

Careful What you Wish for? Risk and Reward with Scottish Tax Devolution

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Abstract

September 2022 marks twenty-five years since the referendum on the creation of the Scottish Parliament. From the early days of devolution, debates over Holyrood's tax powers have been a recurring theme. Recent reforms to the Parliament's tax powers have been driven by the Scottish National Party and the Scottish Conservatives, an indirect coming together of arguments from two unlikely political allies. Both have, however, embraced arguments for greater autonomy and fiscal responsibility within Scottish devolution. This article reflects upon the experience of enhanced tax devolution in Scotland through the lens of three competing 'logics' of devolution, namely: a logic of 'accumulating competencies'; 'delivering fiscal responsibility'; and 'capacity to pursue distinct policies'.

Keywords: devolution, Scottish government, Scottish National Party, Scottish Conservatives, taxation

Introduction

TAX DEVOLUTION within the UK remains a central element of our political debate, with few arguing against further decentralisation of tax levers. In England, the former Secretary of State for Levelling Up has made clear that the devolution of business rates is 'definitely the direction of travel [the UK government] want to go down'.¹ At the same time, an independent Fiscal Commission has looked at options for tax devolution to Stormont. Wales, meanwhile, is finding its feet with new responsibilities for income tax. Yet, there has been relatively little reflection on the existing experience of enhanced tax devolution in the UK. In this article, we reflect on Scotland's tax devolution journey.

In 1999, the new Scottish Parliament was granted responsibility for many aspects of

day-to-day public spending, including health, education and justice. But tax powers were limited to local taxes (including council tax) and modest flexibilities on income tax (the 'tartan tax'). Since then, a series of reforms has increased Holyrood's tax powers. First, the Calman Commission led to greater flexibilities over income tax, along with the devolution of stamp duty and landfill taxes. Second, the 'vow' in the final days of the 2014 independence referendum saw David Cameron, Ed Miliband and Nick Clegg promise 'extensive new powers for the Parliament'. The Smith Commission that followed recommended that Holyrood raise around 50 per cent—symbolically important in unlocking the phrase 'the majority'—of its budget from taxes raised in Scotland. These reforms were designed to deliver two: 'overarching improvements to the devolution settlement: a more accountable and responsible Parliament; and a more autonomous Parliament'.²

This was a coming together of two arguments: a push for 'more powers' to do things differently, aligning with demands for the Parliament to be more 'fiscally responsible'. This

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¹'Gove calls for devolution of control of business rates to England's mayors', *Financial Times*, 4 February 2022.

²The Smith Commission. *Final Report*, 2014, pp. 4 & 5.

brought together unlikely allies: the SNP and the Conservatives, who were instrumental both in shaping the arguments for tax devolution and, as the parties in power in Holyrood and Westminster, negotiating its implementation.

In this article, we provide some reflections on Scotland's experience of tax devolution, identifying several issues that have emerged. In doing so, lessons can be drawn for other parts of the UK looking to follow a similar path. We show that, using the current in-vogue phrase of 'risk and reward', the 'reward' has come through an ability to set distinct tax policies, albeit these (both through choice and constraints) have tended to tweak UK tax structures rather than offer fundamental reform. But a cost—at least so far—has come in the form of financial 'risk'. Scotland's budget is under pressure from weaker tax growth and, in the years ahead, is projected to be smaller than would have been the case had tax devolution not gone ahead. This is despite taxing higher earners more. At the same time, improvements in fiscal responsibility have only partially materialised. Budget scrutiny has been patchy.³ The creation of a more complex budget system has arguably, so far, resulted in less clarity over lines of fiscal responsibility.

We argue that Scotland's experience of enhanced tax devolution should be understood in terms of *both* 'risk' and 'reward'. On the one hand, we have the three competing logics of the 'rewards' of enhanced devolution—a logic of accumulating competencies as an objective in itself; the objective of delivering fiscal responsibility; and an objective of pursuing distinct policies—with the first two producing the necessary coalition of disparate interests to enact these changes. On the other hand, there is the 'risk' element, including what is an acceptable level of risk to transfer and the tools to manage this risk. Some of these risks have materialised during Scotland's experience of tax devolution to date. Debates on fiscal devolution in the UK typically focus upon the rewards, but as we show, the risks are real and require careful

management. Politicians—on all sides—need to be careful what they wish for.

