

Federalism: the best future for Scotland

The report of the Home Rule and Community Rule Commission
of the Scottish Liberal Democrats



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Preface by Willie Rennie MSP

Leader of the Scottish Liberal Democrats



I am delighted that the members of the Home Rule and Community Rule Commission led by Sir Menzies Campbell MP have published this report.

They were asked by our party, the Scottish Liberal Democrats, to set out the details of 'home rule' for Scotland within the United Kingdom where we would have control over most aspects of our domestic affairs but still enjoy the protection and strength that come from being part of the United Kingdom. They were asked to set out how home rule would work in the 21st century, taking account of the changes in the world since the 2008 financial crash and the changes across the UK since devolution started in 1999.

They have shown how home rule for Scotland could work well, but would be even better if it were part of a move towards a federal United Kingdom, where every part of the United Kingdom could have similar levels of responsibility.

The report sets out radical tax plans that would give the Scottish Parliament the powers to raise the greater part of the money it spends while confirming the advantages of social and fiscal equity across the United Kingdom. The proposals for control of taxes on income and wealth give powerful tools to address inequality in Scotland. The recommendations for partnership-working between different tiers of government will allow us to tackle issues such as poverty across the UK in a fully integrated way.

The Commission has set out a route map for home rule. Its aim is to build a consensus which can be endorsed at the 2015 general election. That plan mirrors the efforts we have made, with others, to enact the great reforms of the Scotland Acts of 1998 and 2012.

The Commission has extended its principles down to the level of local communities. There are radical recommendations for autonomy and power for local councils, together with greater opportunities for the smaller communities within councils to have the power to shape their own areas.

These proposals stop in their tracks the centralising tendency of governments.

This report will set Scotland on a liberal path, which gives power to the people of Scotland, at a national level and in their communities.

A handwritten signature in black ink that reads "Willie Rennie". The signature is written in a cursive, slightly slanted style.

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Introduction by Sir Menzies Campbell MP Chair of the Home Rule and Community Rule Commission



I have been a supporter of home rule and a Scottish Parliament all of my political life.

Home rule for Scotland within a reformed, federal United Kingdom has long been the constitutional aim of Liberals and Liberal Democrats.

Now, the constitutional debate in Scotland is arriving at an important staging post. The future shape of Scotland, and the very existence of the United Kingdom, are at stake in the forthcoming referendum.

It is time that the constitutional debate reached a settlement which will sustain our country in the unprecedented challenges of today and in the future. Our approach represents a robust view behind which most people in Scotland can gather, one that serves to unite, not divide us.

We have always believed that the constitutional future of Scotland requires a broad consensus if it is to attract the support and loyalty of the bulk of the people.

We offer our contribution in that spirit.

We do so by asserting our conviction that the four nations of the United Kingdom are best served by continuing a partnership which has served them well; by recognising that constitutional reform is necessary to ensure that the structures of the United Kingdom reflect the aspirations of its people and the demands of a modern democracy. To do so requires an approach which maintains the United Kingdom but allows its different parts the opportunity to make such decisions as they and their citizens require in relation to those issues which most directly affect their daily lives.

Our approach is federalism, a system of government used across the world which allows for the expression of different identities within one system, but combines with it the additional influence and strength which comes from co-operation and common purpose. We argue for a distribution of powers among the nations of the United Kingdom, for joint action where that is necessary and effective, and for parliaments and assemblies across the United Kingdom to have substantial democratic choice and opportunity combined with the responsibility that comes from significant financial powers.

We have set out in detail in our report how to proceed on the road to federalism. We shall not be content with ensuring a good outcome for Scotland – we regard it also as a first step

for the United Kingdom towards a modern constitutional future. Others may in sincerity wish no more than to redefine Scotland's relationships within these islands, but our ambition is necessarily greater.

It is now very clear that there are essentially two options: the breakup of the United Kingdom into its constituent units, or a modernised, federal United Kingdom.

Home rule within a federal United Kingdom is the best way forward for Scotland and for Britain.

For us the need for reform does not stop at Holyrood; it is also clear that the approach of the current SNP Government which argues for independence is actually a highly centralised one, replacing Westminster with Holyrood. It is destructive of local democracy, and contrary to Liberal Democrat values. The view of other parties may be that the debate is entirely about the balance of power between Westminster and Holyrood. Our view is that it should be about real empowerment of the people and communities across Scotland.

Building on the work of the Steel Commission on *Moving to Federalism* we have set out our vision of what a home rule Scotland would look like, and what the implications are likely to be for a United Kingdom reformed on a federal basis. We invite other parties, organisations and individuals across Scotland to consider our views and engage in principled debate. We are conscious that the constitutional structures of our country should be built on the broadest possible consensus if they are to endure and be sustainable.

