



# **Powers for a purpose - strengthening devolution**

Scottish Labour Devolution Commission

Interim Report  
April 2013

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## Foreword

Scottish Labour is the party of devolution. We believe that a strong Scottish Parliament, within a strong United Kingdom, delivers the best possible outcomes for the people of Scotland. That is why a Labour Government set up the Scottish Parliament, and why we will fight to preserve it. It is our conviction that constitutions must serve the needs of the people.

I have established the Scottish Labour Devolution Commission to examine the existing devolution settlement. The question we have sought to address is: how can we strengthen the present constitutional arrangements to serve Scotland better, and meet the aspirations of the Scottish people for fuller devolution, while maintaining the integrity of the UK that they so much value?

There is a wide range of views in Scotland on devolution and where additional powers and responsibilities should lie. This is why I have committed Scottish Labour to the widest possible engagement with expert opinion and external stakeholders on this issue. This report, setting out our initial findings, I believe provides the basis for an informed and serious dialogue with the people of Scotland on how we can strengthen devolution and better meet their needs.

Scottish Labour is determined to lead the debate on how we enhance and develop devolution and we will do so in the most positive terms. We enter the debate focussed not on just where powers sit but crucially how powers can be best used to support individuals, families, communities and businesses in Scotland.

Too often, the debate on constitutional change has been about the false choice offered by the SNP: a choice between separation and rule from Westminster. Our concern is powers for a purpose – not devolution of powers for their own sake. We will not participate in a constitutional auction – we have considered the issues on the basis of where powers best reside.

The discussion is not just about decision-making at the Scottish Parliament or Westminster: it is about where power should best lie amongst multiple levels of government to ensure that decisions which affect people are made at the most appropriate level. That means it is essential to think about local government and communities. In the end, for us, real devolution is about people and how they can be empowered.

The members of the Commission have made a substantial contribution to the production of this interim report. I would like to thank them, as well as the Commission's Academic Advisory Group and Secretariat, for their expertise and determined commitment in taking this important piece of work forward.

I am very grateful to those who have given evidence, and engaged with us as we considered the issues. We very much welcome further responses from the length and breadth of Scotland, as well as from further afield, to the issues we raise and the questions we are exploring, in order to help us produce our final recommendations.

**Johann Lamont MSP**  
Leader, Scottish Labour

## **THE COMMISSION**

- Jackson Cullinane (Regional Political Officer and Regional Coordinating Officer, Unite)
- Margaret Curran MP (Shadow Secretary of State for Scotland)
- Victoria Jamieson (Chair, Scottish Labour)
- Johann Lamont MSP (Leader, Scottish Labour)
- Gregg McClymont MP (Shadow Minister for Work and Pensions)
- Duncan McNeil MSP (MSP for Greenock and Inverclyde)
- Anas Sarwar MP (Deputy Leader, Scottish Labour)
- Catherine Stihler MEP (MEP for Scotland)
- Councillor Willie Young (Aberdeen City Council)

## **ACADEMIC ADVISORY GROUP**

The Commission is supported by an Academic Advisory Panel that advises it on all aspects of its work.

- Professor Jim Gallagher CB FRSE (Nuffield College, Oxford)
- Professor Arthur Midwinter (University of Edinburgh)

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# Executive summary

## Introduction

- The terms of reference for the Scottish Labour Devolution Commission are as follows:
- “To consider issues relating to the future development of Scottish devolution, produce an interim report that will be submitted to the Scottish Labour Conference in 2013 and a final report containing recommendations on further devolution thereafter.”
- The Commission membership encompasses all parts of the labour movement and is committed to the widest possible engagement with expert and public opinion.

## Scottish Labour and devolution

- Scottish Labour is the party of devolution. Labour’s support for devolution pre-dates the existence of the SNP – we have been making the case for devolution for over 100 years. Devolution is a cause we advocate out of deep-rooted conviction, not pragmatic necessity. Any debate on our constitutional future cannot be a political fix: it must be about what is best for Scotland. Devolution is not a journey that leads to independence – it is a journey towards true home rule. Nothing we say in this report will placate the SNP – they will only ever be satisfied by separation.
- After Labour’s landslide election victory in 1997, we delivered a referendum in two months and a Scottish Parliament in two years. Devolution has secured beneficial change for the people of Scotland. Since 1999, many important measures to create a better and fairer Scotland have been passed, including abolition of feudal tenure, land reform, and the ban on smoking in public places. The Scottish Parliament has used all of the powers at its disposals with the exception of its tax varying powers. More certainly could be achieved: for example, the latest flagship policy of the SNP for an independent Scotland, to use powers to provide more childcare, is already a devolved matter.
- We also believe it essential to underline that the UK Government, working in tandem with effective devolved government, can achieve real results for the people. Let us not forget it was a UK Labour government, working with a Labour-led administration in Scotland, which made substantial inroads into poverty by making work pay through the minimum wage and tax credits, investing in early years and childcare, and increasing spending on schools. It was also a Labour Government that delivered a right to 28 days paid holiday for full time workers, gave free TV licenses for over-75s and introduced the New Deal that benefited millions of people in Scotland. Furthermore, it was a Labour Government that gave the Bank of England operational independence over monetary policy – an arrangement nationalists want to keep in an independent Scotland.
- The Scottish Labour Devolution Commission has attempted to address one overriding question: how can we meet the aspirations of the Scottish people for fuller devolution while maintaining the integrity of the UK which we know they value strongly?

- In looking at this, we have reviewed the taxation powers of the Scottish Parliament, its funding, and the range of its powers. The Scottish Parliament's powers are very wide, as virtually all domestic policy is devolved, apart from welfare benefits; but its taxation powers are relatively narrow, even after the implementation of the Scotland Act 2012, so that it remains substantially funded by taxes raised at Westminster.

### **The opportunities for further devolution: taxation**

- By any international standard, the Scottish Parliament has very wide spending powers, but by comparison narrow tax powers. Scope exists for greater devolution of taxation powers than is currently planned under the Scotland Act 2012. "Full fiscal autonomy" however is no more than a thinly disguised version of independence, and no serious commentator proposes it as anything other than that. We have reviewed individual taxes, following the principle of subsidiarity, devolving powers over decision-making to the lowest practicable level.
- At this stage, only devolving Value Added Tax (VAT) can be completely ruled out, as European law does not permit this. Assigning a share of VAT is technically possible, but this would potentially import risk and volatility to the Scottish Budget without giving any tools to manage that risk.
- Income tax is clearly the best candidate for further devolution. It raises enough revenue to make a significant increase in the proportion of the Scottish Budget accounted for by the Parliament's own resources (closing some of the "fiscal gap"). In our view, a strong case exists for devolving income tax in full, and we are minded to do so. We do, however, wish to consult widely on this issue. The advantage of devolving income tax – a revenue stream that provides a substantial, stable tax yield – is that it would provide a broader range of fiscal choices, enhancing accountability and responsibility for decisions made by the Scottish Parliament on taxation and public expenditure. It would also enable the Scottish Government to make the tax system more progressive. However, we would not want to devolve income tax in a way which would increase the administrative burden on employers, and indeed on individuals
- There is potential scope for further devolution of other taxes, although the case for devolving the third large domestic tax, national insurance, given its linkage to old age pensions and other contributory benefits, remains in our view open to question.
- Amongst other smaller taxes, corporation tax is the most frequently mentioned candidate for devolution. We can see the case for greater flexibility in regional economic policies, but believe devolution should not simply be viewed as a means to introduce tax competition so that businesses can find ways of reducing their overall tax burden by moving profits between different tax jurisdictions. This is a pernicious practice of which we have seen a great deal in recent years, and we have no desire to encourage it.

- Providing that the application of different rates of air passenger duty in Scotland to the rest of the UK did not contravene EU law, and it could be shown that any associated administrative and economic issues could be overcome, we believe that there is a strong case that air passenger duty should be devolved.
- We are of the view that vehicle excise duty should be devolved, and would be interested in views on the potential for doing this. We are less convinced of the case for devolving duties on tobacco and alcohol because of the problems of avoidance. There is a case for devolving some other taxes, such as inheritance tax or capital gains tax, but these raise relatively small sums of money, and any administrative challenges would need to be overcome.
- It would obviously be technically possible to devolve oil taxation on most of the North Sea, but in practice this would import a risk of unpredictable effects on devolved spending. Indeed, it would build a "fiscal cliff", of uncertain size and timing, into Scottish public spending plans – as would be the case under independence.

### **Stability in public services**

- When we look at devolving further tax powers, it is important to consider stability of funding for public services. This is an issue to which the proponents of other models of fiscal devolution have given insufficient consideration. The present grant arrangements have many strengths, and provide stable and predictable funding levels for important public services run by the Scottish Parliament. We have no wish or desire to make Scotland's public services poorer.
- No convincing alternative to the Barnett formula which meets this requirement has thus far been proposed. Advocates of alternative models of devolution argue for a needs-based formula, but do not set out how much Scottish public spending would be at risk as a result. If consideration were to be given to a move to a needs-based formula, it would be essential that this issue was exhaustively explored and consensus achieved.

### **The responsibilities of the Scottish Parliament: devolution and welfare**

- The responsibilities of the Scottish Parliament are already very wide. Virtually all domestic policy apart from macroeconomic management, taxation and welfare benefits is already devolved. Welfare benefits such as pensions are the only major domestic spending programme not devolved, but represent the largest single government budget in Scotland (as elsewhere in the UK).
- Labour has always been the party of the UK Welfare State. We take pride in this fact, and will do everything we can to sustain it against the attacks it faces from the Conservatives and SNP. We oppose the Conservative-led government's welfare agenda, but this does not lead us to the conclusion that the solution is to tear up the Welfare State that has served us well. We believe it is an argument for Labour governments at both Westminster and the Scottish Parliament.

- It was a UK Labour government, working in tandem with a Labour-led administration in Scotland, which made substantial inroads into reducing inequalities by making work pay through the minimum wage and tax credits, investing in early years and increasing expenditure on schools.
- We believe that being able to pool resources and risks across a larger and more resilient political community than would be provided by the individual nations alone is the best way to provide security for all. Experience worldwide backs this up: benefits like old-age pensions are almost invariably the responsibility of national, rather than sub-national, governments.
- Labour is therefore committed to maintaining common pensions and benefits across Britain, sharing resources and risks with the rest of the country to which we belong. That is the best way to provide security for Scotland's people. Additionally, we see that devolving such a large element of spending as social security would increase the Scottish Parliament's budget very substantially. So it would inevitably widen, rather than narrow, the gap between its spending and taxing and therefore reduce its fiscal accountability. In the next phase of our work, however, we want to look at whether there are any particular areas of social security which relate closely to devolved services, or where there is already scope for variation in different parts of the country, and whether there may be a case for devolution there.

### **Reversing centralism: reinvigorating local democracy and empowering people**

- For Scottish Labour, the allocation of powers to different levels of government is not driven by nationalist dogma, but by a judgement about how people's needs can best be met. That applies to the distribution of power within Scotland, as well as between Westminster and the Scottish Parliament. The SNP have disempowered local government by centralising power. This is what local government feared when the Parliament was set up, and it is wholly contrary to the approach advocated by the Labour-commissioned McIntosh Commission.
- Nowhere is the effect of centralisation clearer than in the area of local taxation. While the SNP argue for fiscal powers for themselves, they have removed them from local government. The council tax freeze does not come without a cost. We must consider whether this is sustainable in the long-term. Labour started the council tax freeze in Glasgow in 2006 because we understood the pressure on families. However, it has now gone on for many years and is beginning to have serious effects on services, and, in turn, on families in that way; it cannot go on forever, but equally we will not simply let tax bills exponentially rise when household incomes are constrained by the pressure created by the Conservative-led government.
- Revitalising local government is not simply a matter of reorganisation. Indeed, given the current pressures faced by local authorities, we do not at this stage find any compelling case for wholesale structural reform of local government. Instead we should be driven by the needs and desires of the population, and want to find the right balance between national standards in certain key public services and the diversity of choices that communities can decide upon.

- There are certain public services where individuals should be entitled to regard uniformly high standards in provision as a right, such as in the key welfare services of education and care for the elderly. Just as there are key UK rights to welfare benefits, so there should be key Scottish rights to public services. However, there should also be freedom and flexibility to allow locally determined priorities in other areas of service provision, with scope for equivalent fiscal choices.
- Wherever possible, powers should be decentralised further, not just from Westminster to the Scottish Parliament, but from the Scottish Parliament to local authorities and communities, and indeed to people themselves. Real devolution is about central government showing trust in local government, and councils extending trust to local communities, neighbourhoods and people. There is a need to return power from state to people, to think anew about the way in which government works so that citizens become more active in public affairs, and communities feel empowered and able to engage in debates about local priorities and delivery. If this were to occur, citizens would be better able to use their empowered position to achieve more effective delivery, ensure services are more receptive to community needs, and support the reinvigoration of local democracy.
- One relatively small, albeit important, example in this regard is the responsibilities of the Crown Estate Commissioners for the seabed and foreshore of Scotland. This responsibility, as the Scottish Affairs Select Committee has recommended, should be devolved to the Scottish Parliament, but only so that it can be further decentralised as far as practicable to local authorities and local communities.
- We want the right relationship between central and local government, and we want local government – which the Scottish people value highly – to be a continuing and valued part of our constitutional settlement. The question for us is whether a form of formal, legal, entrenchment could do this, and if so how.
- Inter-governmental relations are essential within a constitutional system with multiple levels of government – if governments are to meet the needs of the people whom they serve, they have to work together better. When devolution was established, less attention was given to mechanisms for supporting interaction than might have been the case. It was perhaps too readily assumed that informal relations between ministers would be sufficient to resolve problems and conflicts as they arose. In our view the mechanisms for inter-governmental relations need to be further developed at all levels.

## Part 1: Introduction

### A. Creation of the Commission

1. On 3 March 2012, at a meeting of the Scottish Executive Committee (SEC), after Johann Lamont's first speech to the Scottish Labour conference as leader, the SEC agreed to the following statement:

"The Scottish Executive Committee notes that the forthcoming referendum is arguably the most important constitutional event in our country's modern history. It will be a time where the world will focus on Scotland and our democracy. The Labour movement has a crucial role to play in this process and to ensure this referendum is fair, transparent, inclusive and decisive.

