Arguments for Full Fiscal Autonomy

Full fiscal autonomy would provide the maximum opportunity to apply the full range of tax policies in Scotland, including business taxes (like corporation tax), taxes on employment (like national insurance), environmental taxes (like the climate change levy) and taxes on consumption (like fuel duty).

1. Full Fiscal Autonomy would enhance the democratic and financial accountability of the Scottish Parliament and Government

- With full fiscal responsibility the Scottish Government would have administrative autonomy over the tax system. This would provide the Scottish Government with the opportunity to **ensure simplicity and transparency, and minimise administrative and compliance burden** – for example, by creating opportunities to put in place a simplified and more efficient collection regime.
- The Scottish Government would have the **potential to raise efficiency by providing a "hard budget" constraint** for devolved spending and revenues, as well as providing more opportunities to pursue innovative ways of funding existing services.
- Full devolution of tax would allow the Scottish Parliament to d**esign and vary all aspects of the design of an individual tax**. This is vital as the application of tax policy generally goes beyond simply adjusting the headline tax rate. For example, allowances against certain taxes (which result in changes to the tax base) can be used to incentivise activities and behaviours, such as research or development, capital investment, or taking on employees.
- It would provide an opportunity **to move away from a complex funding formula** to a more transparent system.

2. Full Fiscal Autonomy would enhance the Scottish Government's ability to capture the benefits of successful policy action

- Full fiscal responsibility would provide the Scottish Government with **greater ability to capture, and recycle, the benefits of successful policy approaches** - in the form of increased tax receipts and reduced welfare payments - providing the opportunity for the full fiscal benefits (or costs) of any major policy changes to accrue to the Scottish budget.
- Under models short of full fiscal autonomy the potential to create complexities in the application of policy levers is increased - for example, some of the benefits of successful policy will accrue to the Scottish Government, whilst some will accrue to the UK Government. This could decrease the effectiveness of, and reduce the incentives to change, policy.
- <u>This reflects the dynamic nature of the impact of tax changes, where, for example, changes in one tax will impact on the revenues from other taxes</u>. **Under the proposals which are short of full fiscal autonomy, many of these dynamic effects would accrue to the UK Government**, and would limit the Scottish Government's ability to capture (and therefore recycle) the full benefits associated with any policy change.
- **In the absence of the ability to fully capture, and recycle, the benefits of successful policy action, the incentive to use additional policy levers is <u>reduced</u>.**
- **The extent to which the Scottish Government has autonomy over the wider range of policy levers – such as welfare, and regulation – will also be a key determinant of the effectiveness and impact of changes in tax policy**. This reflects the interdependencies between tax policy and the wider use of economic policy.

3. The Scottish Government would have greater opportunity to balance risk and manage volatility in tax revenues

- Some tax revenues are more volatile than others. Full fiscal autonomy provides the opportunity to balance this risk and manage volatility in revenues by, for example, using more stable tax revenues (such as excise duties, where revenues would be assigned) to help partly mitigate volatility in other more cyclical tax revenues.
- The ability to effectively manage the volatility of certain revenues, and ensure stability in the public finances, will also require corresponding enhanced borrowing responsibilities.
- With full fiscal responsibility the Scottish Government would also have the opportunity to provide a stimulus to the economy – provided it is consistent with an overall coherent macroeconomic and fiscal position – to support the development of counter-cyclical policies. In particular, it would allow for specific responses to be introduced which reflects the unique conditions, and needs, of the Scottish economy.

4. Full Fiscal Autonomy would enable fiscal policies in and for Scotland to be set for specific Scottish circumstances and priorities, and would provide the opportunity to deliver a step change in growth performance

- Access to a coherent package of policy levers – as proposed in the model of maximum self-government – would allow the Scottish Government to deliver a step-change in Scotland's economic growth performance and to address long-standing inequalities through the creation of a genuinely bespoke set of complementary policies more aligned with Scotland's unique strengths and preferences (see table).

Taxation	Public Spending	Regulatory Levers	Institutions & Representation
Corporation Tax Income Tax National Insurance Oil & Gas Taxation Capital Gains Tax Tax Credits & Allowances Fuel Duty Air Passenger Duty VAT (assigned revenues) Crown Estates Excise Duties (assigned revenues)	Welfare Infrastructure Borrowing Procurement Education & Skills Employment Services Economic Development Transport (including rail) Health Housing	Competition Consumer Protection Industry Regulation (includes energy, telecoms, postal services & rail) Minimum Wage & Employment Legislation Energy Markets & Regulation Immigration (post-study work visa) Company Law & Insolvency Environmental Regulation Planning	Governance & Institutions Social Capital Administration Enhanced EU Representation International Trade Responsible Capitalism

- Scotland's performance since devolution – where successive Scottish administrations have helped to narrow an historic gap in performance with the UK across a range of indicators – highlights the potential for improvement that comes with the ability to tailor policies to local circumstances.
- Under the model of maximum self-government the Scottish Government would have greater autonomy to pursue approaches to increasing employment, productivity and the working age population – the key drivers of long-term growth performance.

- Previous Scottish Government analysis, presented in *Outlook for Scotland's Public Finances*, illustrated how "*by using the powers of independence to increase productivity by 0.3 percentage points per annum, boosting the working age population, and increasing the employment rate by just over 3 percentage points could generate additional tax revenues of £5 billion a year by 2029-30*."

- Although full fiscal autonomy would not provide access to the full range of policy levers available with independence, it could – when accompanied by a complementary and coherent package of wider economic levers – provide the Scottish Government with the opportunity to set an overall policy framework to generate long-term improvements in productivity, working age population and employment. Such improvements could generate additional tax revenues in future years. [**note** – *a key limitation of full fiscal autonomy, compared to independence, is that the Scottish Government would not have access to all elements of expenditure and would therefore be unable to adjust spending in areas such as defence to support growth enhancing initiatives*]

- For example, the Scottish Government would have the opportunity to:
    - **Transform childcare** in Scotland – boosting participation and providing greater employment opportunities for parents with young children;
    - Use **tax policy**, such as corporation tax, to encourage the rebalancing and reindustrialisation of the Scottish economy – e.g. through more effective capital allowances to encourage investment;
    - Use enhanced borrowing powers to **prioritise the timing and scope of investment** in Scotland's infrastructure boosting productivity across the economy;
    - Increase Innovation - by establishing an Innovation Agency to drive innovation growth and **using tax powers to encourage innovation and investment in research and development**;
    - Use **employer taxes** – such as National Insurance reliefs – to support employment and encourage more sectors/companies to recruit staff;
    - Use **Air Passenger Duty** to improve international connectivity and boost tourism;
    - **Directly represent Scotland's distinct economic interests and priorities** in the EU and in government to government relations with a formal role in determining UK priorities, policies and positions on reserved matters that affect Scottish interests;
    - Develop **a Population Strategy which attracts and retains overseas talent** – e.g. by reintroducing the **post-study work visa** - and encourages the creation of international business and innovation networks;
    - Put in place **competition and regulatory policies** that improve and streamline the consumer protection and regulatory regime to reduce duplication and promote consistency in the vital sectors of communication, energy, transport, and water;
    - Pursue a **more balanced approach to employment legislation** – compared to the lightly regulated UK model - that protects the rights of employees and focuses on good quality jobs; and
    - Pursue a **more coherent approach to welfare and employment**.