Scotland's new tax powers

In 1999, the Scottish Parliament and its Executive took responsibility for the powers that had been the function of the Scottish Office. These included health, education, local government, police and fire, and economic development. A key feature was the absence of welfare payments. This was owing, in part, to an expectation of 'solidarity' across the UK and the argument put forward by many prominent advocates of devolution, including Gordon Brown, that the best way to tackle inequalities was to boost income levels at the UK level.⁴

A significant feature of Scotland's initial devolution settlement was the imbalance between spending and tax responsibilities. Only two local taxes were under the responsibility of the Scottish Parliament: council tax and non-domestic (business) rates. Holyrood did have the ability to vary the basic rate of income tax by 3 pence, but this power was never exercised. In consequence, over 90 per cent of the Scottish budget was funded from the Westminster block grant. Initially, although there were debates over greater tax devolution, it only moved up the political agenda towards the end of the first decade of devolution. Why was this the case? In part, the early years of devolution coincided with a period of economic stability and significant public spending growth. It was also a period of party congruence, with Labour dominant in Westminster and the largest party in the Scottish Parliament.

The pivotal moment, however, was the election of the SNP in 2007. This was soon followed by the 2008 Calman Commission. Established by the opposition parties and supported by the UK government, it recommended greater flexibility to vary income tax. UK standard and higher rates in Scotland were to be reduced by 10 pence, with a corresponding cut in Scotland's block grant. Holyrood then had the opportunity to set a Scottish rate of income tax (SRIT), with HMRC forecasting how much this would raise. If for example,

³See, Policy Scotland, 'Additional powers: better understanding? Better scrutiny?', University of Glasgow, 2021; <https://policyscotland.gla.ac.uk/additional-powers-better-understanding-better-scrutiny-a-new-report-on-scotlands-new-budget-powers/> (accessed 8 July 2022).

⁴See G. Brown, *The Labour Party and Political Change in Scotland, 1918–1929: The Politics of Five Elections*, unpublished History PhD, Edinburgh University, 1981.

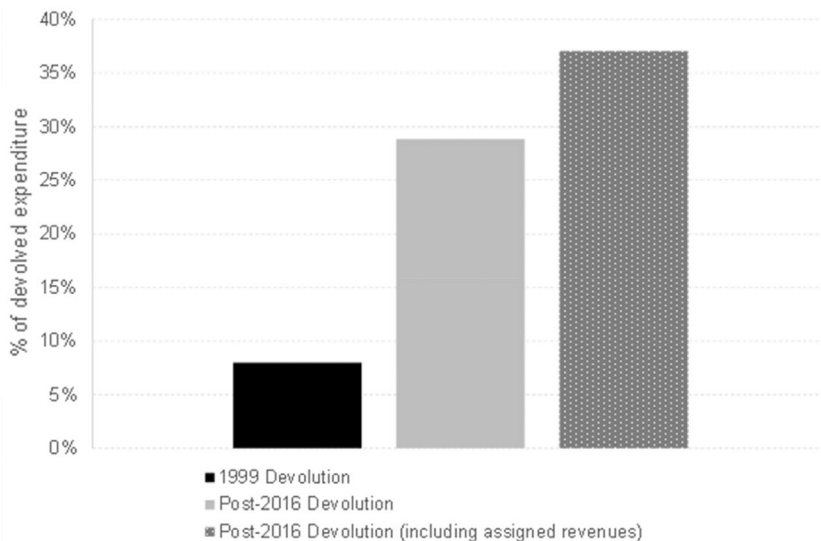


Figure 1: How have the tax powers of the Scottish Parliament evolved?
 Source: Scottish Government, 'Government expenditure and revenue, Scotland'.

the SRIT was 10 pence, the budget would be no better or worse off. If a higher rate was set, the UK government would transfer what it believed to be the additional revenues raised (and vice versa). Alongside this, there was the devolution of stamp duty on property transactions and landfill tax. These recommendations formed the Scotland Act 2012.