Labour is the party of devolution. It is essential that we as a movement lead the debate on how it develops and changes. There is a wide range of views in Scotland as to where additional powers and responsibilities should lay, not just those devolved to the Scottish Parliament, but from the Scottish Parliament to local authorities across Scotland."

2. Following this, plans were set in place to establish a Devolution Commission, supported by an Academic Advisory Group, to take forward a substantive programme of work.
3. The Commission, it was agreed, should form a decision-making forum that would make recommendations on the enhancement and development of devolution to all layers of government. It was decided that the Commission should bring together individuals from across the labour movement, who would engage with the people of Scotland during the course of its work, and consult with the widest possible expert opinion.

### B. Terms of reference

4. The terms of reference for the Devolution Commission are as follows:

"To consider issues relating to the future development of Scottish devolution, produce an interim report that will be submitted to the Scottish Labour Conference in 2013 and a final report containing recommendations on further devolution thereafter."

5. The Commission is responsible for:

Scope – reviewing the current devolution settlement, and, in light of experience, recommending evidence-based changes to the present constitutional arrangements that enable Scotland to become a fairer, more equitable country; considering the role of local government within the current devolution settlement and how we can make it more open and effective; further improving the accountability of all levels of government and at the community level; and securing the position of Scotland as a strong and integral part of the United Kingdom.

Engagement – seeking the views of members of the Scottish Labour Party, its affiliated organisations and a wide and diverse range of interested individuals and organisations from across Scotland.

Output – producing an interim report to the Scottish Labour conference in spring 2013; and producing a final report to the Scottish Labour Party thereafter that recommends a coherent, evidence-based package of measures to enhance devolution and better serve people in Scotland.

Capability – ensuring the Commission has the capability to deliver and to plan to meet current and future needs.

### **C. Membership**

6. The Commission membership encompasses all parts of the labour movement. The current membership of the Commission is as follows: Jackson Cullinane, Margaret Curran MP, Victoria Jamieson, Johann Lamont MSP, Gregg McClymont MP, Duncan McNeil MSP, Anas Sarwar MP, Catherine Stihler MEP and Councillor Willie Young.
7. An Academic Advisory Group – responsible for supporting the work of the Commission – was appointed consisting of Professor Jim Gallagher and Professor Arthur Midwinter.
8. The Commission is supported by a Secretariat function which provides members with the information and analysis they require to carry out their duties effectively.
9. The membership of the Commission, Academic Advisory Group and any sub-groups that are established may evolve over time.

### **D. Meetings**

10. The Commission, since its first meeting, has met on approximately one occasion per month. The frequency of meetings is determined by the workload and may change over time. The Chair may convene additional meetings as deemed necessary.

11. After extensive preparations, the Commission met for the first time on 9 October 2012. The Commission has since met on the following occasions:
  - 12 November 2012;
  - 7 December 2012;
  - 11 January 2013;
  - 28 January 2013;
  - 4 March 2013; and
  - 4 April 2013.
12. The Commission will continue to meet on a regular basis right up to the publication of the final report. In addition, members of the Commission are engaged in continual written correspondence on relevant issues.
13. The Commission has identified a number of initial work streams. These are on the following subjects:
  - Taxation;
  - Welfare; and
  - Local government.
14. The work streams report to the Commission on a regular and systematic basis. We are also in discussions with trade unions and their legal firms, as well as interested stakeholders, on the possibilities for enhanced devolution in the areas of employment law and health and safety.
15. Our future work will also include examination of other areas, including broadcasting, data protection, gambling, open governance and responsibility for consumer education, advice information and advocacy.

## **E. External engagement**

16. The Commission is committed to a wide-ranging programme of external engagement. As part of its work, the Commission has received evidence from expert academic opinion on devolution and other issues.
17. Having completed the initial phase of our work, which involved consulting leading expert opinion in oral evidence sessions and identifying the main issues of concern, we are now seeking the written views of the wider public and key stakeholders to both test our initial findings and gain insights on how to best proceed. The Commission will be accepting written submissions from interested

stakeholders, including individuals, businesses, trade unions and any other organisations wishing to share their views on devolution and help us in our considerations of how the devolution settlement might be modified to better serve the people of Scotland. The written evidence and opinions received will be invaluable both in our preparation of a final evidence-based package of recommendations, and in understanding what would be broadly supported in Scotland.

18. The Devolution Commission is committed to the widest possible engagement, not just with party members but with people from across Scotland. For this reason, it has been decided to hold a series of external engagement events in both large and small council areas, highland, island and rural communities as well as cities. As the work of the Commission continues, external engagement with the widest possible number of interested individuals and groups will continue.

## **F. Towards a final report**

19. This interim report is not the end of the process – it is a staging post towards the final report. The Commission will undertake more evidence-gathering and investigative work before it makes final recommendations on the future of Scottish devolution.
20. In the following chapters, we set out why Scottish Labour is the party of devolution – a commitment that predates the formation of the SNP, gave rise to the creation of Scotland’s current devolved institutions, and helped pave the way for the establishment of the Calman Commission that led to the Scotland Act 2012; examine the current public funding arrangements, and possible alternatives on taxation and welfare; and consider issues surrounding the future of local government, democracy and empowerment of communities.
21. “Full fiscal autonomy” is no more than a disguised version of independence, and no serious commentator proposes it as anything other than that. However, a number of thoughtful contributors have convincingly argued that scope exists for greater devolution of taxation powers than is currently planned under the Scotland Act. We can see that the principle of subsidiarity, where powers over decision-making are devolved to the lowest practicable level, is at least as arguable in relation to taxation policy as to other policy areas. The question is what is practicable and in the best interests of Scotland. We are therefore continuing our rigorous examination on the potential for devolving further taxation powers.
22. At this stage, in the considered view of the Commission, the only tax which it is possible completely to rule out devolving is VAT; European law does not permit this. As for other taxes, there is potential scope for further devolution in income tax, air passenger duty, vehicle excise duty, inheritance tax and capital gains tax, although the case for devolving national insurance, given its linkage to old age pensions, remains open to question.

23. The Commission takes the view that tax devolution should not simply be viewed as a means to introduce tax competition so that businesses can find ways of reducing the overall tax burden by moving profits between different tax jurisdictions. We have seen in recent months just how ingenious international corporations can be in minimising their tax liability by laundering profits through low tax jurisdictions. This is a pernicious practice, and we have no desire to encourage it.
24. When considering the issue of devolving further tax powers, there are real concerns about stability in public spending: it is an issue to which the proponents of other models of fiscal devolution have given insufficient consideration.
25. The Commission believes that the scope for further devolution in welfare is less compelling than in the area of taxation. Labour is committed to a UK-wide system of social security, on the basis that a person in need of assistance in Gateshead is as deserving as someone in Glasgow or Glamorgan. This does not, however, preclude the possibility for greater flexibility in the provision of welfare.
26. We do not believe that the man in St Andrew's House always knows best. The SNP have disempowered local government by centralising power –realising the fears expressed by the McIntosh Commission as long ago as 1998. We will return central-local government relations to the mutual respect enshrined in McIntosh.
27. The reinvigoration of local government, ensuring more participation in the democratic process, and increasing empowerment of communities are Scottish Labour's cause. The Scottish Government's refusal to fund the council tax freeze means that while individuals may pay less, the communities they live in are worse off and, as a result, so are they. We must consider whether this is sustainable in the long-term.
28. Rejuvenating local government is not simply a matter of reorganisation. Indeed, given the current pressures faced by local authorities, we do not at this stage find any compelling case for wholesale structural reform of local government. Our focus is on the self-renewal of councils, and a clear and honest relationship of mutual respect between central and local government rather than prescribing changes in law or expensive structural reorganisation.
29. Ultimately, real devolution is about empowering communities and people. In our view, it is insufficient to confine any discussion on devolution to the roles of local and central layers of government, or for the boundaries of this debate to focus solely on the powers exercised by these two tiers. We believe that, whenever is practicable, central government ought to devolve decision-making to local government, and local authorities should devolve power to local communities, neighbourhoods and people.

## Part 2: Scottish Labour: the party of devolution and social justice

### A. Introduction

30. Scottish Labour is the party of devolution. It was Labour that argued for a Scottish Parliament and we created it when we came to power in 1997. We believe that strong devolution, within the United Kingdom, can deliver the best possible outcomes for the people of Scotland. As has been the case for over 100 years, Scottish Labour is determined to lead the debate on how we enhance and develop devolution, and we will do so in the most positive terms.
31. Labour's support for devolution pre-dates the existence of the SNP. It has been a cause that has been advanced by successive generations of Labour politicians. As a party that is committed to meeting the challenges of an increasingly interdependent world, Scottish Labour rejects the narrow nationalism of the SNP. Labour does not view the world through the distorting spectacles of an inward looking nationalism, but asks how we can both develop and use institutions of government to provide the people of Scotland with security, opportunity and fairness.

### B. Scottish Labour and devolution - a long history

(i) Keir Hardie to J. P. Mackintosh

32. Devolution has been at the heart of the Scottish Labour Party's political agenda since its inception. Famously, in the 1888 Mid-Lanark by-election, Keir Hardie, Labour's first leader, stood on a platform that included a pledge to establish a Scottish Parliament. Hardie could not have been clearer on his commitment to devolution: "I believe the people of Scotland desire a Parliament, and it will be for them to send to the House of Commons a body of men to achieve it."<sup>1</sup>
33. It has never been part of the aims and objectives of the Labour Party to separate Scotland from the UK. Instead, in its early years, the demand from Labour was, in Keir Hardie's refrain, "Home Rule All Round." This meant Home Rule within the UK – not independence. The phrase was used in a similar way to a later proponent of devolution, Professor John. P. Mackintosh, Labour MP for Berwick and East Lothian from 1966 to 1978. Mackintosh favoured use of the Victorian term of "Home Rule", even though it had fallen out of common usage, largely because of its clarity in conveying the need for institutional structures that connected to people's everyday lives.

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1 E. Hughes (ed.), *Keir Hardie's Writings and Speeches, from 1888 to 1915*, (Glasgow: Forward, 1928), p. 13

34. The Labour Party Conference of June 1918 reaffirmed support for devolution, when a resolution was passed stating “some early devolution of both legislation and administration is imperatively called for”, and that “there should be constituted separate legislative assemblies of Scotland, Wales and England.”<sup>2</sup>
35. Throughout the 1920s, Labour remained committed to the cause of Scottish Home Rule within the United Kingdom. In 1924, a Scottish Home Rule Bill was introduced by George Buchanan, Labour MP for the Gorbals. The then Labour Government approved the general principle of the Bill, which retained to Westminster a number of services provided at a UK-level, including the Post Office, Customs, Army, Navy, Foreign Affairs and Tax Collection. The memorandum of the Bill stated the proposals were “... an extension of the policy of Devolution within the UK.”<sup>3</sup> A joint Exchequer Board, accordingly, was to be established to allocate financial resources.
36. In 1927, a second Scottish Home Rule Bill was introduced by James Barr, Labour MP for Motherwell, and seconded by Tom Johnston, who served as Secretary of State for Scotland in Churchill’s wartime coalition government. Johnston, Labour MP for Stirling and Clackmannan West, was vehemently opposed to the idea of Scottish independence. However, more a devolutionist of the head than the heart, Johnston believed that any move to Home Rule “must not only be evolutionary, they must be clear, business-like and evoke the minimum of opposition both in England and Scotland.”<sup>4</sup>
37. As part of a larger programme of constitutional reform, Labour again led the case for devolution in 1929, outlining in its election manifesto, *Labour’s appeal to the nation*, a plan for legislative assemblies for Scotland, Wales and England, with “autonomous powers in matters of local concern.”<sup>5</sup>
38. Perhaps the most passionate advocate for Scottish devolution was James Maxton, Labour MP for Glasgow Bridgeton. One of the original Red Clydesiders, Maxton argued: “Give us our parliament in Scotland. Set it up next year. We will start with no traditions. We will start with ideals ... men and women ... [will] spend their whole energy, their whole brain-power, their whole courage, and their whole soul, in making Scotland into a country in which we can take people from all nations of the earth and say: ‘This is our land, this is our Scotland, these are our people, these are our men, our works, our women and children: can you beat it?’”<sup>6</sup> Maxton, however, was no nationalist. In 1941, Maxton wrote of the SNP: “They came to us who were international socialists and asked us to give up our internationalism in favour of nationalism. That I was not prepared to do.”<sup>7</sup>
39. Given the challenges of rebuilding Britain’s war-ravaged economy, establishing the NHS and creating the Welfare State, devolution was not a priority for the 1945-51 Labour Government. As a result, the cause of devolution within the Labour Party fell into abeyance, albeit only temporarily.

2 G. D. H. Cole, *A History of the Labour Party from 1914*, (London: Taylor & Francis, 1951), pp. 66-67.

3 G. Brown and D. Alexander, *New Scotland, New Britain*, (London: Smith Institute), p. 14.

4 G. Walker, *Tom Johnston*, (Manchester: Manchester University Press, 1988) , p. 141.

5 Labour Party, *Labour’s appeal to the nation*, (London: Labour Party 1929).

6 G. Brown, *Maxton*, (Edinburgh: Mainstream Publishing), p. 161.

7 G. Brown and D. Alexander, *New Scotland, New Britain*, (London: Smith Institute), p. 3.

40. The greatest proponent of devolution in the post-war period was J. P. Mackintosh. Donald Dewar once remarked of Mackintosh: "He did not base his argument on nationalism. It was not the glorification of the Nation State. It was never Scotland right or wrong. His vision was good government, an equitable democracy, that borrowed, elevated, created opportunity for the citizen."<sup>8</sup> From his days as a political campaigner in the late 1950s, through to his premature death in 1978, just prior to the devolution referendum, Mackintosh was a consistent and principled campaigner for devolution. In 1966 he published an influential book, *The Devolution of Power*, arguing for the decentralisation of power, addressing what he viewed as the problem of people's disconnection from distant government, the overburdening of the "centre", and the challenges of connecting local, regional and national government.
41. More specifically, Mackintosh's case for devolution was founded on a belief that the Scottish Office should be subject to greater democratic control and accountability – a critique of the limitations of "administrative devolution." Mackintosh believed in the "Union State", meaning the organisation of the United Kingdom around the diversity of its four nations, full representation of different identities and recognition of common bonds.
42. In 1969, Labour again led the way, when Harold Wilson's government established the Kilbrandon Commission, which recommended the establishment of devolved assemblies for Scotland and Wales. Following this, at the Labour Party's Dalintober Street Conference during the late summer of 1974, Labour officially committed itself to an elected assembly. Labour subsequently fought and won the October 1974 general election on this programme.
43. In 1976, it was a Labour Government that introduced the first Devolution Bill to the House of Commons, a piece of legislation piloted through Parliament by the young minister (and future Labour leader) John Smith. During a debate on the Bill – which, following its enactment, was unable to command the requisite number of votes in the subsequent referendum – J. P. Mackintosh famously declared: "People in Scotland want a degree of government for themselves. It is not beyond the wit of man to devise the institutions to meet these demands."<sup>9</sup>
44. Part of the reason Labour was unable to introduce devolution from Hardie to Callaghan was an inability to reconcile the competing ambitions of devolution and the Welfare State. As Gordon Brown argued in his study of Scottish Labour: "no one [in the Labour Party] was able to show how capturing power in Britain – and legislating for minimum powers of welfare, for example – could be combined with a policy of devolution for Scotland."<sup>10</sup>

8 G. Walker, "John P. Mackintosh, Devolution and the Union", *Parliamentary Affairs*, (Oxford: Oxford University Press, 2012), 65:1.

