scottish Government to gain or lose financially”—

I wonder, with regard to welfare and particularly paragraph 54 of the report in relation to the creation of new powers, what the rationale behind that area was. Surely if any Government or indeed the Scottish Parliament wanted to utilise those powers and create new benefits there would be a financial cost implication.

Lord Smith: Yes, there would. If the Scottish Government wanted to bring in additional benefits, it would have to find some way of paying for them. That is almost the exact answer to the earlier question that was asked.

Stuart McMillan: But that being the case one could argue that the Scottish Government could be put in a negative position, or at a disadvantage compared with the current situation.

Lord Smith: If it decides to pay additional benefits, it will have to fund them. It cannot say, “We want to pay additional benefits—can we have the money to do that?” That money will have to be found.

Stuart McMillan: Okay.

The Convener: I seek one point of clarification on universal credit before we move on to the constitution. I know that you cannot go into any detail about which party said what—I do not expect you to do so—but was the decision about universal credit made on the basis that it was technically impossible or that it was politically difficult?

Lord Smith: What is the right answer to that, Jenny? [*Laughter.*] A general and useful discussion was had, and a consensus was arrived at. Is that not a good enough answer, convener?

The Convener: The question is a pretty reasonable one. I am not asking for specific details.

Jenny Bates: The answer is that we looked at the technical implementation of the proposals and whether you would want to devolve the full amount

of universal credit, and both factors played into the discussion. Like many of the conversations we had, the conversation was about the right view on what should happen and how much power should be devolved.

The Convener: So the power could be devolved, but the issue was whether it should be.

Jenny Bates: What I can say is that both issues were looked at in the discussion about universal credit.

The Convener: Okay.

Lewis Macdonald: But it was agreed that the coherent thing to do was to keep it together, with the flexibilities around housing and timing that you have described.

Lord Smith: Yes.

The Convener: We move on to constitutional stuff. I believe that Drew Smith wanted to ask about that issue.

Drew Smith: Yes. Thanks very much, convener.

Lord Smith, you have mentioned a number of times that the two Governments will need to work together on certain issues. I suppose that the hardy perennial of the discussion about Scotland's constitution is the question of how we create partnership arrangements. You highlighted that issue in your report, but I wonder whether you wish to share with the committee or put on record your thoughts about what needs to change in that respect.

Lord Smith: I preface my response by pointing out that, if all of this is enacted, a huge amount of authority will come to the Scottish Parliament. It will be able to decide the number of MSPs; it will be made permanent in UK law; 16 and 17-year-olds will be allowed to vote, if it so decides; and there could be boundary changes. All sorts of things will be available, and an amazing embodiment of power will come to the Parliament.

What was your question again?

Drew Smith: There has been discussion about the workings of joint ministerial committees in the past and how the Parliaments come together. Do you have any thoughts on those matters?

Lord Smith: It became very obvious to me and, I think, to other members of the commission as they listened to civic Scotland that the comments were not just the perennial ones about how, in fisheries and agricultural policy—both of which are very important to the Scottish economy—we are not really listened to. The process of devolution has led to Governments saying, “Well, let's devolve—we don't really need to talk.” That is just wrong.

Where common cause is made—on Europe, or on energy policy in relation to fuel poverty or energy efficiency—we should say, “Hey, is Scotland a wee bit different in this area?” and listen to the Scottish voice instead of having a one-size-fits-all policy. You know which areas I am talking about—for example, there is a different type of fuel poverty in Scotland.

We are saying to institutions such as Ofgem and DECC—I hope that you do not mind if I use shorthand; you know that I am talking about the Department of Energy and Climate Change—and in relation to European and other matters that there ought to be mutual respect between the two Governments. They ought to listen to each other and communicate in a whole range of areas.

You are most likely always hearing comments such as, “Hey, our fisheries are not being represented.” We are saying not just that we have to try harder, but that there should be a memorandum of understanding so that the voices are heard. In the case of the Office of Communications or Ofgem, we would say that consultation with the Scottish people must take place in advance of new policies on broadcasting or energy being brought in.