The 2014 Smith Commission—coming soon after the independence referendum—was bolder, not just in terms of the degree of autonomy it recommended, but the extent to which it thought that Holyrood should take a stake in the performance of Scotland's economy. The Commission recommended that all non-savings non-dividend (NSND) income tax revenues should be transferred (over 90 per cent of income taxes in Scotland), more than doubling the scale of income tax devolution. The first 10 pence of the standard rate VAT and the first 2.5 pence of the reduced rate VAT were also to be assigned (in effect, assigning around half of the VAT revenues raised in Scotland).⁵ Aggregates levy and air passenger duty were to be devolved too. Figure 1 shows

the evolution of Scotland's tax powers as a percentage of devolved expenditures since 1999.

Crucially, a revised 'fiscal framework' was negotiated between the Scottish and UK governments in 2016. This included methods to adjust the block grant to compensate the UK government for the tax powers being devolved to Holyrood, a new independent fiscal commission, and rules for day-to-day budget management. Most importantly, and in contrast to the original income tax powers of the Scottish Parliament, Holyrood became responsible not just for the *marginal* changes in revenues from tax decisions, but for the relative performance of the *entire* base of devolved (or shared) taxes in Scotland.⁶ In short, should Scotland's tax base grow more quickly than the equivalent tax base in the UK, the Scottish Parliament's spending capacity would be better off than it would have been before tax devolution. Should it grow more slowly, it would be worse off.

Alongside this, eleven social security benefits, mainly related to ill-health, disability and care for the elderly, are being devolved. In

⁵The timing of VAT assignment has yet to be agreed. Challenges over estimating VAT revenues raised in Scotland and delays associated with Covid-19 have delayed implementation.

⁶The technical details of the Fiscal Framework are set out in HM Treasury, 'The fiscal framework', 2016.

2022/23, these are forecast to total around £4 billion and reach over 1 million claimants.

How has ‘risk and reward’ fared?

To assess the experience of Scottish tax devolution we explore the concept of ‘risk and reward’ given its prominence in recent debates in the UK, looking at two elements: (i) autonomy, and (ii) spending levels.⁷

Autonomy

For the SNP, the key prize from tax devolution was increased autonomy. They have used their new powers to make Scotland—in their eyes—the ‘fairest taxed part of the UK’ and the ‘lowest taxed part of the UK’, as Nicola Sturgeon has claimed. This has included a five-band income tax schedule, with a starter rate between £12,570 and £14,732 set 1 penny below the UK basic rate of 20 pence. Other measures, including adding 1 penny to the higher and top rates and freezing the thresholds where taxpayers move into higher bands, have been designed to raise revenue. The aim has been to collect around an additional £500 million from taxing higher earners more than in England. The SNP points out that, as a result of these decisions, the majority of Scottish income taxpayers pay less than if they lived in England. The maximum saving for anyone is, however, only £21.62 per annum. For higher earners, the differences are larger. For example, an individual earning £50,000 in Scotland faces an additional tax burden of £1,489 per annum in 2022/23.

A similar trend is evident with other taxes. For example, the schedule of tax on property transactions is more progressive in Scotland, with lower rates on cheaper properties alongside higher rates on more expensive ones. On local taxes, the same story emerges. On council tax, the ratio of tax paid by properties in bands E–H compared to A–D is higher in Scotland, whilst the typical band D tax is less than in councils in England. For businesses, qualification for 100 per cent relief extends to a broader base of smaller business properties. With progressivity the focus, the poundage is lower

than elsewhere in the UK, although any saving for most businesses is again small. Larger Scottish businesses pay a ‘supplement’ on top of the standard poundage. But critics have argued that whilst individual tax policies have been more ‘progressive’ at the margin, this does not necessarily mean the establishment of a fair tax system. For example, the SNP has not replaced the council tax. This is despite a 2007 manifesto commitment to do so.