9 Quotation engraved on the threshold of the Donald Dewar Room at Scottish Parliament.

10 G. Brown, *The Labour Party and Political Change in Scotland, 1918-1929: the politics of five elections*, (Edinburgh: Edinburgh University PhD), p. 523.

45. More importantly, however, there was an inability within Labour to bridge the gap between those who were “devolution-idealists” and “devolution-pragmatists.” The first group – including individuals such as Maxton and Mackintosh – sought a constitutional settlement for Scotland but generally failed to address issues of detail, such as on parliamentary composition, the appropriate electoral system, and, perhaps most significantly of all, specific powers that should be devolved and reserved. The second group – including Tom Johnston and one of his successors, the late Bruce Millan, Secretary of State for Scotland in the 1976-79 Labour Government – was more disposed to focus on practical and functional matters, concentrating not on the great possibilities devolution could offer, but instead on what could be achieved.
46. The two competing traditions within Scottish Labour – centred around devolution pragmatists and idealists – were only reconciled by John Smith and Donald Dewar during the late 1980s and 1990s, making the creation of a Scottish Parliament a genuine possibility and not just an elusive pipe-dream.
- (ii) John Smith and Donald Dewar – the enduring legacy
47. On 21 October 1988, Donald Dewar made a speech at Stirling University, in which he declared his intention to lead the Labour Party into the Scottish Constitutional Convention. Dewar said that: “The people must decide if they are prepared to live a little dangerously in order to achieve what they want ... It means that the Labour Party must be prepared to negotiate and not simply seek to enforce the devolution package that we already have before the public.”<sup>11</sup>
48. Dewar confronted the argument that devolution would lead to independence, contending: “The key question is the place of Scotland in the United Kingdom. Here, in recent times, there is evidence of a determined attempt to polarise the argument. The pitch is that Scotland must pick between a full incorporating union or total independence. The suggestion is that there can be no workable middle way and that those who advocate some form of devolution are in effect impossibilists. I do not believe that this is necessarily so.”<sup>12</sup>
49. For Labour, devolution offered the means of directing the Scottish people’s sense of dual identity – a feeling of Scottish-ness and British-ness – into a political reality. Dewar argued in his 1988 speech: “We are both British and Scottish, and the two are not exclusive but essentially compatible. Political statehood is not essential to the status of genuine nationalism. What is needed is a political solution which recognises and buttresses the Scottish identity within the framework of the United Kingdom.”<sup>13</sup>

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11 Donald Dewar, Andrew Williamson Memorial Lecture at Stirling University, (21 October 1988). See L. Paterson, *A Diverse Assembly: The Debate on a Scottish Parliament*, (Edinburgh: Edinburgh University Press), pp. 169-173.

12 *Ibid.*

13 *Ibid.*

50. In March 1989 the Scottish Constitutional Convention held its first meeting. It was made up of 58 of Scotland's 72 MPs, 7 of its 8 MEPs, 59 of 65 councils and representatives from various groups, including the Scottish Trade Union Congress, Scottish Council for Development and Industry and religious leaders. The SNP, driven by its desire for separatism, pulled out of the Convention. Nevertheless, it continued its work, with Labour taking a leading role. The Convention consulted widely across the country and, on 30 November 1990, an agreement on what form a Scottish Assembly should take was signed. The Convention worked because it was for Scottish democracy, not against British democracy.
51. By the early 1990s, following John Smith's election as leader of the Labour Party, devolution had become "unfinished business." It became Labour's mission to deliver devolution and meet, in Smith's words, the "settled will of the Scottish people." Unfortunately, Smith's tragic and early death robbed him of the ability to deliver on this promise.
52. From 1993 to 1995, George Robertson, as Shadow Secretary of State for Scotland, led Labour's charge in the refinement of those aspects of the Convention requiring fuller development. The Constitutional Convention continued to meet, having successfully met on the centre ground, and unwearingly made plans. This culminated on 20 November 1995, when under the executive chairmanship of Canon Kenyon Wright, the Convention produced its final report, *Scotland's Parliament, Scotland's Right*, helping to pave the way for the Scottish Parliament established in 1999.<sup>14</sup>
53. The cause of devolution was embraced by the Blair government. In 1996, Blair published a book laying out his "vision" of Britain, in which he made the argument for devolution: "There are now two significant impulses in modern democratic politics around the theory of the state. The first is to bring government closer to people. Big, centralised government is out. Devolution and decentralisation are in."<sup>15</sup> For Blair, devolution would strengthen the UK – not weaken it. Later in the book, Blair asserted: "Devolution will not just be good for Scotland and Wales. It will be good for the whole of the UK as it brings power closer to people and is part of a wider process of decentralisation."<sup>16</sup>
54. In 1997, Labour's general election manifesto made the case for devolution in simple terms: with the introduction of devolution, it was argued, "the Union will be strengthened."<sup>17</sup> However, Labour ministers regarded the Scottish Constitutional Convention scheme as a broad agreement of principles – not a detailed blueprint. As a consequence, Dewar had to settle the outlines of his devolution plans immediately after Labour's victory in May 1997. The decision was taken to make all powers, except for those specifically reserved to Westminster, subject to the Scottish Parliament; in contrast, Labour's 1978 Devolution Bill, each devolved power had been individually stated.

14 Scottish Constitutional Convention, *Scotland's Parliament, Scotland's Right*, (Edinburgh: Scottish Constitutional Convention, November 1995).

15 T. Blair, *New Britain: my vision of a young country*, (London: Fourth Estate, 1996), p. 258.

16 *Ibid*, p. 270.

17 Labour Party, *New Labour – because Britain deserves better*, (London: Labour Party, 1997).

55. Within three months of the 1997 election, Dewar produced a White Paper on devolution. When Dewar introduced the Scotland Bill, he read the first clause, "There shall be a Scottish Parliament", paused, looked up at his audience and said, "I like that." He expertly piloted the legislation through the House of Commons, and, in September 1997, a mandate for a Scottish Parliament in a referendum was won: 74.3 per cent of those voting supported a Scottish Parliament, and 63.5 per cent were in favour of giving it tax-raising powers.
56. In the first election to the Scottish Parliament, in May 1999, Scottish Labour won 56 of the 129 seats, and Dewar became Scotland's first First Minister.
57. The Scottish Parliament was Donald Dewar's great triumph and legacy. As the historian Tom Devine has written, while devolution was far from being a "one-man band", "Donald Dewar's place in history is undeniably secure as the pre-eminent architect of that final settlement."<sup>18</sup>
- (iii) Devolution – Labour and the "new politics"
58. The creation of the Scottish Parliament has heralded a new way of doing politics – a politics that is more participative, more creative, and less confrontational. The Scottish Parliament differs from Westminster in its methods of working. This is perhaps the most important legacy of Dewar's design. The Scottish Parliament has deliberately adopted modern methods of working. The architects of devolution believed it should be accessible, open and responsive to the needs of the public; encourage participation by organisations and individuals in decision-making; and would seek the views and advice of specialists and experts.
59. As at Westminster, most legislation in Scotland is initiated by the Scottish Government. However, the committees of the Scottish Parliament perform, in essence, the functions of both the Westminster select committees and Westminster's public bill committees.
60. The influence of committees in the Scottish Parliament extends across a broad range. Unlike their Westminster counterparts, they can initiate legislation. For instance, Scotland introduced a smoking ban in public places a year before the introduction of a similar measure in England; and, although the relevant Scottish legislation was eventually adopted by the government, it originally emerged from the Scottish Parliament's Health Committee.
61. Devolution has been a success. In 2010, indeed, devolution was voted the second most successful policy of the past thirty years in a survey of academics conducted with the Political Studies Association. (The most successful policy was Labour's introduction of the minimum wage in 1999.) Devolution has also delivered for the people of Scotland. As Wendy Alexander has argued, during the Scottish Parliament's first session, when financial resources were scarce, "radicalism took many forms."<sup>19</sup>

18 W. Alexander (ed.), *Donald Dewar: Scotland's first first minister*, (Edinburgh: Mainstream, 2005), p. 203.

19 *Ibid*, p. 217.

62. In total, 62 Bills were passed and became Acts of the Scottish Parliament. Amongst the most important measures to advance greater social justice in Scotland were the abolition of feudal tenure, land reform, introduction of a graduate endowment, and repeal of clause 28. This was followed in the next parliamentary session by major measures, such as the ban on smoking in public places and controls on anti-social behaviour.
- (iv) Calman and the Scotland Act 2012
63. Scottish Labour took the lead in creating of the Calman Commission, laying the way for the Scotland Act 2012. On 30 November 2007, Wendy Alexander, Labour leader in the Scottish Parliament, delivered a keynote speech at Edinburgh University, entitled “A New Agenda for Scotland.” In the speech, she argued: “What the next generation will demand of the current generation is a settlement that honours the birth of devolution without being hidebound by it ... It is up to us to offer a better alternative. A new Scottish Constitutional Commission will allow us to do just that.”<sup>20</sup>
64. The following week, on 6 December 2007, a motion, in the name of Alexander, was tabled in the Scottish Parliament, stating: “That the Parliament, recognising mainstream public opinion in Scotland, supports the establishment of an independently chaired commission to review devolution in Scotland; encourages UK Parliamentarians and parties to support this commission.”<sup>21</sup> The remit of this Commission would be to review the provisions of the Scotland Act 1998, in the light of experience and recommend changes to the present constitutional arrangements that would enable the Scottish Parliament to better serve the people of Scotland, improve the Scottish Parliament’s financial accountability, and continue to secure the position of Scotland within the United Kingdom.
65. As the instigator of the debate, Alexander sought to engender support for a review of the devolution settlement. During the debate, she argued: “It is clear that Scotland wants to walk taller within the United Kingdom, not to walk out. How do we move forward? How do we align power and responsibility more closely within this place? Let us address the case for greater financial accountability. The review of Scotland’s future should be about more than party politics.”<sup>22</sup>
66. This initiative led to the establishment of the Commission on Scottish Devolution, chaired by Sir Kenneth Calman. The Commission began work in April 2008 and published its final report, *Serving Scotland Better: Scotland and the United Kingdom in the 21st Century*, in June 2009.<sup>23</sup> The main recommendations of the Calman Commission were as follows:

20 W. Alexander, “A New Agenda for Scotland”, Lecture on a Future Vision for Scotland, University of Edinburgh, (30 November, 2007).

21 Scottish Parliament Official Report 6 December 2007 col 4133-85.

22 Ibid col 4135.

23 Commission on Scottish Devolution, *Serving Scotland better: Scotland and the United Kingdom in the 21st Century: final report*, (Edinburgh: Commission on Scottish Devolution, June 2009).

- Cutting the basic and higher rates of income tax levied by the Scottish Government by 10p in the pound, with a corresponding reduction in the block grant, calculated using the Barnett formula.
- Giving the Scottish Parliament the power to set a Scottish income tax rate, applying to all bands.
- Devolving Stamp Duty Land Tax, Landfill Tax, Air Passenger Duty and Aggregates Levy to the Scottish Parliament.
- Giving Scottish ministers additional borrowing powers to cover the cost of capital projects, or temporary shortfalls in their budget.
- Devolving powers for the administration of Scottish elections.
- Devolving the regulation of airguns.
- Devolving power to set drink-drive limits.
- Devolving the power to set speed limits.
- Devolving responsibility for nature conservation at sea.
- Improving relations between the Scottish Parliament and Westminster by creating mechanisms for regular meetings and discussions between ministers, MPs and MSPs.

**67.** The UK government accepted most, but not all, of Calman's recommendations. The main exceptions not included in the Scotland Act were devolution of air passenger duty, assignment of income tax on savings and distributions, and funding for policy relating to animal health. The Scotland Act was enacted on 1 May 2012, marking the next stage of the process to change the devolution settlement. The new Act heralded the largest ever transfer of financial powers to Scotland since the creation of the UK.

**68.** The new powers included in the Scotland Act are as follows:

#### Finance

- A new Scottish rate of income tax to be in place from April 2016;
- The full devolution of stamp duty land tax and landfill tax, from April 2015;
- The power to introduce new taxes, subject to the agreement of the UK Government;
- A new £2.2 billion capital borrowing power for the Scottish Parliament, to be in place from April 2015 – with a limited version of the power in place from April 2013 to enable the Scottish Government to fund £100 million of pre-payments for the Forth Road Crossing;

- Extended current borrowing powers to help manage volatility in tax receipts and the creation of a new Scottish cash reserve to manage the new revenue receipts; and
- A new power, welcomed by the Labour Party, to devolve further taxes by order, so that the scope of fiscal devolution can be extended.

#### Non-Finance

- Formally changing the name of the Scottish Executive to the Scottish Government;
- Scottish Ministers to have powers in relation to the misuse of drugs;
- Scottish Ministers to have powers relating to the administration of elections to the Scottish Parliament;
- Power to regulate air weapons devolved to Scottish Parliament;
- Scottish Ministers to have a role in appointment process for BBC Trust member for Scotland and MG Alba Trust Members;
- Scottish Ministers to have a role in the appointments process for the Crown Estate Commissioner with special responsibility for Scotland;
- Scottish Ministers to have power to set regulations for the drink-drive limit;
- Scottish Ministers to have the power to determine the national speed limit in Scotland; and
- Ensuring that the criminal penalties that apply in Scotland Act are updated to reflect the current standards applied in Scottish courts.