That is all we are saying. The system is kind of broke and is not working perfectly, and that is getting in the way. I am talking about civil servants, too. If we fix things quite formally at ministerial level, there will be an opportunity for such an approach to cascade down.

Drew Smith: That is a helpful contribution to the debate. I would like to hear more of what you have to say on that, but to move the discussion on I will ask you about another issue that you raised, which is public understanding of the constitutional framework in Scotland. To what extent is the stability and success of your agreement—of our agreement—dependent on a level of public understanding of where power lies that goes beyond the present level.

Lord Smith: That is fundamental. I was quite surprised, on my travels, to have people say to me, “You must ensure that the health service is a matter for the Scottish Parliament.” I was even surprised myself to find out that the health service was devolved in 1948, when I was four. It was devolved then because all the health services were set up independently.

I knew from my schooldays that education has been devolved since about 1451—we just have a different education system in Scotland. However, there is a perception that we do not really control our health service and education system: that we think that we control them, but maybe we do not. There is a lot of confusion out there, even among people who I thought should know those things.

By the way, I thought that 16 and 17-year-olds had a better grasp of some of it.

We are bringing additional taxation and welfare powers to Scotland, but, for those things to work, people need to understand what is in the hands of the Scottish Government. People in the UK and in Westminster also need to understand what has been devolved. There is a lot of misunderstanding about that. All I am saying is that, as well as having Governments talking together, for goodness’ sake let us ensure that people understand what is devolved and how it works.

Drew Smith: Finally—I will let in other colleagues in just a moment—do you find that surprising? We have just had a referendum debate, and comments are often made about how educated our whole country has become in matters political, which is seen as a positive thing. People seem to have stronger and better articulated views on how they would like the country to be run, but they do not seem to have a great understanding of how it actually is run.

Lord Smith: There is still a long way to go, but I think that what has happened this year—and, to an extent, last year—in the run-up to the referendum has been important. Of those who could vote, 85 per cent actually voted and engaged in the process. People I know who do not have a political bone in their body were asking questions about how things are run and so on—incidentally, those people have not gone away. That is a good thing for democracy.

In case we run out of time, I make a plea that the people round this table ensure that the work that we have done over the past 10 weeks is seen through—from its current agreement form into legislation—and that some of the things that I have pointed to on improving people’s education and knowledge about what is happening are done, too.

I am sorry—that was a long-winded answer.

10:00

The Convener: I bring in Mark McDonald quickly, before Lewis Macdonald deals with issues on which Lord Smith made personal recommendations.

Mark McDonald: I will be very quick.

You mentioned creating permanence for this institution in law. Given that there is no written constitution in the UK and that no Government by definition can bind its successor, how do you envisage that being a reality?

Lord Smith: The UK law will say that this institution is permanent; that is our intention. However, nothing—since the Magna Carta, I

think—can be permanent; I am told by constitutional experts down in London, in what used to be called Dover house but is probably now called Scotland house, that that cannot be done because it would bind future Parliaments. However, we intend the law to be written in such a way that a plague of boils or something will break out if anyone ever decides to prorogue—or whatever you want to call it—this Parliament. The language will be as strong as it is possible to be.

You are absolutely right that nothing is permanent, because future democratically elected Governments could change that permanence. However, this Parliament will be permanent and it will be described as permanent in UK law. Of course, as I say, UK law can be changed.

If you know a way of making the institution permanent, tell me, because that is the Scottish people's will.

Patrick Harvie (Glasgow) (Green): There was a way.

The Convener: It is called a written constitution.

Lord Smith: That is the next task.

The Convener: That would probably help the process, but we will not go there.

Lewis Macdonald: The Smith agreement, as you have described it very well, will create a Parliament with even greater responsibilities. That broadened range of responsibilities requires broadened expertise. The same is true of Government. I am interested in your recommendations on parliamentary and independent oversight of the Scottish Government with the extension of powers. Will you tell us a little bit about your thinking behind that and where the scrutiny that exists in the Scottish Parliament would fall short in relation to the additional powers to be made available to the Scottish Government?