Decisions taken on social security are also relevant for the discussion on tax devolution. Indeed, a key motivation for increasing taxes on higher earners has been to fund social security policy differences with England. Policies to replace existing UK policies are more generous in the criteria for qualification and payment schedule. At the same time, new benefits, including a new Scottish Child Payment (SCP), have been introduced. This £10 per week benefit, rising to £25 per week by the end of 2022, is for families in receipt of certain qualifying UK benefits including Universal Credit and Jobseeker’s Allowance.

Budget outcomes

If gaining—and using—new tax powers has been the ‘reward’, the impact on Scotland’s budget has been the ‘risk’. As set out above, the Scottish budget is now determined by a mix of a block grant and devolved taxes. So, is the Scottish budget better or worse off following further tax devolution? A useful indicator is what is called the ‘net tax’ position. The net tax position can be positive/negative for two reasons. First, the Scottish government might choose to increase/decrease relative tax rates. Second, the Scottish tax base might grow relatively more quickly/slowly.

In the early years of tax devolution, the net tax position was positive, with Scotland’s budget slightly better-off than it would have been without tax devolution. But the uplift has been much less than the increase in the tax burden would suggest. In 2020/21 for example, the net improvement from income tax devolution was only around £100 million, despite a tax policy that it is estimated should be raising closer to £500 million (the equivalent of more than £5 billion in UK terms). This net income tax position is predicted by the Scottish Fiscal Commission to actually turn negative from 2021/22 until 2023/24. The reason is that the

⁷P. Johnson, ‘More devolution of tax powers is a risk worth taking on all sides’, *Times*, 20 December, 2021.

Scottish tax base has been growing—and is projected to grow—more slowly than the UK as a whole (with outturn data weaker than forecast too, leading to negative adjustments having to be made in subsequent years). The relative difference on income tax is forecast to shift back in Scotland's favour from 2024/25 onwards. But this is, in part, a result of UK government plans to lower the basic rate of income tax to 19 pence elsewhere in the UK. This will turn on its head the narrative that lower earning income taxpayers pay less tax in Scotland. Any attempt to match the UK decision will reduce Scottish revenues and squeeze the Scottish budget.

Added to this, Scotland's new social security powers are costing more than the amounts transferred from Westminster to deliver a comparable level of benefit spend. The Scottish Fiscal Commission estimates that this will add nearly £1.3 billion per annum to Scotland's budget bill by 2026/27. Unless the net tax position improves substantially, this implies day-to-day devolved budgets will need to be smaller than they would otherwise have been to pay for such commitments. The Scottish Parliament, having accumulated new competencies and used these new tax powers to 'do things differently', is now facing the fiscal reality of taking on responsibility for its tax base.

Explaining Scotland's budget experience

Having reviewed the 'risk and reward' experience of Scottish tax devolution we now turn to explore the reasons for these outcomes.

Form of fiscal devolution

The most obvious driver of the outcomes set out above is the design of the fiscal framework established to support Scotland's tax powers. In our view, four elements are key.

First, the scale of tax devolution has grown significantly in recent years. Post-2017, the proportion of devolved revenues as a share of the Scottish budget has risen from around 8 per cent to 29 per cent currently, with a further rise to 37 per cent post the assignment of VAT revenues.

Second, the individual tax flexibilities offered to the Scottish Parliament with recent

devolution are more expansive than before. Both the original 'tartan tax' and the Calman SRIT had strict limits on how power could be exercised. Both, for example, only allowed changes in tax rates and not the thresholds at which different rates could be levied. Now, short of lowering the personal allowance beyond the UK rate or changing the definition of 'income' for tax purposes, the Scottish government is—in principle—free to put in place any income tax structure it likes. On the fully devolved taxes, the autonomy is even greater.

Third is the technical way the powers have been transferred, linking budget outcomes with movements in the overall Scottish tax base. Crucially, the Scottish government now bears the risk not just for changes at the margin from different policy choices, but for any factor that shifts relative performance (good or bad). This includes different policy choices by the UK government which exercises a wider range of economic and fiscal levers. The exposure of the Scottish budget to the risk of worse relative performance of tax revenues contrasts with the original 'tartan tax' proposal. In that case, Scottish policy makers could decide to increase or decrease the basic rate by 3 pence, with the amount of money transferred an estimate *only* of the effect of that change. Now, the Scottish budget varies depending upon the relative performance of the full Scottish income tax base (even if policy stays the same). It is this mechanism that was designed to 'incentivise' politicians to ensure that the Scottish economy performed well and to hold the Scottish government 'accountable'.