### C. Conclusion

69. For over 100 years, since its foundation, Labour has advanced the cause of Scottish devolution. It is an issue Scottish Labour has approached not simply out of pragmatic necessity. It is a cause Scottish Labour has advanced out of deep-rooted conviction. From Hardie to Dewar, Labour politicians have been at the forefront in leading the case for devolution. The desire has always been to meet the Scottish people's legitimate desire for more powers within the constitutional context of the UK.
70. It was Labour that argued for a Scottish Parliament and we created it when we came to power in 1997. It was, moreover, Labour that initiated and led the debate which led to the establishment of the Calman Commission, and the subsequent passing of the Scotland Act 2012. In doing so, Labour has ensured greater democratic accountability for decisions affecting the people of Scotland and strengthened the union. This will continue to be a cause on which we will lead.

## Part 3: The opportunities for further devolution: taxation

### A. Introduction

71. This chapter reviews fiscal devolution in Scotland, examines the opportunities for further tax devolution, what constraints there might be on it, and what trade-offs would be involved.

### B. Fiscal devolution in the UK

72. The UK is a fiscally centralised state.<sup>24</sup> The Treasury collects all taxes, apart from local taxes: and, moreover, ministers nowadays set virtually all local taxes across the country as well. The traditional arguments for central taxation are twofold. Firstly, uniform taxation is economically efficient (discussed in more detail below) and, secondly, bringing the entire tax yield into a central pool allows distribution according to need across the country. More recently, Conservative governments have centralised fiscal power over local government taxes to an unprecedented degree: and the present Scottish Government has effectively removed all taxation discretion from Scottish local authorities.
73. Fiscal powers, however, are related to spending as well as taxation, and in this debate it is essential to take account of the extent of spending decentralisation – not merely take it for granted. By international standards, Scotland is unusually highly decentralised in terms of spending – all the more so since central government grants come without any attached conditions, which is extremely unusual internationally – but presently not decentralised in terms of taxation, although this will change, following the passing of the Scotland Act 2012.
74. This balance between taxation and spending, as with every country, is a product of history. The high spending decentralisation in Scotland goes back to the period of administrative devolution. This too explains the lack of conditionality on central government grants: during the period of administrative devolution, when the Scottish Office was responsible for the administrative governance of Scotland, there was no need to apply formal conditions. This carried over almost without thinking into the post-1999 devolution settlement. The result is that the devolved Scottish Government has, by international standards, a remarkable degree of spending autonomy.
75. The result of this degree of spending decentralisation and tax centralisation is that there is a “fiscal gap”. This is true in all countries, as there are no examples where the sub-national government raises all of the money it spends. In Scotland, however, the size of the “fiscal gap” is unusually large: even after the Scotland Act 2012, the majority of the Scottish Parliament expenditure will be funded by Westminster grant. This limits the autonomy of the Scottish Parliament to determine the size of its Budget: the Budget is determined more by Westminster than the Scottish Parliament.

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<sup>24</sup> The UK is the second most fiscally centralised country in the OECD. Only New Zealand is more fiscally centralised. See OECD, *Government at a Glance 2009*, (Paris: OECD, 2009).

76. The Scotland Act was intended to assist with this, but the gap still remains. The “Devo Plus” argument is predicated on the belief that this gap should be reduced as close as possible to zero.<sup>25</sup>

### C. Could more taxes be devolved?

77. Nevertheless, other countries devolve more taxes than is currently the case in the UK, and federal systems typically allow for much greater tax variation, but tend to have less emphasis on fiscal equalisation for need. These too are products of history, but can also in part be attributed to a number of factors: problems associated with, say, different sales taxes are less significant if a country is 4,000 miles wide. However, even a small country like Switzerland has remarkably decentralised taxes – for example, income tax varies, over very short distances, from Canton to Canton.

78. In general, it is easier and makes more sense to decentralise taxes on “tangibles” such as property that move around less, and have national taxes on “intangibles”, such as profits or online transactions. Thus, property taxes are very easy to decentralise, while sales taxes are more difficult to devolve. Table 3.1 below looks at all the taxes applying in Scotland, and assesses the scope for decentralising each, with potential consequences.

79. As Table 3.1 shows, three big taxes account for 60 per cent of domestic tax revenue: value added tax (VAT), national insurance (NI) and income tax. It is not possible to devolve VAT under European law. Assigning a share of VAT is technically quite possible, but this would import risk and volatility to the Scottish Budget without giving any tools to manage that risk. It is in principle possible to devolve NI contributions, but, as they are connected to contributory social security benefits like old age pensions, this would make sense only if welfare benefits were to be devolved. (Part 4 on welfare and devolution discusses this point in greater detail.) Income tax, in contrast, is already in part devolved, and could in principle be devolved more, as it is elsewhere.

80. The Scotland Act 2012 gives the Scottish Parliament the power to set a Scottish rate of income tax to be administered by HM Revenue & Customs (HMRC) for Scottish taxpayers. It is expected to apply from the 2016-17 tax year. The Income Tax Act 2007, accordingly, will be amended to peg the income tax rate for Scotland’s taxpayers at ten percentage points below the main UK rate.

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25 See Devo Plus, *A Stronger Scotland within the UK: First report of the Devo Plus Group*. (Edinburgh: Devo Plus, May 2012).

**TABLE 3.1: Estimated breakdown of tax revenues and scope for further devolution**

Taxes collected in Scotland			
	£ million revenues in 2010-11	% of total non-North Sea revenue	Scope for devolution?
Income tax	10,634	23.5%	Already partly devolved; more technically possible
VAT	8,560	18.9%	Not possible under EU rules
National insurance contributions	8,018	17.7%	Technically possible but linked to contributory benefits such as old-age pensions
Corporation tax (excl. North Sea revenue)	3,114	6.9%	Technically possible but tax competition issues: profits are readily mobile
Fuel duties	2,339	5.2%	Technically possible, but with substantial administrative changes, concerns about tax competition, and subject to EU law
Tobacco duties	985	2.2%	Concerns about avoidance and subject to EU law
Alcohol duties	895	2.0%	Concerns about avoidance and subject to EU law
Stamp duties	595	1.3%	SDLT already devolved Stamp duty on securities such as shares easy to avoid
Capital gains tax	244	0.5%	Technically possible
Other taxes on income and wealth	362	0.8%	Concerns about avoidance
Insurance premium tax	210	0.5%	Concerns about avoidance
Betting and gaming and duties	113	0.3%	Concerns about avoidance
Air passenger duty	183	0.4%	Technically possible: should be devolved subject to EU law
Landfill tax	99	0.2%	To be devolved
Climate change levy	61	0.1%	Presently spread across the whole UK
Aggregates levy	54	0.1%	To be devolved
Inheritance tax	159	0.4%	Technically possible in principle
Vehicle excise duty	470	1.0%	Technically possible in principle, though some issues about possible avoidance
Non-domestic rates	1,891	4.2%	Already devolved
Council tax	1,986	4.4%	Already devolved
Other revenues (public sector trading surpluses, rents, TV licences, National Lottery distribution, etc.)	3,703	9.3%	Not relevant
<b>Total current revenue (excluding North Sea revenue)</b>	<b>45,177</b>	<b>100.0%</b>	
Comparative data			
North Sea revenue: Geographical share	7,951		
Total public spending for benefit of Scotland	61,625		
Within which, spending by Scottish Government and local authorities	35,932		
Within which, social protection expenditure	21,047		

**Source: Government Expenditure and Revenues in Scotland (GERS), and HM Treasury's Public Expenditure Statistical Analysis (PESA)**

- 81.** HMRC will issue tax codes to employers in the months before April 2016 which will identify those employees who are Scottish taxpayers, and employers will deduct tax at the appropriate rates, which may be higher or lower than or the same as those which apply in the rest of the UK. The definition of a Scottish taxpayer will be based on the location of an individual's main place of residence. For employees and pensioners, the income tax change will be applied through PAYE. A proportion of the income tax paid by all Scottish taxpayers will go towards funding spending by the Scottish Government. If the Scottish Parliament sets a different rate it will apply to all the income tax rates – the basic rate and the higher rate will all go up or down by the same percentage, relative to the UK rate.
- 82.** The new Scottish income tax rate will need to be set every year by the Scottish Parliament. The block grant from the UK government to Scotland will then be reduced to reflect the fiscal impact of the devolution of these tax-raising powers.
- 83.** It would be possible to devolve all rates, and all income tax receipts, or even to devolve allowances and thresholds. Three issues, however, arise:
- The administrative challenges for employers and HMRC of running different allowances and a different tax structure, and not just a different Scottish rate;
  - The risk to the Scottish Budget of being dependent on one tax only for close to half of its revenue; and
  - The challenge of "social union", and whether Scotland should be able to have a different degree of progressiveness in the tax system (in either direction) than the rest of the UK.
- 84.** Income tax is clearly the best candidate for further devolution. It raises enough revenue to make a significant increase in the proportion of the Scottish Budget accounted for by the Parliament's own resources (closing some of the "fiscal gap"). In our view, a strong case exists for devolving income tax in full, and we are minded to do so. We do, however, wish to consult widely on this issue. The advantage of devolving income tax – a revenue stream that provides a substantial, stable tax yield – is that it would provide a broader range of fiscal choices, enhancing accountability and responsibility for decisions made by the Scottish Parliament on taxation and public expenditure. It would also enable the Scottish Government to make the tax system more progressive. However, we would not want to devolve income tax in a way which would increase the administrative burden on employers, and indeed on individuals.
- 85.** Of the other taxes, corporation tax is the most frequently mentioned candidate for devolution. The SNP have talked admiringly about Ireland's 12.5 per cent rate of corporation tax. This is substantially lower than the UK's current main rate of 23 per cent. In a speech to the Northern Ireland Assembly at Stormont in 2008, Alex Salmond referred to the 12.5 per cent rate, saying "Scotland's Government believes very strongly that, with measures such as low competitive tax, we can match or even exceed"

the success in Ireland.<sup>26</sup> More recently, Alex Salmond has been talking about a less ambitious but still substantial cut in corporation tax to 20 per cent. (The present UK Government intends to reduce the rate to 21 per cent in April 2014, and then 20 per cent in 2015.) Large reductions in corporation tax in Scotland would not be easy, requiring tax increases elsewhere, spending cuts or borrowing in order to balance the books.

86. Most of those who want to devolve corporation tax simply regard it as a tool for promoting economic development. However, would the Scottish Government actually be able to afford such a tax cut for business? Research carried out by IPPR suggests this would be very difficult in the short to medium term. This is because Scotland since 1990 has raised less money in tax than it spends on public services, and welfare benefits (even if North Sea oil revenue is included). To give an idea of the scale of the challenge: if Scotland's corporation tax rate had been 12.5 per cent in 2010-11, IPPR has projected that £3.9 billion less would have been raised in tax (including North Sea oil).<sup>27</sup> Even if a tax cut stimulated economic activity, this is an enormous gap to fill. The problem for Scotland with emulating Ireland's 12.5 per cent rate would be the subsequent loss of revenue from the existing corporation tax base, amounting to billions of pounds a year. It would take an absurdly large effect on economic growth to offset this loss of revenue. It is easy to see that by doing some simple arithmetic. If the rate of corporation tax were reduced by one third, corporate profits would have to double to bring in the same amount of revenue. There is no conceivable reason to think that such a large effect would happen. Reducing corporation tax yield by one third would cost Scotland £1 billion a year – equivalent to almost the entire budget of the Scottish police service.
87. It is highly dubious to say that Scotland could simply emulate Ireland on corporation tax. Scotland has a higher public spending-to-GDP ratio than Ireland, resulting from more generous Welfare State provision, and, as a consequence, Scotland has greater public spending commitments to maintain. It also has an existing corporation tax base, and revenue stream, which cutting rates would reduce.
88. The problem for the rest of the UK with corporation tax devolution is essentially one of tax avoidance – at present, companies put huge effort into minimising their tax liabilities by using accounting devices to locate their profits in lower tax jurisdictions. To get the benefit of a lower Scottish rate, all companies would have to do is relocate their profits – not relocate the economic activity. The result might be a small gain in revenue to Scotland, but it would not be from economic activity; the result would also be a problem for the rest of the UK as businesses reduce their overall tax liabilities. Corporation tax avoidance by multinational companies is a major problem for governments across the world, as has been very clearly seen in recent months in the UK and elsewhere. It would be undesirable for any scheme of tax devolution to provide further opportunities for corporations to avoid their obligations.

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26 T. Gordon, "Salmond in 'fantasy land' over tax plans, says former adviser", *Herald*, (29 January 2012).

27 Katie Schmuecker, Guy Lodge, Lewis Goodall, *Borderland: Assessing the implications of a more autonomous Scotland for the north of England*, (London: IPPR, November 2012).

However, it may, in principle, be possible to devise schemes to avoid this risk, along the lines suggested by the Holtham Commission for Wales.<sup>28</sup> We would welcome views on where the balance of advantage lies here. Overall, however, we believe it would be counterproductive to create conditions for wasteful beggar-thy-neighbour corporation tax competition between Scotland and the rest of the UK – a competition to the bottom in which the losers would be the public in Scotland.

