

'Scotland's devolved tax powers'

Introduction

- Thanks for the invitation today.
- It's nice to know that when a tax professional asks you to lunch, you get the full meaning of the phrase 'there is no such thing as a free lunch!'
- However being an economist, I have the opportunity to get my own back as the request was for me to forecast speaking for around 10 minutes. So with my professions track-record at forecasting, settle in for anywhere upwards of 25 mins of economics chat!
- But seriously thanks for the opportunity to speak with you.
- I've been asked to set out some reflections on the experience of the first few years of tax devolution.

Changes and institutional reform

- To start, it often goes unnoticed – particularly given the continual constitutional ding-dong – just how significant a change we're seeing to tax devolution in Scotland.
- I started my interest in Scottish fiscal policy in 2001. I was at Glasgow Uni and just about to embark on my PhD looking at the international experience of fiscal decentralisation.
- Back then, what was striking, was just how limited Scotland's tax powers were compared to our competitors.
- Devolved and assigned taxes were equivalent to just 12% of the Scottish Budget.

- But now, and assuming that all the planned powers come on stream, this will rise to nearly 50%. On top of that, around £3.5bn of social security responsibilities will come on the books in April.
- Now many will argue that we need to go further, and the repatriation of powers from Brussels may provide some new responsibilities (or not depending upon you believe!), but at the very least I think that we can all agree that Holyrood's powers - for better or worse - have been transformed.
- One positive has been the boost to capacity in tax, economics and financial management that this has led to.
- The Scottish Fiscal Commission has not only ensured that the Budget is underpinned by credible forecasts, but their work is helping us to better understand the Scottish economy and public finances more broadly.
- Audit Scotland is doing great work to monitor not just trends in day-to-day public spending but is also undertaking new analysis around the sustainability of public budgets in this new fiscal landscape.
- Parliament and government have greatly increased their capacity.
- Our institute has also grown. One encouraging aspect that we're seeing is a growing interest amongst young people in Scotland's economy and public finances.
- We run an initiative called Economic Futures which includes work placements for students from Scottish universities. Last year it was oversubscribed 10 to 1.
- [So a shameless plug!! If you're able to provide an opportunity for a young person then please drop me an email!]

Public understanding & accountability

- On balance, I think that most people would agree that tax devolution has been welcome and strengthened the powers of Holyrood.
- A parliament where the focus was primarily about dividing up a pot of money always felt like half the story.
- Now there is now an increasingly vibrant debate, not just about how much money is spent, but how much is raised (and from what sources).
- But it's not all been plain sailing.
- We've seen that with the shelving of plans – at least temporarily – to assign VAT to the Scottish Budget this year.
- Assigning VAT was always baffling. How many people in this room know how much VAT their firm is liable for in Scotland and how much for the rest of the UK?
- In addition, there have – and remain – challenges in levels of public understanding of the new Fiscal Framework.
- For me, there are too many actors – the OBR, the SFC, HMRC, Treasury, the Scottish Government – each with their own individual role and responsibility but not one taking oversight for the framework.
- This poses a risk to accountability. And – as we have seen over the last year – it creates opportunities for misunderstanding and mischief.

Reflections on policy change

- Another reflection is on the evolution of policy.

- If one of the aims of tax devolution was to not just give politicians accountability, but also autonomy, then it has clearly succeeded.
- Indeed, in some areas, government has been bolder than first thought.
- The introduction of a 5-band income system was a visible statement of intent to do things differently.
- The new child payment shows a similar willingness to be bold in social security.
- Now as tax professionals I'm sure it gives you headaches when policy departs from the rest of the UK. But that's what tax devolution is all about.
- So policy has led to divergence as arguably it should.
- However, whether or not the decisions taken on a tax-by-tax basis add up to an overall coherent strategy is open to question.
- This isn't just a criticism of government. All parties typically work in the same silos.
- The current debate is framed around making the case that for each individual tax devolved, Scotland has the 'fairest system in the UK'.
- But looking at specific taxes in isolation to see if they are 'fair' or 'progressive' relative to the UK, crowds out a more important debate about whether or not the *system as a whole* in Scotland could be fairer or more efficient.
- For example, current policy ensures that "*over half of all Scottish income tax payers pay less tax than if they lived elsewhere in the UK*". But the maximum saving is 40p per week. Is this soundbite sensible at a cost of £50m?

- On income tax more generally, the policy is to raise the overall tax liability in Scotland vis-à-vis the UK supposedly to invest in public services. But on business rates, the policy is for and I quote *“95 per cent of properties to pay a lower poundage than they would in other parts of the UK”* . Articulating that you pay more for better services on income tax, but that you should pay less on business rates. seems hard to square. Particularly when the evidence is that the beneficiaries of rates reductions often tend to be landlords rather than businesses themselves.
- What about consistency of protecting those on low incomes? How does that sit with above inflationary increases in the regressive council tax? But again, business rates are going up less than inflation?
- And of course, whilst we focus our attention on how rates and bands compare to the rest of the UK, the big structural reforms that everyone agrees are needed – e.g. on designing an effective local tax to replace the outdated, inefficient and regressive council tax – get kicked into the long-grass.

Reflections on process

- My fourth reflection is that – despite some progress – we’re some way off an effective budget process for the new powers.
- Debate and scrutiny by parliament remains condensed in too a short period of time – and that’s even before the UK Government messes up the budget timeline!
- I know that my friend and colleague Charlotte Barbour and ICAS have thought carefully about options to tidy up and streamline the legislative process including the introduction of a Tax or Finance Bill to allow for more effective scrutiny.

- And this would be one welcome development.
- More generally, efforts to improve year-round budget scrutiny have been ongoing now for a few years – with mixed success.
- For example, after a promising start, the new annual Medium Term Financial Strategy process stalled last year. Indeed, last year’s Medium Term Financial Strategy was quite an achievement in that it wasn’t a strategy and really didn’t say much about the medium term!
- And finally, the Budget document itself adds little to the process. Last month’s tome was over 280 pages long - nearly three times the length of the UK Budget. This year the theme was wellbeing. Ploughing my way through 283 pages didn’t do much for my wellbeing.
- But more seriously, the constant re-classifications amongst portfolios make it nigh on impossible for anyone to scrutinise priorities. Or even be clear about the substance that underpins these priorities in the first place.

Final Remarks

- Next year, we have the review of the Fiscal Framework. And that’ll mark 5 years of tax devolution. Some parts have worked well. Others less so. So the review will be interesting.
- We also have the next Scottish election.
- Back in 2016, the debate around tax was largely about who planned to raise the most to spend.
- But it will incumbent on all political parties to set out a much broader and joined up approach to all aspects of tax policy – both individually and strategically – for the next 5 years of tax devolution.