Fourth, the administrative way the powers have been implemented is—as identified by the OECD—'complex and largely untested'. The Scottish budget is now a mix of a block grant, devolved and shared tax revenues, various adjustments to Westminster funding to account for tax devolution, different borrowing programmes and rules on the use of savings. Various rules also now exist for forecasting and reconciling changes in tax revenues from year to year. This inherent complexity, while now evident, was not the source of much debate during the transfer of powers.

The economic context

If the fiscal framework provides the foundations for Scotland's experience since tax

devolution, the performance of the economy has been the main driver of outcomes. Scotland has a prosperous economy. On key metrics such as economic output per head, it ranks as the richest part of the UK outside London and the South East. But what matters for the Scotland budget under the new fiscal framework is how it has been performing relative to the UK as a whole *since* further tax devolution, and it has been lagging behind the UK over this period. The average annual growth in GDP per person in Scotland between 2009 and 2019 was 0.6 per cent. This contrasts with growth of 1.3 per cent in the UK as a whole. Both are down from their 1998–2007 averages of 2.0 per cent and 2.1 per cent respectively, but Scotland is down by more. The same holds for the period since 2016 when these new tax powers were first exercised.

On key determinants of income tax revenues—labour market participation rates and average earnings—a similar story emerges. What explains these trends? First, the proportion of Scotland's population aged 55+ is increasing more rapidly than in the UK as a result of weaker historical in-migration, a long-term decline in the birth rate and improved life expectancy. Older age groups typically have lower employment participation rates, putting pressure on Scotland's income tax base relative to the UK. Second, earnings growth has been slower in Scotland than in the rest of the UK, driven, in part, by the tapering off of activity in the North Sea. One-third of all jobs supported by oil and gas activity in the UK are estimated to be in Scotland.⁸ These jobs typically pay above the national average and contribute disproportionately to income tax revenues. The outlook for the North Sea over the next few years is more positive than it has been (because of the recent spike in energy prices), but the long-term trajectory is one of decline in oil and gas mitigated (hopefully) by a transition to new forms of sustainable energy.

Whilst there are differences of opinion over the Scottish government's management of the economy, it is hard to argue that tax policy choices since 2016 have led to a significant (negative) divergence in tax revenue growth.

⁸See, Oil and Gas UK, 'Workforce and employment insight 2021', OGUK, Aberdeen, 2021.

Recent HMRC evidence, for example, on the impact of higher taxes in Scotland, suggests that this has had little impact on tax revenues.⁹ Instead, we conclude that the divergence we have seen has largely stemmed from factors outside the immediate control of devolved policy makers (indeed, any policy maker at Westminster too), and reflect longer-term dynamics that policy has yet to address fully.

Discussion

The experience of 'risk and reward' through tax devolution in Scotland provides a rich seam to study the practicalities of constitutional change. Yet, it remains striking that this narrative continues to frame debates over the devolution of tax powers, in Scotland and elsewhere in the UK. What are the key reflections from the Scottish experience that need to be understood and that have shaped the experience of 'risk and reward'? We identify two key elements.

The 'logics' of devolution

There are three 'logics' that can frame calls for greater devolution. First, there is a (nationalist) logic that supports accumulating more competencies, regardless of how such competencies are used. A second logic is instrumental, seeing more competencies as a means of pursuing objectives that cannot be achieved or are inhibited by existing competencies. A third logic is a fiscally conservative one, viewing it necessary to balance the Parliament's competence to spend public money with more fiscal responsibility to make decision making more accountable. These are not necessarily mutually incompatible, but involve different emphases. It is possible to support an accumulation of competencies in pursuit of instrumental goals and even to make the Parliament more fiscally responsible.