89. Air passenger duty (APD) is an excise duty which is due on chargeable passengers being carried from a UK airport on chargeable aircraft. APD is not payable by inbound international passengers who are booked to continue a journey to an international destination within 24 hours of their scheduled arrival in the UK. If a passenger “stops-over” for more than 24 hours, APD must be paid in full. Since May 2009, APD has been structured around four distance bands, set at intervals of 2,000 miles from London to the capital city of the destination country. This change was designed to ensure that those flying longer distances, and thus contributing more to aviation emissions, pay more for the environmental cost in tax. Each destination band has two rates of duty depending on class of travel, so there are eight different rates of APD in total. Although APD is not payable on flights departing from airports in the Scottish Highlands and Islands, flights from other parts of the UK to airports in this region must pay duty. Providing that the application of different rates of APD in Scotland to the rest of the UK did not contravene EU law, and if it could be shown that any associated administrative and economic issues could be overcome, the Commission is of the view that a strong case exists that APD should be devolved.
90. Of the other smaller taxes, towards the bottom of Table 3.1, some could in principle be devolved: but they do not make a large impact on the fiscal gap. Excise duties are among the larger of these, for example on alcohol or tobacco, but devolving them would create potential problems of avoidance. Amongst these taxes the best candidate for devolution is, arguably, vehicle excise duty. Overall though, there would be a need to overcome some difficulties, such as a potential distortion when vehicles are first registered, and for fleets of vehicles belonging to hire companies. The location of most personal cars, on the other hand, is well defined.
91. There is also a case for devolving some other personal taxes, such as inheritance tax or capital gains tax (CGT), but these raise relatively small sums of money, and any administrative challenges would need to be addressed. In 2010-11, these taxes would have raised revenue of just over £400 million in revenue in Scotland (£159million for inheritance tax and £244 million for CGT).
92. Most people have no experience of inheritance tax, as they do not accumulate enough wealth in their lifetime to be affected by it. It is paid on an estate when an individual dies, though sometimes on trusts or gifts made during a person’s lifetime. The majority of estates do not have to pay inheritance tax as they are valued at less than the threshold – £325,000 in 2012-13. The tax is payable at 40 per cent on the amount over this threshold or at a rate of 36 per cent if the estate qualifies for a reduced rate because a charitable donation is made. Inheritance tax is subject to “tax planning”;

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28 Independent Commission on Funding and Finance for Wales, *Fairness and accountability: a new funding settlement for Wales*, (Cardiff: July 2010).

as people make significant efforts to reduce the liabilities under the current arrangements. Married couples and registered civil partners can effectively raise the threshold of inheritance tax due on their estate when the second partner dies up to £650,000 in 2012-13. More complex schemes are also common for large estates. This would suggest that establishing a separate inheritance tax system in Scotland might potentially further incentivise tax avoidance. On the other hand, inheritance tax is a personal tax, like income tax, and there may be scope for it to be improved and reformed and, if potential difficulties can be resolved, we can see a case for devolving responsibility for it to the Scottish Parliament.

- 93.** Capital gains tax is another tax which most of the population do not encounter. It applies to individuals and businesses, and is levied on the profit when an “asset” that has increased in value is disposed. (Disposing of an asset includes: selling it; giving it away; transferring it to someone else; exchanging it for something else; or receiving compensation for it, such as when an insurance payout is made when an asset is destroyed.) Most assets are liable to CGT when an individual or business disposes of them, although some are exempt such as personal possessions disposed of for £6,000 or less, the sale of a car, and, in most cases, the main home. From 23 June 2010 onwards, the CGT rates have been: 18 per cent and 28 per cent for individuals (the rate depends on total taxable income); 28 per cent for trustees or personal representatives of someone who has died; and 10 per cent for gains qualifying for Entrepreneurs’ Relief. Capital gains tax is another tax often used in “tax planning”. It can be advantageous for individuals to ensure that profits they make are realised as capital gains, rather than as income, so as to take advantage of the nil rate amount for capital gains. Nonetheless, it is a part of personal taxation, and there is a case for devolving it, provided potential administrative complexities can be overcome, and the scope for tax avoidance minimised. As the Scottish Parliament will already have powers over the taxes on land and real estate, through council tax, non-domestic rates and stamp duty land tax (which is to be replaced by a new land and buildings transaction tax), we can see particular merit in devolving CGT on transactions on land.
- 94.** Oil is in a different category. North Sea oil receipts were very important to the UK economy in the 1980s. However, they have tailed off since then, inevitably, and although they are significant in comparison with Scottish public expenditure, they are no longer as important for the UK as a whole. This contrasts markedly with the situation in the 1980s, when North Sea oil was critical to the UK’s fiscal position. Presently, in very broad terms, North Sea oil receipts make up most of the difference between domestic tax receipts in Scotland and spending: devolved Scottish public spending is about 18 per cent per head higher (identifiable spending by Scottish Governments) than the UK average on devolved expenditure, and overall identifiable public spending is about 14 per cent higher than the UK average whereas tax receipts excluding oil per capita are slightly lower, leaving a fiscal deficit of £7 billion.

95. The major problem is that oil is a finite resource, and oil revenues will start to reduce in the near future. No one knows for sure exactly by how much or when – much depends on the world price of oil, but the decline will be substantial: even the most optimistic assumptions do not have oil production continuing at current levels for long into the near future. Moreover, there will be a big drop in tax receipts when companies have to start spending on decommissioning platforms. Oil taxation could be devolved – it is technically quite possible – but it would be highly difficult in practice because of the likely effect on spending. It would build a “fiscal cliff” into Scottish public spending plans. This “fiscal cliff”, of course, would be difficult to fund under independence.<sup>29</sup> The Scottish Government’s own economic advisory panel set up a fiscal working group which recommended “medium-term” reductions in public spending so the oil revenue could be put into an oil fund. It remains to be seen how such a fund could be established given that an independent Scotland would be £7.6 million in deficit.

#### D. Tax Devolution: further issues

96. The more Scotland relies on its own resources, the less it relies on shared UK taxes. Complete fiscal self-sufficiency is independence, and any system of finance for Scotland within the UK involves some sharing of UK resources. This is something which the Labour Party welcomes: taxation rightly transfers resources from individuals who are able to pay to support those who are not. This is currently applied across the UK, and as a result money is transferred across different parts of the country. As we have seen, because it makes good sense to raise taxes at the national level, and to decentralise spending decisions, in all countries there are transfers of resources from national to devolved government. Such transfers should continue but greater reliance on Scottish taxation raises the question of how the remaining transfer would be calculated.

97. At the moment, such calculations are based on the Barnett formula, established by the Labour Government in the late 1970s. If the Scottish Parliament is to rely more on resources raised from Scottish taxation, then some adjustment will have to be made to that calculation. Under the Scotland Act 2012, the UK Government propose to retain the Barnett formula, but make an adjustment to take account of devolved tax income that is likely to be received. This seems a sensible approach. Proponents of “Devo Plus” argue for a needs-based formula, but do not set out how much Scottish public spending would be at risk as a result.

98. Of course there is no objective, neutral, commonly agreed measure of spending need. That is one reason why the Barnett formula has survived for so long. Scotland does have a number of serious social and other problems, notably in relation to health and social deprivation – and, of course, an unusually large landmass which increases the cost of service delivery. Barnett nevertheless has many strengths, notably that it provides stability to levels of public funding, and so the public services and their management. No convincing alternative which meets this requirement has thus far been proposed.

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<sup>29</sup> The “Fiscal cliff” would be the sudden reduction in spending needed if Scotland had to rely on its domestic taxes only, when oil revenues were no longer available.

## E. Conclusion

99. There is scope for further devolution in the area of taxation: it clearly is possible, but it is naive to think that it can completely close the fiscal gap – nowhere else in the world does this – and any package has to take account of the effects and the rest of the UK.

## Part 4: The opportunities for further devolution: welfare

### A. Introduction

- 100.** Labour has always been the party of the Welfare State. We take pride in that, and will do everything we can to sustain it against the attacks it faces. To consider how best to balance our commitments to welfare and devolution, it is important to look at the nature of the British Welfare State. The Welfare State comes in two halves: (i) directly provided services such as health, education, social work and housing (ii) and cash benefits. The former are devolved, but cash benefits remain reserved. This division goes back, not just to the devolution settlement of 1998, but ultimately to the 1945-51 Attlee government. When the system of social security recommended by the Beveridge report was put into place, cash benefits were administered uniformly across Britain. The National Health Service (NHS), by contrast, was administratively decentralised, and the legislation which set it up was separate in Scotland from that in England and Wales as education was also. Thus today, while education and health legislation are administered, devolved and delivered in Scotland, national insurance (NI) and cash benefits are administered and provided by the UK state.
- 101.** This chapter examines issues which would arise in devolving cash benefits and the scope for further devolution in this area.

### B. Social Security spending in Scotland

- 102.** Social security is the UK government's single largest item of public expenditure. In 2011-2012, total government spending was £695 billion. Of this amount, £159 billion was paid out in benefits. In Scotland, social protection spending including benefits – such as old age pensions, child benefit, income support and disability benefits – accounted for nearly 40 per cent of identifiable public spending. Tables 4.1 and 4.2 shows the scale of social protection expenditure in Scotland and how this compares to English levels. Old-age pensions are by far the biggest component of the benefits bill.
- 103.** Scotland's relatively high level of benefit spending is driven by the individual circumstances of claimants, which is, in turn, driven by long-term social trends, most notably the age structure of the population, and changing patterns of economic activity. Scotland is now economically typical of the UK in terms of income and unemployment, but some continuing high levels of benefit expenditure may still be linked to the de-industrialisation that took place during the 1980s. The levels of benefit spending in future however will be substantially driven by the age structure of the population.

**TABLE 4.1: Social protection spending in Scotland, 2005-6 to 2010-11**

(£m)	2006-7	2007-8	2008-9	2009-10	2010-11
Social protection	15,955	16,956	18,317	19,903	20,741
Of which social services	2,420	2,834	3,051	3,180	3,265
Per head (£)	3130	3310	3546	3835	3972
Per head indexed to UK =100	110	108	109	108	109

**Source: HM Treasury PESA Table 9**

**TABLE 4.2: Main components of social protection spending 2010-11**

Main benefits	Scotland (£ per head)	(England)
Old age pensions	1413	(1329)
Incapacity, disability, etc.	579	(449)
Family benefits, tax credits income support	757	(752)
Unemployment benefits	93	(82)

**Source: HM Treasury PESA Tables 10.5, 10.6**

104. Future benefit expenditure will be in particular driven by the increasing proportion of the population over pensionable age. The number of people aged 75 and over is projected to increase from 410,000 in 2010 to 500,000 in 2020 – a growth of around 23 per cent. It is then projected to continue to rise, reaching 740,000 in 2035 – an increase of 82 per cent over the 25 year period. The number of pensioners living in the country will increase by 551,200 by the year 2035. The percentage of Scots who are of pensionable age will rise from the current figure of 16 per cent to almost 25 per cent in 2035. The dependency ratio – the ratio of people aged under-16 and over pensionable age to those of working age – is projected to rise from around 60 per 100 in 2010 to 64 per 100 in 2035.<sup>30</sup> The number of persons over the age of 75 in Scotland is projected to rise proportionally more than the UK as a whole.

30 General Register Office for Scotland, *Projected Population of Scotland (2010-based)*, (Edinburgh: GROS, October 2011)

### C. The principle of social insurance

105. Beveridge's idea of a Welfare State was based on the idea of social insurance. It replaced previous mutual insurance systems (like friendly societies) with national insurance. Workers, and through them their families, were insuring against the risks of ill health, unemployment, old-age or injury. Assistance paid from general taxation was a safety net for the very poorest.
106. However, old-age pensions are now the main contributory benefit (insurance stamps matter for them), and most other benefits are now means-tested and supported from general taxation. Nevertheless, welfare is still in substance (even if not in strict form) a system of mutual insurance. Every individual faces risks like old age, illness, and unemployment: rather than carrying these risks individually they are pooled – not in a pension fund or a friendly society, but across an entire country, to become not private but “social” insurance. Individuals pay in, increasingly via general taxation (based on ability to pay rather than an insurance premium), and take the benefits when they need them. Obviously the larger the pool, the more the risks are likely to average out, and the easier an insurance scheme is to manage. Social insurance provides the largest pool of all.

### D. Divergence in the Welfare State

107. It has always been seen as a fundamental principle of the UK Welfare State that benefits and burdens depend on need, not geography. Of course this has not always been delivered in practice. Services vary from place to place in an unmanaged way (for example, it might have been better for your health to live near a big teaching hospital) and to some degree in the different nations of the UK. Since devolution, however, some of the social rights of UK citizens now depend explicitly on where an individual resides. This is because devolved parliaments and government can take different decisions about the services for which they are responsible: so we see different patterns of delivery in the NHS, where devolved administrations in Scotland and Wales have not followed the present government's market-driven policies in England, and in the provision of some services, for example care for the elderly. In contrast, as cash benefits are nationally administered, there is no geographical variation. (The only exceptions have been council tax benefit and housing benefit, which take account of local tax and rent levels. Council tax benefit is now to be decentralised, while the present government are cutting housing benefit in ways which are causing harmful and damaging problems for many people and planning to roll it into universal credit.) As a result, in relation to almost all cash benefits, there is no scope to take account of differences in different parts of the country.
108. In considering whether it would make sense to devolve provision, and so increase differences in benefits, we have to ask, would it matter if pensioners in Scotland were paid more generous pensions than in England, or if unemployment benefits were higher in Doncaster than Dundee? As a Labour Party, we think that does matter. In addition, Scotland faces a number of long-term demographic challenges. According to a recent report by the Scottish Parliament's Finance Committee, Scotland's population is ageing nearly twice as fast the UK as a whole, meaning there will be fewer working

age people to support more pensioners in Scotland than in the UK – a decline from one in four to one in three in Scotland by 2050. In addition the working age population is set to increase by 7 per cent between 2010 and 2035, while the pensionable population is set to increase by 26 per cent over the same period. The proportion of Scotland’s population of pensionable age is projected to increase by 2.9 percentage points between 2010 and 2035, compared with a 1.7 percentage point rise for the UK.<sup>31</sup> And, secondly, what would the consequences be of this? As we go on to discuss, we can see some significant concerns about potential consequences.

## E. Welfare and belonging: the “social union”

109. Welfare States send a powerful signal about belonging. The first act of Bismarck, once he had established the boundaries of the German Reich in the 1860s, was to introduce old-age pensions. The creation of the Welfare State after the Second World War bound the UK (social classes rather than nations) together. Consequently, it is not surprising that nationalists want to devolve welfare: they want to create a more exclusively Scottish sense of national identity, to replace the loyalties which already bind British people together. The last Labour Government, by contrast, accepted the Calman arguments that being able to pool resources and risks across a larger and more resilient political and economic community than that provided by the constituent nations alone was important for the security of all involved, and that benefits were the key instrument of “social union”, which already bind the UK together in a very powerful way. Their report (worth quoting at length) stated:

*“There are areas where the people of Scotland have over many years shared rights and responsibilities, and pooled risks and resources, with the rest of the Union. These are areas of common welfare. The most notable is social security – old age pensions, benefits paid to people seeking work or those unable to do so, and allowances and credits supporting children and families. Even in federal states, however, it is common (though not universal) for social protection of this kind to be a federal, rather than state or provincial, responsibility. This makes both economic and social sense: economic sense because one part of the country may be differently affected, or affected at different times, by economic change or shocks; social sense because providing people whose circumstances are the same with the same financial support wherever they are in the UK shows solidarity and mutual support. At present social protection is financed by UK-wide*

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31 Scottish Parliament Finance Committee, *Demographic change and an ageing population, 2nd Report, 2013 (Session 4)*, (Edinburgh: Scottish Parliament Corporate Body, February 2013), paras, 14-18.