Lord Smith: A number of people have said to me—I am just mouthing what they said—that the Scottish Parliament's committee system does not work as well as the one in Westminster. I do not quite know why, but scrutiny of what is happening is not as strong. By the way, I am going before a Westminster committee tomorrow, so I thank you for the opportunity to rehearse; I believe that it is a blood sport down there.

If you have huge powers to increase or reduce taxes and to do things on welfare, you need the Parliament to scrutinise those matters in plenary sessions as well. People will have to step up to the plate, if you like. If you are accountable now to an electorate for about £15 billion-worth of taxation and, with the commission's proposals, you will be accountable for direct devolved income tax worth £6.8 billion as a starting point, and if MSPs will be

able to decide how many MSPs there should be, what the electoral boundaries are and whether 16 and 17-year-olds get the vote, you will need to think very carefully about the great responsibility of being a mature Parliament. Part of that relates to the committee system; part of it relates to the Parliament operating properly and scrutinising everything that is going through.

Lewis Macdonald: I very much concur with your reference to the maturity of the institution being critical. The convener mentioned Donald Dewar. It was said that, because the committee system would effectively be a second chamber, a unicameral system would do, given the range of powers that were to be devolved. Has that changed, given that the committee system has perhaps not lived up the expected scrutiny levels?

Lord Smith: I am only reporting what people have told me. I had never actually sat in a committee until fairly recently.

Are you looking for a second house—a house of lairds, perhaps? By the way, I am not looking for a job there. I do not think that you need a second chamber at all. It would just add another complication. However, I have been told that you need to look at how the committee system works, how diligent the committees are and how strong they can be in calling a Government and other organisations to account. In our report, we say that we expect a number of organisations will have to come before the Scottish Parliament and I want that scrutiny to be strong as well.

With power comes responsibility; that is what I am really talking about.

Lewis Macdonald: On devolution from the Scottish Parliament to local communities, your conclusions say

“that will require significant further thought”.

Is that an additional layer of improving democracy within Scotland?

Lord Smith: I believe so. That was a very strong voice and it came through in all sorts of areas, particularly welfare, charities and so on. Cities and rural areas said that Holyrood getting extra powers is welcome and all very well, but in areas such as welfare and poverty, rural poverty is different from inner city poverty. It is absolutely proven academically that the closer that we get to the point of need, the better the welfare provision is, because providers understand what they are dealing with.

The power is in Holyrood and lots of people asked you to think about devolving more power down to the point of need in a lot of areas. That is all. It is just a voice in the street. I am not saying whether all five parties bought into that, but I heard

it time and time again. All I am saying to Holyrood is that, with the additional powers that you are getting—even with the existing powers that you have—you should think about devolving some of that to everyone's advantage.

The Convener: Rob Gibson has the last question. Please make it quick.

Rob Gibson: Scottish Parliament committees cannot compel witnesses in the same way that UK Parliament committees can. Should that change?

Lord Smith: That is a matter for democratically elected people such as you. I know that the Presiding Officer is looking at the committee system right now—more power to her elbow. I am not here to provide solutions. If you, as parliamentarians who were elected by the people, decide that you should have the ability to force people to come before committees, you should look at that.

The Convener: Thank you for coming, Lord Smith. I know that time was short this morning, so I am grateful to you for giving us your time. We could easily have spent two or three hours on this, but we recognise diary pressures.

What happens next? On Thursday, we have the UK Government and the Scottish Government, and I suspect that the questions will be a bit more searching about where we go now. Around the table we recognise the scale of our responsibility in ensuring that, when the legislation is eventually introduced, it is all practical.

My final piece of advice for Lord Smith is that blood sports have been outlawed, so you can tell them that tomorrow if they get out of hand. [*Laughter.*] I thank you and Jenny Bates for giving evidence this morning. I am grateful.

Meeting closed at 10:09.

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