At times, SNP narratives have spanned each of these logics. While never abandoning its

⁹HMRC, 'Estimating Scottish taxpayer behaviour in response to Scottish income tax changes introduced in 2018 to 2019', 16 December 2021; <https://www.gov.uk/government/publications/estimating-scottish-taxpayer-behaviour-in-response-to-scottish-income-tax-changes-introduced-in-2018-to-2019> (accessed 8 July 2022).

support for independence, over much of the period since devolution, the SNP has had a pragmatic approach, supporting accumulating competencies. This reflected an awareness of the lack of support for independence at that time: the ESRC Scottish Election Study 2007 found that only 23 per cent of voters supported independence, while 45 per cent wanted more devolution and 32 per cent wanted no change. Even amongst SNP voters, only 59 per cent supported independence and 37 per cent supported more powers.¹⁰ The SNP recognised that its best hope at that time was to achieve independence by a gradual accumulation of competencies.

For example, in 2009, the newly elected SNP-led Scottish government made the case for full fiscal autonomy (or 'devo max') arguing that it would 'provide significant autonomy in the setting of fiscal policies to match the preferences and circumstances of the people of Scotland and would represent a significant step forward'.¹¹ This document is noteworthy too for its references to improved fiscal responsibility from tax devolution. However, and crucially, this has not involved a fixed position on every particular public policy issue, with priorities shifting over time, reflecting both the views of its evolving leadership and the objective of retaining a broad coalition of public support as well as among elected members and the party membership.

The biggest change in positioning has been from within the Conservatives. Long-term sceptics of devolution, they led the 'No' campaign in 1997, and opposed tax devolution, warning a 'tartan tax' would harm the economy. But with the Scottish Parliament firmly established, a new generation of Conservative politicians argued that a fiscal framework that only gave policy makers the powers to spend money was flawed (a 'pocket money parliament' of sorts).¹² Devolution was thought to only work if Holyrood took on responsibility

for raising a significant proportion of its own budget. What is striking is just how, for a party that was opposed to tax devolution in 1999, the current design of Scotland's new tax powers drew heavily on Scottish Conservative Party proposals. Their 2014 Strathclyde Commission recommendations on the specifics of tax devolution (for example, income tax, VAT and air passenger duty) were largely implemented like-for-like in the Smith Commission recommendations. Importantly, however, so too was their stipulation that it 'must be a condition of any further fiscal devolution that a robust and stable long-term mechanism is devised, which will demonstrate a clear link between Scottish fiscal policy choices and expenditure in Scotland'.¹³ Given the political dynamics in Scotland, this is remarkable.

What has emerged and has driven the nature of further fiscal devolution in Scotland is a confluence of disparate interests. This has involved Conservative support for greater fiscal responsibility and SNP ambitions for the accumulation of competencies finding common cause. There has been a narrative from the SNP on creating a fairer welfare and tax system, an instrumentalist logic, and there has been some evidence that it has pursued this (although critics will argue that they have done so cautiously leaving the impression that such instrumentalism is to demonstrate Scottish distinctiveness). Alternatively, progressive instrumentalism may have been limited by conservative fiscal responsibility. In other words, any ambition to embark on bold progressive measures is tamed by the need to retain a core part of the SNP's electoral support. For the Conservatives, a key element of the reforms was establishing a direct relationship between Scotland's economic performance and Scottish public spending (although it is highly debatable if the improvement in scrutiny that they hoped this would bring has materialised).

The new fiscal arrangements in place in Scotland represent a devolution of both risk and reward. In doing so they deliver something for each part of this coalition of disparate interests. To date, most of the attention has been focussed on the 'reward' from gaining

¹⁰R. Johns, D. Denver, J. Mitchell and C. Pattie, *Voting for a Scottish Government: The Scottish Parliament Elections of 2007*, Manchester, Manchester University Press, 2010, p. 85.

¹¹Scottish Government, 'Fiscal autonomy in Scotland: the case for change and options for reform', 2009, p. 36.

¹²R. Davidson, 'Time for change at Holyrood', *The Scotsman*, 1 June 2014.