*resources. Tax revenues are pooled and shared out on the basis of need to individuals (and thus indirectly, to different parts of the UK). This seems to us to be a fundamental part of the Union (emphasis added)... The risks, and the resources to deal with them, are shared. It has a very explicit expression in the form of National insurance, which is linked to benefit entitlements. But it is also seen in pooling other taxation like income tax or VAT and even in the pooling of windfalls like taxes from oil revenues and other natural resources."*<sup>32</sup>

110. The Devolution Commission believes that Calman's conclusion that being able to pool resources and risks across a larger and more resilient political and economic community than would be provided by the individual nations alone remains highly persuasive.

#### **F. Welfare and taxation: the economic union**

111. All welfare systems involve pooling both risks and the resources to deal with them. The logic of pooling risks among individuals and regions and across generations within the largest possible geographical area is widely recognised in the economic literature. Economic shocks tend to be asymmetric, affecting individuals and regions in different ways and at different times. Resource-pooling at the UK-level provides UK citizens with the safety-valve of a broader and more versatile tax base to cope with such unpredictability.
112. A less theoretical argument is whether Scotland could continue to afford, on its own, its present levels of welfare spending. If benefits were devolved, so that the Scottish Government could vary them, there would have to be very substantial tax devolution to finance this. It would hardly be reasonable to expect English taxpayers to pay for higher Scottish benefits. Welfare devolution is therefore linked to fiscal devolution. This makes obvious sense also because the benefit system is the major engine of redistribution, alongside income tax.
113. A short summary of Scotland's fiscal position is as follows. Public expenditure per head in Scotland is significantly higher than in the UK as a whole. (Devolved public spending is approximately 18 per cent per head higher, and overall identifiable expenditure about 14 per cent. The remainder, non-identifiable expenditure on services such as defence, is mostly allocated on a per capita basis.) Tax revenue (excluding North Sea oil) is estimated to be slightly below the UK average per head.<sup>33</sup> On this basis, Scotland would fall far short of the money it needed to sustain present public services and welfare benefit payments. Most of the gap could be filled if Scotland is credited with all of the revenue from off-shore oil arising off Scottish coasts to spend on Scottish services. That would leave Scotland very vulnerable when the oil revenue runs out, or when its price fluctuates in global commodity markets. This makes the theoretical argument about risk pooling much more real.

32 Commission on Scottish Devolution, *Serving Scotland better: Scotland and the United Kingdom in the 21st Century: final report*, (Edinburgh: Commission on Scottish Devolution, June 2009), paras. 2.24-2.25.

33 Scottish Government: *Government Expenditure and Revenue in Scotland 2012*, HM Treasury Public Expenditure Statistical Analysis.

## G. Welfare devolution and tax devolution

114. Those who argue for tax devolution, such as the proponents of “Devo Plus”, suggest that they are trying to solve the problem of the “fiscal gap”: that the Scottish Parliament raises much less in taxes than it spends, and this distorts its economic incentives. The problem with welfare devolution is that it would widen this gap hugely. At the moment the Scottish Parliament spends just over half of Scottish public spending. If welfare were devolved that would rise to about 90 per cent. However, as VAT (which accounts for approximately 19 per cent of non-North Sea oil revenue) cannot be devolved, it is very hard to get anything like that level of tax devolution. Thus, if welfare became a devolved function of the Scottish Government, the fiscal gap would be worsened and so the fiscal accountability of the Scottish Parliament reduced.
115. At the minimum, it would be necessary to devolve all of income tax and NI, and give the Scottish Parliament extensive borrowing powers to finance welfare payments acting as automatic stabilisers at a time of recession. Even then, a lot of risk would be imported into the Scottish Budget. This borrowing would have implications for UK macroeconomic management, and so would inevitably be subject to constraints.

## H. Public opinion

116. Despite these arguments, it has been suggested that public opinion in Scotland shows a strong appetite for more devolution, including for welfare. Table 4.3 shows a majority in surveys support devolving taxation and social security. This is the data on which those who argue for “Devo Max” rely, and they show, at first blush, that Scots appear to want Westminster to deal with foreign affairs, but the Scottish Parliament to deal with everything else.

**TABLE 4.3: Which institution should make important decisions?**

	Scottish Parliament	UK Government at Westminster	Local councils in Scotland	EU
	%	%	%	%
Health service	66	26	5	*
Schools	62	14	23	*
Welfare benefits	62	25	9	1
Defence and foreign affairs	31	63	1	3
Taxation	57	37	3	*

117. However, when a different set of questions are asked, the issue becomes less clear. Recent research by Professor John Curtice and Rachel Ormston, published in March 2013, confirmed that Scots are rather less willing to accept the possible consequences of devolving decision-making than a superficial reading of the data would suggest. This research found that, whereas 64 per cent of Scots think the Scottish Parliament should make most decisions about welfare benefits, only 34 per cent were happy with the idea of having a different old age pension in Scotland than in England. This led Professor Curtice to the conclusion: "Here at least, it seems that Scots are rather less willing to accept the possible consequences of devolving decision making."<sup>34</sup> Overall, in Professor Curtice's assessment: "More devolution is often described as the most popular option for Scotland's constitutional future. That is at risk of being an exaggeration. Remaining within the Union but giving the Scottish Parliament responsibility for everything apart from defence and foreign affairs is certainly not the first preference of a majority of people in Scotland, and may not even be the single most popular option."<sup>35</sup>
118. This is the "devolution paradox": citizens appear to want devolved institutions to have more powers; yet they appear also to be uncomfortable with territorial policy variation. This is hardly surprising, as people's immediate reactions to public opinion poll questions are not what they might conclude if they have the opportunity to look at the evidence and review the question. This is exactly the sort of pattern which is often seen when difficult public policy questions are reviewed by citizens' juries. People need to have the opportunity to see all the arguments to inform themselves of the "pros" and "cons." Welfare devolution is an issue on which public opinion has to be informed, not simply followed.

## I. International comparisons

119. Looking at how welfare functions are discharged in federal countries gives some guidance on the scope for devolving welfare. In almost all federal states, even those in which considerable powers are devolved, social security is the responsibility of the central government. Reviewing the international evidence, we see that there are no countries in which welfare is a decentralised responsibility. Even in countries such as Switzerland, where many tax and other powers are the responsibility of the Canton, rather than the federal government, social security is provided at the federal level. In federal countries, such as Germany and the United States, social security programmes are overwhelming federal rather than state driven. Even in a country with as decentralised a fiscal system as Canada, much of core welfare provision is run at the federal rather than the provincial level.

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34 John Curtice and Rachel Ormston, *More Devolution: An Alternative Road?*, (Electoral Reform Society and from ScotCen Social Research, March 2013), p. 13.

35 *Ibid*, p. 17.

120. As in the UK, all of these systems have developed historically. However, the twin pressures of risk pooling and nation-building have left social security a federal function – even in nations such as Germany where it began as a decentralised one. Sub-national governments have implementation responsibilities, and in others they have responsibility for some particular aspects of cash welfare – for example, in Canada, residual welfare, not covered by national social insurance, is a provincial responsibility.
121. There is however not an absolute division between the redistributive elements of welfare: those carried out at the national level, and the distributive, and those typically devolved or decentralised. There are a number of examples where the circumstances of individual people attract help and support from both levels of government. For example, responsibility for care of the elderly is primarily a devolved matter, but pensions and other payments to support those who need care, notably attendance allowance, are managed at the national level. At the minimum, this creates a need for coordination of policy between the national and the devolved governments, so that the services and support which are offered to people are as seamless as possible. Similarly there may be an argument that those elements of cash welfare which already vary from place to place could be devolved.
122. For this reason, an issue worth further exploration is whether there should be some adjustment of the boundary of responsibility here and devolving some cash benefits which match closely with devolved services, can already differ across Britain. This might enable services to be better integrated, perhaps with local authorities, which deliver many of the services in practice. This is an issue on which we would welcome views, and to which the Devolution Commission will devote further attention. The role of local government is considered further in this report.

## J. Conclusion

123. The following conclusions can readily be drawn:
- Scotland's relatively high level of welfare spending is a reflection of our economy and demography, and this will increase in the future because of growing numbers of elderly households.
  - All welfare spending is about the pooling of risks and resources. There are good economic arguments for doing this at as wide a level as possible to cope with economic shocks and needs for benefits which arise differently across different parts of the country. There are equity arguments for treating people equally in different parts of the UK.
  - The Labour argument for welfare is that the "social union" should be uniform throughout the UK. Welfare is a key part of nation building, and so nationalists will seek to devolve it if they can, whether that is in the interest of the population or not.

- Polling evidence is contradictory. It supports the idea of devolving welfare but also uniformity of provision across the UK. This is an area in which fuller information might well change public opinion.
- Wholesale devolution of welfare could only be linked to very substantial tax devolution, in order to pay for any variation. This carries fiscal risks.
- International experience, in general, supports the reservation of welfare. Further work would have to be carried out to see whether there was any scope for partial devolution of some aspects of welfare to Scotland.

## Part 5: Reversing centralism: reinvigorating local democracy and empowering people

### A. Introduction

124. The issue of devolution has too often been approached through the prism of devolving powers from Westminster to the Scottish Parliament – rather than considering the opportunities for further devolution of powers to local government, communities and people. The purpose of devolution was never to devolve power to a Scottish Parliament, only to see it accumulate powers from the local level upwards. At its best, devolution is about partnership between different levels of government and the local communities they serve. Given the importance of this issue, the Commission will be issuing a general call for written evidence to all local authority leaders on the future of devolution and local government, and we will be sending out an invitation to leading council figures to attend evidence sessions.
125. Above all, real devolution is about empowering communities and people. In our view, it is insufficient to confine any discussion on devolution to the roles of local and central layers of government, or for the boundaries of this debate to focus solely on the powers exercised by these two tiers. We believe that, whenever is practicable, central government ought to devolve decision-making to local government, and local authorities should devolve power to local communities, neighbourhoods and people.
126. This chapter examines the decline of local government in Scotland during the 1980s and early 1990s and its rehabilitation in the late 1990s and early 2000s, the SNP's disempowerment of councils through centralisation since 2007, how we will move forward to achieve a reinvigoration of local governance and democratic institutions, and ultimately the empowerment of communities and people.

### B. The decline and rehabilitation of local government

127. The centralisation of power in Scotland took place in two stages, under the Conservative governments from 1979 to 1997, and under the SNP government since 2007. The Scottish local government system had previously benefitted from administrative devolution, over structure, finance and regulation, leading to the creation of strong regional and local district councils in 1973.<sup>36</sup>
128. The 1980s and 1990s were a difficult time for local government. During this period, when councils came under attack from a government committed to reducing the power of local government, Labour and local authorities stood side-by-side against centralisation. Through the dark times of Conservative Government, it fell to the Labour Party and local government to uphold the values of fairness, justice and opportunity.

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36 A. Midwinter, *Local Government in Scotland – Reform and Decline*, (London: Macmillan, 1995).

129. The Conservative Party had traditionally exhibited a considerable degree of respect for local government. The Thatcher governments, in contrast, were committed to rolling back the state through spending cuts and privatisation of service provision, and reducing councils' fiscal, organisational and policy autonomy through grant controls, rate-capping, centralising of business rates, capital controls on rents and compulsory competitive tendering.
130. The failure of such measures led to the replacement of domestic rates with the deeply unpopular poll tax, and a messy local government reorganisation which broke up the regions' strategic capacity and created a single-tier system, supported by a plethora of joint boards.
131. In response, Labour joined forces with the Convention of Scottish Local Authorities (CoSLA) on the Scottish Constitutional Convention to fight for the cause of devolution and empowering local communities. Consequently, when the Convention's final report was published in November 1995, it recommended that any future devolution legislation should commit the Scottish Parliament "to secure and maintain a strong and effective system of local government, embodying the principle of subsidiarity so as to guarantee the important role of local government in service delivery."<sup>37</sup> (Recently CoSLA has published a paper which sets a new frame for this debate, going further than subsidiarity in the sense that it has called for a debate on a constitutional guarantee of powers. We discuss this issue in greater detail below.)
132. The Labour Government, elected in 1997, was not only pledged to devolution – it was committed to re-empowering local government and democracy after the years of Conservative rule. It was for this reason that the Labour Government commissioned Neil McIntosh, the former chief executive of Strathclyde Regional Council, to examine the relationship between local authorities and the Scottish Parliament. Following 18 months of extensive research and consultation, McIntosh recommended the signing of a covenant between the 32 councils and Scottish Parliament; establishment of a formal working agreement between ministers and councils based around parity of esteem and partnership; and the introduction of a more proportional electoral system in local elections. McIntosh's vision was based on partnership, a need to replace past adversarial relations, and strengthening local discretion. His final report argued:

*"The principle of subsidiarity, which underlies the legislation which has created the Parliament, is equally applicable to the relationship between the Parliament and local government. There is always a temptation for any administration to centralise – to draw powers into itself – and this is the reverse of subsidiarity. One way of expressing subsidiarity is that wherever a greater concentration and centralisation of powers and functions is proposed, the onus of proof must always be on those who propose centralisation, to demonstrate that it will indeed bring greater benefit to the public at large relations between local government and the Parliament ought to be conducted on the basis of mutual respect and parity of esteem."*

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37 Scottish Constitutional Convention, *Scotland's Parliament, Scotland's Right*, (Edinburgh: Scottish Constitutional Convention, November 1995).

133. The covenant with local government and compact with the voluntary sector were important statements by Scottish Labour following the establishment of the Scottish Parliament. We also argued that, since local government has three year budget horizons, this arrangement should be extended to the third sector to enable them to plan properly.
134. After the Scottish Parliament's official opening on 1 July 1999, its first major plenary debate was on the McIntosh Commission report. This was symbolically important: it demonstrated the importance of local government within the new devolution settlement. The Labour-led Scottish Executive introduced most of McIntosh's main recommendations. In 2001, a new "Partnership Framework" was signed between the Scottish Executive and CoSLA, defining working relationships and consultation arrangements.
135. The Local Government in Scotland Act followed in 2003. This gave local authorities a more prominent role in community leadership, placing the promotion of partnerships in delivery of public services on a statutory basis; and a framework was set up to improve strategy and efficiency through Community Planning and Best Value legislation.
136. The next year, the Scottish Parliament passed the Local Governance (Scotland) Act 2004, paving the way for the introduction of a proportional electoral system for council elections, based on the Single Transferable Vote (STV) system, and a change in the minimum age for standing as a councillor from 21 to 18. The introduction of STV was far from a self-interested act. Though it carried obvious electoral drawbacks for Labour, it was a measure designed to improve and enhance local democracy. Since the first election under STV in May 2007, there has been a more proportional distribution of seats amongst the main political parties. STV has not only made the voting system more proportional, it has led to changes in the way councils work, particularly in relation to political governance, and the agreement of coalitions have become widespread: after the 2012 local government election, over half of Scotland's 32 local authorities were governed by coalitions.

### **C. The return to centralisation under the SNP**

137. The SNP have disempowered local government by centralising power. This approach is precisely what the McIntosh Commission feared.

138. The SNP's predisposition towards centralised control is seen in their approach to Community Planning and Single Outcome Agreements (SOAs). The mechanisms of Community Planning and SOAs, which were intended to develop a strategic approach to the planning and coordination of service delivery, have created a bureaucratic system whereby councils are expected to demonstrate how they will deliver central priorities and spending commitments, leading to plans which Audit Scotland described as overly bureaucratized and difficulties in linking plans, priorities and budgets as a result.<sup>38</sup> A report by CoSLA's Improvement Service concluded that the removal of ring faced funds, the council tax freeze and agreed spending commitments had not created enough flexibility to move resources, and that SOAs had "excessive detail."<sup>39</sup> In contrast, Scottish Labour believes that Community Planning should be a process through which public sector organisations work with local communities, trade unions, businesses and the voluntary sector, to identify and solve local problems, improve services and share resources. The aim should always be to ensure people and communities are genuinely engaged in the decisions made on the public services which affect them.
139. A serious challenge facing local government is a policy that the SNP herald as one of their main achievements: the council tax freeze. The SNP falsely claim that there are no negative consequences for council taxpayers and their solution – a local income tax – is (rightly) gathering dust on a shelf in St Andrew's House. By taking away local authorities' flexibility, the SNP's council tax freeze is further diminishing their fiscal autonomy, and increasing the dependence of councils on central grant funding. The result is that local authorities are strapped into an ever-tightening straightjacket by a government bent on centralisation.
140. The council tax freeze is popular amongst some sections of the electorate because when people examine their bill each month they see it retained at the same rate. Labour started the council tax freeze in Glasgow in 2006 because we understood the pressure on families.<sup>40</sup> However, it has now gone on for many years and is beginning to have serious effects on services, and, in turn, on families in that way; it cannot go on forever, but equally we will not simply let tax bills exponentially rise when household incomes are constrained by the pressure created by the Conservative-led government. As a result, we are interested in views on the appropriate balance between supporting families and public services and how to strike it.

38 Audit Scotland, *An overview of local government in Scotland 2010*, (Edinburgh: Audit Scotland, 2011)

39 B. Christie, *Interim Report on the first phase Single Outcome Agreements in 2008-0 for the Improvement Service on behalf of COSLA and SOLACE*, (Edinburgh: CoSLA, 2009).

40 The Council Tax freeze was also partly a hangover from the Conservatives' reorganisation of councils in the 1990s. When the Conservatives reorganised local government, the cities in particular were separated from their wealthier hinterlands although still needed to keep many regional services going. This meant the cities started off with higher levels of council tax to enable a whole raft of wider services to be sustained.

141. Although ring fenced in the early years, the council tax freeze is now simply an accounting assumption in the block grant settlement which adds pressure on local government. Although marketed as a tax freeze, it is also a cut in resources available for core services. While the Scottish Government claims to have maintained local government's share of the Scottish Budget, it has not maintained its funding for core services (i.e. the council tax funding is a subsidy to taxpayers, not funding for services). This explains why the Budget Adviser's report to the Scottish Parliament Finance Committee stated that local government has borne the brunt of staffing cuts, whilst other devolved services have broadly maintained staffing levels until this year. The result has been 35,000 lost jobs in local government since 2007 according to the Scottish Government's own statistics.
142. Whilst it is not within the scope of the Devolution Commission to make recommendations on the future of local government finance, it is clear that a strong argument exists that the current funding arrangements are not sustainable as presently constituted. When the next Scottish parliamentary elections are held in 2016, the council tax freeze will have been in place for a decade. By the time of the next election, the council tax will not have been subjected to a revaluation exercise for over 25 years. This issue needs to be re-examined and any analysis on the future of local government finance should be based on the wildest possible engagement with interested stakeholders. We will also recommend considering other ideas to increase the flexibility of local authorities in the area of non-domestic rates, ways of extending Tax Incremental Funding to fund public sector investment in infrastructure, and exploration of a wider set of initiatives, including assigned or devolved local taxes, sales taxes, tourist taxes, municipal bonds, social impact bonds and other funding vehicles.

#### **D. Local government's role as the engine of regional economic renewal**

143. It is not within the remit of this Commission to make suggestions on Scottish Labour's economic policies, let alone develop an industrial strategy. We do, however, wish to express our view that harnessing the growth potential of Scotland's local economies, cities and regions is the key to unlocking economic recovery and securing long-term strength. In our view, local government has a proven track-record in stimulating economic renewal and growth, and we believe it could do even more if it was further empowered to tailor and adapt local economic development strategies to the requirements of local enterprises and labour markets.
144. Working in collaboration with central government, local authorities have a central role to play as engines of regional economic growth, actively engaging with business, trade unions, universities and civil society, to build the skills, infrastructure, finance and the enterprise culture that is needed to secure lasting productivity gains, value creation and sustainable investment.
145. Whenever is possible and practicable, economic levers should be devolved to the local level: involving those most directly affected in decision-making processes will help ensure that essential infrastructure is located to meet local needs, housing and employment sites are linked by appropriate

transport connections, and the local skills base is matched with employers' needs.

146. We believe it is necessary to examine the opportunities for local authorities to take back powers over areas such as skills, transport, housing, and other growth-related levers that can support economic development. One idea we consider worth exploring, for example, is whether certain functions currently held by Skills Development Scotland can be devolved to local authorities.
147. Local authorities face two major problems: they are forced to deal with the consequences of budget cuts and possess inadequate resources and levers to drive forward economic renewal. Councils will never be empowered to drive forward growth until they have greater control over funding. We believe there is scope for devolving greater decision-making powers over how funding is spent from the central to local government level. In our view, central government needs to provide a strategic focus and lead, leaving local government to concentrate on delivery.
148. There needs to be recognition that cities have a key role to play in driving the economic performance of Scotland. With the right blend of strategic leadership and energy, cities such as Glasgow, Edinburgh, Aberdeen and Dundee – building on their reputations as globally recognised centres of learning and culture – can become growth centres for Scotland, making decisions that shape long-term economic development. Cities are obviously the major hubs for business and we wish to encourage this. There is a need to invest in infrastructure and amenities to enable cities to support existing businesses, to retain them, to attract new inward investment and to incubate new businesses that will ensure economic sustainability for generations to come. On balance, we believe that cities do best when the city is empowered within its regional context, so they can stimulate not just their economies but also neighbouring local authorities, and we welcome views on how this is best achieved.

## **E. Reinvigorating local government and democracy**

149. We have repeatedly emphasised that Scottish Labour is the party of devolution, and takes great pride in the decentralisation of power to the Scottish Parliament in Edinburgh. This was a historic shift, but it is not an end in itself, and nor is it the final destination of devolved power. Wherever possible, powers should be decentralised further, not just from Westminster to the Scottish Parliament, but from the Scottish Parliament to local authorities and communities, and indeed to people themselves. The allocation of power is a means to an end, enabling people and communities to take greater control over their own destinies, and the things which will enable them to secure more prosperous and fairer communities. It is for that reason, unlike nationalists with their narrow focus on securing powers at a Scottish level, whether that is the most appropriate or not, that Labour believes in decentralising from the Scottish Parliament as well as to the Scottish Parliament. This has been described in different ways, including the principle of subsidiarity, that functions should be allocated at the level of government nearest to those affected wherever that is practicable, or as the ideal of double devolution – devolution from central government, so that powers can be further devolved again to

wherever they can be most effectively exercised.

- 150.** One area where this has been suggested is in relation to the Crown estate. In March 2012, the House of Commons Scottish Affairs Select Committee published a report on the Crown Estate Commissioners' (CECs) management of the Crown property, rights and interests which make up the Crown Estate in Scotland. The Committee concluded: "at best, the organisation [CEC] has a fundamental misunderstanding of the needs and interests of local communities and indigenous industries on the Scottish coast ... At worst, it behaves as an absentee landlord or tax collector which does not re-invest to any significant extent in the sectors and communities from which it derives income." Accordingly, it was recommended that the administration and revenues of the ancient Crown property, rights and interests in Scotland, which are currently managed as part of the Crown Estate (including the seabed and the foreshore) should be devolved then decentralised as far as possible to local authorities and local communities, with devolution to the Scottish Parliament conditional upon an agreement between the Secretary of State for Scotland and the Scottish Government on how such a schemes should be implemented, on the basis of the principle of subsidiarity. This seems sensible to us, and, after exhaustive examination, we feel able to endorse the Scottish Affairs Select Committee's recommendation on this subject.
- 151.** The role of local government is absolutely critical. Local authorities are directly elected, they are the closest tier of government to citizens, are well placed to understand local priorities and pressures, and can often see opportunities that are invisible from St Andrew's House or the Scottish Parliament. The idea of councils as deliverers of services is not enough. Councillors should scrutinise service performance and take responsibility for ensuring improvement when required. Reinvigorating local democracy also means we need to think about the role of councillors as local tribunes, challenging public services on behalf of the user. Of course councillors have always done this, and for many of the best local representatives, standing up for the electors is a passion: we need to recognise that more clearly, and find ways to allow this to be seen more explicitly as a key task of elected local government.
- 152.** Councils will nevertheless remain major deliverers of services: local government is responsible for about one third of the overall spending of the Scottish Parliament. Some of this will be provided directly, such as schools, and some, such as homecare for the elderly, often through contracting with voluntary or private agencies. We need to think about how standards of local service delivery can be driven up across local authorities. In March 2013, the Improvement Service published data on local views covering a wide range of areas, including schools, housing and street cleaning. The figures revealed substantial differences in levels of satisfaction and service across Scotland.
- 153.** Important questions arise about the degree of local discretion in the provision of these services. We have seen very clearly that local authorities' autonomy has been restricted by centralisation in recent years. This can result in a curtailment of local choices and a situation where resources are not properly focussed on local concerns: this can, in turn, lead to dissatisfaction with provision and public disillusionment in councils' capacity to meet local demands successfully. To address this, one school

of thought suggests efficient and effective local service provision requires greater local determination. Given this, it is argued that councils need greater freedom and flexibility to deliver policies that meet local circumstances, something that is especially important in a hugely diverse nation like Scotland. Furthermore, it could be argued that widening the scope for councils to implement their preferences is reinforced by the fact that, while measures of well-being have attempted to be defined, no single definition exists for how local authorities should act to improve well-being.

154. Acceptance of this view would mean agreeing to a greater level of divergence between local authorities in their choices and how funds are utilised. The contention that this will result in a "postcode lottery" does not treat a complex matter in a serious way. An alternative view, containing some merit, is that it is in postcodes where communities have the autonomy to adapt policies to local needs that public service provision is of the highest standard. In reality, in key service areas, standards already vary substantially from area to area. Indeed, NESTA has recently argued that centralisation may be the root cause of the postcode lottery itself:

*"Supporting mass innovation rather than stretching particular [uniform] solutions questions the efficiency of so-called 'economies of scale'. The most cost-effective impact will not be achieved by pushing a single one-size-fits-all solution or limited number of models of best practice, particularly in approaching tough, entrenched social challenges.*

*More local diversity necessarily results in a variety of provision. But a greater variety of approaches is necessary where specific social contexts, behaviours and networks have a demonstrable impact on people's actions and attitudes. Areas differ in the prevalence of certain environmental, health, and re-offending issues. For this reason, we already have postcode lotteries – not because public services are insufficiently standardised, but in part because they are too standardised.*

*While minimum standards in public services should remain, it is the current fiction of supposedly standardised provision in mainstream public services that generates concern about 'postcode lotteries', more than the fear of more genuinely local and diversified responses that would be much better placed to make an impact on the inequalities that persist."*<sup>41</sup>

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41 Laura Bunt and Michael Harris, *Mass Localism: A way to help small communities solve big social challenges*, (London: NESTA, March 2010), p. 35.

155. It has also been argued that fairness and diversity are not mutually opposed values. The case for this position is not a new one. For example, Beatrice and Sidney Webb, founders of the Fabian Society and leading figures in the development of early twentieth century local government, argued:

*“The case for a local administration of ... services rests primarily on the consciousness among inhabitants of a given area, of neighbourhood and of common needs, differing from those of other localities; and of the facility with which neighbours can take counsel together in order to determine for themselves what shall be their mental and physical environment and how it can be best maintained and improved.”<sup>42</sup>*

156. On the other hand, with some justification, many people strongly favour uniformity in local service provision, regarding these as social rights that should not vary across different council areas. Understandably, parents across the country all want the very best educational opportunities for their children, and expect common standards in schooling, the curriculum, educational management and so on. Similarly, in caring for the elderly, or adults with particular needs, local authorities work very closely with the NHS, and in relation to health provision people rightly expect the same standard from the NHS everywhere in the country.
157. These are important choices, which have sometimes in the past simply been ignored or brushed under the carpet. One possible way to resolve this issue is to agree upon an appropriate balance between suitable minimum national service standards and the diversity of choices that communities can decide upon, and that balance may properly differ in relation to different local services.
158. The debate on this subject needs to move on: it cannot simply framed be around uniformity in service provision versus local variation. The issue has to be approached much more subtly. There are certain public services where individuals should be entitled to regard uniformly high standards in provision as a right, such as in the key welfare services of education and care for the elderly. Just as there are key UK rights to welfare benefits, so there should be key Scottish rights to public services. However, it is also right to think about increasing freedom and flexibility to allow locally determined priorities in other areas of service provision, with scope for equivalent fiscal choices. We welcome views on how this could best be achieved.