¹³*Commission on the Future Governance of Scotland*, Strathclyde Commission, Scottish Conservatives, May 2014, p. 10.

these powers and being able to exercise them, but the risk element is an integral part of the new fiscal powers and requires much greater attention than it is currently receiving. This is perhaps most obviously demonstrated by the decision to assign VAT revenues to the Scottish budget—a policy that transfers risk for the relative performance of the VAT base in Scotland but brings no ability to change rates or bands.

The process of reform

Could the outcomes—most importantly in this context the ‘risks’—we have seen crystallise since tax devolution have been foreseen? Perhaps. But it is worth highlighting that the speed at which the powers were negotiated and transferred was unprecedented. The Smith Commission published its recommendations within just over two months. It was just twenty-eight pages long. The Scotland Act that turned these recommendations into action was delivered in just over a year. Unlike the 2014 independence referendum, there was little in the way of external scrutiny or public debate. Parliamentarians scrutinising the bill constantly complained of the lack of information on the evidence developed to inform negotiations.

Not only that, but this was an explicitly political negotiation as opposed to a principles-based (or civic society-designed) framework. An implication of this was that each party’s ‘red line’ was incorporated into the final arrangement. This produced an asymmetric process focussed upon how Holyrood’s powers could be reformed, not how the UK tax or fiscal system might change. The result of this process was a complex model, often relying upon *ad hoc* solutions to political disagreements.

Many will argue that ‘this is devolution for you’. It brings responsibilities, opportunities, potential rewards, but also risks. Interestingly however, there has been limited—if any—debate about the level of risk-sharing in the devolved system with a ‘lack of consensus, or even debate, about the type of fiscal risks and incentives Scotland (and other devolved governments) should face’.¹⁴ Most other states with substantial sub-national devolution

(including Germany, Canada and Australia) try to assess the spending needs or the revenue-raising capacity of different parts of their country, and then calculate transfers to offset some or all of the differences. Scotland and the UK do not. Debates over risk focussed upon a narrow definition of ‘no detriment’ in terms of being no better or no worse off simply from replacing an element of funding for Scotland with taxes. But there was much less discussion of what might happen beyond day one.

Conclusion

The devolution of tax powers to the Scottish Parliament has been unprecedented. Both the SNP and Conservatives were enthusiastic supporters of this transfer. As we have argued, this largely stems from a focus on the *ad hoc* ‘accumulating competencies’ logic of devolution. From the SNP’s perspective, ‘more powers’ was consistent with its gradualist approach to independence. For that, they were willing to accept a transfer of risk. For the Conservatives, that tax risk was a missing piece in the jigsaw that would lead to better accountability and responsibility. What was less developed was how further fiscal powers could address specific public policy challenges.

The transfer of powers has enabled Holyrood to set different tax policies. This has been the reward of devolution. But, the cost has been that the Scottish budget for day-to-day devolved services is forecast to be squeezed relative to what it would otherwise have been, despite efforts to raise the tax burden on higher earners. This may turn around in the next couple of years, but the Scottish budget is now exposed to structural risks in the Scottish economy that have been years in the making and which will have an impact upon relative tax performance.

In time, the hope is that with tax powers, an informed and mature debate will emerge. But this has only been partially fulfilled so far. Disagreements over funding between Holyrood and Westminster have remained a source of tension. Moreover, by making the Scottish budget dependent, in part, upon the entire devolved tax base in Scotland, other arguments beyond devolved policy making—including UK government decisions on

¹⁴See D. Bell, D. Eiser and D. Phillips, ‘Adjusting Scotland’s block grant for new tax and welfare powers: assessing the options’, Institute for Fiscal Studies, London, 2015.

Brexit—have been used to explain (and defend) relative weaker performance.

There are positives from Scotland's experience of tax devolution, but the experience also suggests that politicians 'need to be careful what they wish for'. Demands for greater devolution can empower policy makers to 'do things differently'. But this needs to be set alongside an appreciation of what is an acceptable level of fiscal risk to transfer, the tools to manage such risk, and who should ultimately bear the burden of that risk.

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