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42 Sidney Webb and Beatrice Potter Webb, *A constitution for the socialist commonwealth of Great Britain*, (London: Longmans, Green and Co., 1920), p. 213.

**F. Real devolution is about people - looking outwards, not upwards**

- 159.** Real devolution is ultimately about people and communities. There is a need to return power from state to people, to think anew about the way in which government works so that citizens become more active in public affairs, and communities feel empowered and able to engage in debates about local priorities and delivery. If this were to occur, citizens would be better able to use their empowered position to achieve more effective delivery, ensure services are more receptive to community needs, and support the reinvigoration of local democracy.
- 160.** Devolution should not be an issue limited to local and central government: the boundaries of this debate needs to extend beyond a discussion on the allocation of powers between these respective tiers. In Scotland, many local authorities have responsibility for large populations: Glasgow City Council, for instance, provides services to over 500,000 people. The populations covered by Scottish local authorities are much larger than many other comparable countries, and this can lead to people feeling that councils are disconnected and unaccountable. Scotland is a centralised state in two senses: central government too often involves itself in the details of local service delivery, and local authorities too often operate in a way that is neither adaptable nor responsive to people's diverse requirements. Real devolution will only be achieved when government, whether in its central or local form, entrusts local communities to play an active and prominent role in delivery of accessible services that can be used by all.
- 161.** There is a strong case for central and local government to have a more strategic focus, offering support and co-ordination rather than getting involved in the micromanagement of solutions. This would result in more effectual governance, bringing power closer to people. At its core, real devolution is about a major change in the relationship between government and people. The challenge is how we connect bureaucratic service delivery structures to local community activity. In order to achieve this, it is imperative that central and local government move away from a managerial and instrumentalist way of operating.
- 162.** The centralised system of government in Scotland has three major consequences. Firstly, it results in local service providers looking upwards towards ministers and civil servants, or inwards to complex bureaucratic coordinating systems, instead of outwards to communities and people. Too often local authorities' success is judged not by delivering services that meet local needs, but rather their ability to meet central government expectations, usually in the form of targets. Secondly, centralisation can lead to local service delivery being approached in a way that is not joined-up, with local requirements not fully considered in the round or in a way that engages people. Thirdly, centralised control widens the democratic deficit, as people feel unable to influence local services. All of the above, it would seem, has contributed to growing public disenfranchisement, as people are unable to influence the services they finance and use.

- 163.** There needs to be a rebalancing in relations between the state, local government and communities. Real devolution means local government, whenever practicable, taking on new powers from central government, but then sharing these powers with citizens, neighbourhoods and communities. To address poverty, promote greater social justice and strengthen communities, it is essential we close the current power gap in society, where necessary by engaging the voluntary and third sectors. The third sector has an important role in empowering people and communities through advocacy, and encouraging social enterprise and services. We accept that there are many complexities involved in moving towards real devolution – shifting power to the level of the neighbourhood is a radical departure. These arguments need to be addressed and we welcome views on this subject. One argument against is that equity in access to services would be put at risk. A counter-argument to this point is that for as long as there continues to be central control over key determinants of opportunities – such as cash benefits and universal healthcare – these risks are very limited. Within local communities, there is a strong case for issues such as use of public space to be determined at the community level. In addressing this issue, subsidiarity is an informative and helpful principle. Subsidiarity holds that government power should reside at the lowest possible level. However, it is absolutely essential that subsidiarity should not be seen as a means for local government to thrust unwanted responsibilities onto unsuspecting individuals and communities.
- 164.** The independence debate is a distraction from the real issue of empowering communities. This has served to crowd out discussion of how far-reaching decentralisation can be overcome by a transfer of power to communities and people. If the policies supported by proponents of independence and Devo-Max were pursued, the result would be the accruing of more powers in the hands of an already overly centralised government. This is something to which we are opposed.

## **G. Constitutional guarantee of powers for local government**

- 165.** In March 2013, Councillor David O'Neill, President of CoSLA, delivered a speech on the need to ensure that local government is protected within our constitutional settlement. This was not an endorsement of the SNP's call for a written constitution or an endorsement of independence. As Councillor O'Neill argued, the UK does have a constitution made up of statutes, case law, parliamentary rules and historical ways of working. It also has Constitutional Conventions that may not have the force of statute, but are very powerful. Councillor O'Neill was arguing that "a way can be found that so fundamentally embeds local government in the 'constitution' that its status would be fundamentally altered."<sup>43</sup>

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43 Councillor David O'Neill, "Presidential Address: Today's Reality, Tomorrow's Vision", (7 March 2013).

166. The UK, perhaps because of its lack of a written constitution, is one of the few countries in the world where the constitutional status of local government is not firmly embedded: this is as true in England and Wales as it is in Scotland. This contrasts with many other countries. For example, in Germany, Article 28 (2) of their constitution (Basic Law) guarantees “the right to regulate all local affairs on their own responsibility, within the limits prescribed by law.”<sup>44</sup> Similarly, the very first article of the French constitution says: “it [the Republic] shall be organised on a decentralised basis.”<sup>45</sup> In Denmark, their constitution states: “the right of municipalities to manage their own affairs independently under State supervision shall be laid down by statute.”<sup>46</sup> In this respect, Scotland and the rest of the UK is somewhat of an anomaly.
167. Although the UK does not have a codified constitution, it is arguable that devolved Scotland does – in a de facto sense – in the form of the Scotland Act 1998. The Act gives the Scottish Parliament complete legislative authority over local government, and does not seek to entrench the position of local government. It is important to realise that entrenching local government in that constitutional settlement would need to be enacted by Westminster: it is not something which could be legislated for by the Scottish Parliament (if it could be then a subsequent Parliament could legislate to reverse it, and that would not entrench the position of local government). Interestingly, constitutional entrenchment by statute is not something that has been – or at a legal level could be – done for the Scottish Parliament itself. The Parliament relies for its entrenchment on the consent of the Scottish people, expressed by the referendum result of 1997. Even so, local government is a very important part of our constitution, codified or otherwise, and it too enjoys the support of the population. We want the right relationship between central and local government, and we want local government – which the Scottish people value highly – to be a continuing and valued part of our constitutional settlement. The question for us is whether a form of formal, legal, entrenchment could do this, and if so how: this is an issue on which we welcome further views.
168. There is clearly an argument to be made for a similar arrangement in Scotland. We have been examining this issue in detail and will continue to do so: we would welcome further thoughts on this subject. For us the key issue is what this guarantee would offer. We see some merit in Councillor O’Neill’s view that councils need a binding understanding that the “proper” relationship between local and national government is one which devolves power and resources, and that frees up councils from “unnecessary statutory duties and central direction”. However, this issue requires careful consideration: one person’s unnecessary statutory duty can be interpreted as another one’s a tool for social justice.

44 Michel Rosenfeld and András Sajó (ed.), *The Oxford Handbook of Comparative Constitutional Law*, (Oxford: Oxford University Press, 2012), p. 616.

45 Stephen Tierney, *Constitutional Referendums: The Theory and Practice of Republican Deliberation*, (Oxford: Oxford University Press, 2012), p. 87.

46 Henning Jørgensen, *Consensus, Cooperation and Conflict: The Policy Making Process in Denmark*, (Cheltenham: Edward Elgar Publishing, 2002), p. 50.

## H. Inter-governmental relations

169. There is a need for different levels of government to work more effectively together at local, Scottish, UK and European level. Voters rightly expect no less. In our view, there is a need for more robust and well-developed mechanisms to inform relations between every level of government. One of the limitations of the Scotland Act 1998 was that, although it set out well-designed legal procedures for resolving disputes about legislative competence, it did not make any provision for inter-governmental interactions.
170. Inter-governmental relations are however essential within a constitutional system comprised of multiple levels of government. When devolution was established, less attention was given to mechanisms for supporting interaction than might have been the case. It was perhaps too readily assumed that informal relations between ministers would be sufficient to resolve problems and conflicts as they arose. There is also a compelling argument that not enough thought was given to the implications of devolution for the wider UK constitution. The issue of intergovernmental relations (and, indeed, inter-parliamentary relations) was dealt with in the Calman Commission report, but although they emphasised the importance of the issue, they stopped short of recommending statutory mechanisms.
171. An innate (although, we do not believe, insurmountable) difficulty with inter-governmental relations is that it requires politicians, who are often in opposition to one another, to cooperate and find consensus. In recent years, we have had experience of widely diverging political views at different levels of government. This has proved challenging, and although there has been some evidence of good inter-governmental dialogue, overall, at present, inter-governmental arrangements remain underdeveloped – at all levels. Voters rightly expect different levels of government to work collaboratively in the public interest and it may be that the incentives for this need to be sharpened. No formal machinery for inter-governmental relations will ever prevent disagreements: disagreement is the very stuff of politics. Nevertheless, in our view, the mechanisms for inter-governmental relations need to be further developed at all levels. We welcome further thoughts from interested groups and stakeholders on this issue and on how the necessary improvements might be achieved.

## I. Conclusion

172. In our view, local democracy should be a vital part of our system of government, but it has been in decline under both Conservative and SNP administrations, with a loss of functions, fiscal autonomy, and organisational discretion over services. Relations between local and devolved government were marked by cooperation and collaboration during the period 1999 to 2007. This approach stands in marked contrast to the centralisation that existed under the Conservative-controlled Scottish Office and is now the hallmark of SNP government.
173. The 1996 reorganisation was disruptive, costly and unnecessarily partisan, and a lesson in what not to do.<sup>47</sup> The SNP approach has been more insidious: the rhetoric of partnership concealing the reality of hollowing out, and denying Scottish councils the fiscal freedoms they seek for themselves. Our aim is promote the devolution of power to councils and communities, in terms of both finance and service delivery, while meeting the expectations of Scottish people for a common high standard in key services. Any options we recommend will avoid cost and disruption, and will deliver real benefits.
174. Previous reorganisations, north and south of the border, provide a cautionary tale about the perils of inadequately designed and poorly implemented changes, as does the SNP's badly handled implementation of police reform and our remit is to propose constitutional strengthening not structural change. We shall therefore focus on strengthening local autonomy and accountability.
175. We do not believe that the man in St Andrew's House always knows best. We do not believe in big government for its own sake, and we certainly do not believe in the nonsense of the "big society". The reinvigoration of local government, ensuring more participation in the democratic process, and genuine empowerment of communities are central to Scottish Labour's approach.
176. The SNP have disempowered local government by centralising power. This approach is contrary to the aspirations and aims of the McIntosh Commission. We will return central-local government relations to the parity of esteem and mutual respect enshrined in McIntosh. In our view, centralised control leads to weaker democratic accountability.
177. The council tax freeze does not come without a cost. Individuals may pay less, but the communities they live in are worse off. In local authorities up and down Scotland, the jobs of those working in vital public services on which people depend have been lost, or are at risk, because of the freeze. The Scottish Government's refusal to fund the council tax freeze means that while individuals may pay less, the communities they live in are worse off and so ultimately are they. We must consider whether this is sustainable in the long-term.

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<sup>47</sup> The cost of the 1996 transition has never been resolved satisfactorily: it was estimated by the Scottish Office to be £146 million but by CoSLA at between £375 million and £720 million: Michael Chisholm, *Structural Reform of British Local Government: Rhetoric and Reality*, (Manchester: Manchester University Press, 2000).

- 178.** Revitalising local government is not simply a matter of reorganisation. Indeed, given the current pressures faced by local authorities, we do not at this stage find any compelling case for wholesale structural reform of local government. Our focus is on the self-renewal of councils, rather than prescribing changes in law. We need organisational arrangements that support change, rather than stand in the way.
- 179.** Real devolution is about people and communities. We need to return power from state to people, to think again about how government works to enable people to participate effectively in matters of public concern, and empower communities to engage in issues surrounding local priorities and delivery. If we can achieve this, we will have achieved real devolution.

## Part 6 The way forward

180. The Devolution Commission will be continuing its programme of work over the coming months. There are four main areas of concern to us: empowering communities; creating greater accountability; establishing a more socially just Scotland; and strengthening Parliament.

### Empowering communities

181. Devolution is not just about transferring powers from one building in Westminster to another in Edinburgh: it is also about empowering local government and communities. We will be looking at what scope there is for the transfer of additional powers to local government and communities, what these powers should be, in addition to the possibility for the further devolution of powers to the Scottish Parliament.

### Creating greater accountability

182. Taxation provides the revenue to support the delivery of social and economic policy objectives. Different forms of taxation can also in themselves be used to drive social and economic change. As a result, we will be examining what potential there is for greater accountability in the tax system and on the further devolution of tax powers to the Scottish Parliament.

### A more socially just Scotland

183. The Welfare State provides everything from child benefit to pensions – it is the foundation that underpins a socially just Scotland and UK. Correspondingly, we will be considering what changes to delivery and devolution, if any, can support a more socially just Scotland

### Strengthening parliament

184. Scottish Labour believes in open, transparent and accountable government. We will be investigating whether the devolution settlement can be improved to support (a) increased civic engagement in the legislative programme, and (b) a balanced parliamentary process that allows all views to be considered.

## GLOSSARY

APD	Air Passenger Duty
CEC	Crown Estate Commissioner
CGT	Capital Gains Tax
CoSLA	Convention of Scottish Local Authorities
Devo-Max	When all taxes are raised and controlled in Scotland and money is sent to Westminster by way of a grant to pay for activities the UK government carries out on Scotland's behalf, such as defence and foreign affairs
Devo Plus	Scottish Parliament takes control over most taxes – with the exceptions of VAT and National insurance – to raise the income necessary to meet Scotland's expenditure responsibilities
GDP	Gross Domestic Product
GERS	Government Expenditure and Revenue in Scotland: a Scottish Government publication estimating Scotland's fiscal balance
Home Rule	A term traditionally used in the UK to refer to a degree of self-government, devolution or independence, for constituent nations
HMRC	HM Revenue & Customs
IPPR	Institute for Public Policy Research
MEP	Member of European Parliament
MP	Member of Parliament
MSP	Member of Scottish Parliament
NESTA	National Endowment for Science, Technology and the Arts
NHS	National Health Service
NI	National insurance
OECD	Organisation for Economic Cooperation and Development

PAYE	Pay-As-You-Earn - a means of payment of income tax in the UK
SEC	Scottish Executive Committee
SOA	Single Outcome Agreement
STV	Single Transferable Vote
UK	United Kingdom
VAT	Value Added Tax