The ideas and structure we have laid out are unlikely to be achieved in one leap. Our priority is to secure and entrench a broader home rule settlement for Scotland, but there can be no doubt that this would benefit from major change at Westminster too. Over time, we are confident that the constitutional debate in England, currently under-developed, will progress and reach a conclusion – but time will be required for that debate. We expect that Scotland will contribute to the terms of that debate, at least by example, but it is for people in England to determine how they wish their own national and regional identities expressed within the constitutional structures of our United Kingdom.

The Liberal Democrats and their predecessors have long argued for federalism, which is not only compatible with home rule but should be its ultimate destination.

We make our report to the autumn 2012 Conference of the Scottish Liberal Democrats. If the recommendations are adopted by the party both in Scotland and in the United Kingdom the principles will form part of the Liberal Democrat manifesto to be put to the electorate across Britain in the General Election of 2015. In that election we will seek a mandate for the approval of Scotland acquiring full home rule status.

We will also set out to persuade people across the UK that a federal structure will serve them best, wherever they live.

A useful contemporary illustration of the benefits of a United Kingdom which is of particular interest to me can be found in the remarkable success of Team GB in the London Olympics and Paralympics. The unity of support from the whole of the UK underpinned these successes and was the focus of the celebrations which followed them.

We set out our views in this report with confidence and a firm belief that our proposals are in the best interests of all of the citizens of the United Kingdom.

Scotland will thrive with the fiscal responsibility and authority that comes with home rule, but that home rule settlement can only be stable if it forms part of the move to a truly federal United Kingdom. We shall promote home rule and federalism at every opportunity.

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Executive Summary

The Home Rule and Community Rule Commission was tasked with setting out proposals to bring about substantial and stable home rule powers for Scotland. This report does that, and shows how these powers and responsibilities would be best achieved by a move to a federal system across the whole of the United Kingdom.

This report builds on the understanding developed by the Steel Commission report and from a century of Liberal and Liberal Democrat campaigning for home rule.

Liberal Democrats work to make sure that individuals and communities get the freedoms to control the circumstances of their own lives for the benefit of themselves, their families and their communities. That is one of the principles of subsidiarity.

Chapter 1 sets out both the background and a forward vision of a strong Scotland within the United Kingdom, making decisions on domestic matters but as part of the United Kingdom family able to exert a positive and influential voice in the world.

Chapter 2 describes how a federal United Kingdom would look and sets out some of the opportunities there would be for joint action, suggesting that the different governments should work together in a more structured way to tackle the great challenges of ‘squalor, ignorance, want, idleness and disease’ identified sixty years ago by that great Liberal, William Beveridge,.

Chapter 3 sets out a radical allocation of tax and borrowing powers to equip the Scottish Parliament with powerful economic levers and fiscal responsibilities.

Chapter 4 takes the principles of subsidiarity and applies them to enhance the status of local government and the powers available to local communities.

A strong, positive future for Scotland

The first recommendation states: ‘The Scottish Liberal Democrats should reassert that they are federalists, in favour of home rule for Scotland within a reformed, federal UK.’

The report explains why this is a stable solution that would be good for Scotland and good for the United Kingdom as a whole.

The report sets out how a federal solution will allow different domestic policies to be pursued in different parts of the United Kingdom but also how it will build on the

continuing strength of joint action at a United Kingdom level as partners in a federal union.

The Commission recommends a route map to a federal future for the United Kingdom:

- It is clear that other parts of the United Kingdom may wish to move at different speeds, to allow time for the debate about arrangements in England, Northern Ireland and Wales to take place there. The move to home rule status for Scotland, in which it enjoys a federal relationship with the rest of the United Kingdom, is a first stage that can proceed ahead of the rest.
- If the result of the 2014 referendum rejects independence, it will secure Scotland's place in the United Kingdom and, consequently, open the door to significant constitutional change across the United Kingdom.
- Consent for change within and across the United Kingdom should properly be secured at the 2015 Westminster general election.

The shape of a federal United Kingdom

The report sets out how federalism would work in practice.

- Formalised partnership-working, a model of cooperative governmental action first suggested in the Steel Commission report. This would require a new federal government to consult with the other legislatures across the United Kingdom on policies that would impact on their statutory responsibilities, and vice versa.
- A new, innovative 'power of initiation', enabling one government to request formally that another take specific necessary action to facilitate policy objectives in an area where the other government has the policy lead.
- Reform to certain United Kingdom-wide institutions such as Her Majesty's Revenue and Customs in recognition of the fact that they will be expected to serve all parliaments and jurisdictions within the United Kingdom.

Fiscal federalism – powers and responsibility

Setting out for the first time how fiscal federalism will support a move to a federal solution for the United Kingdom, the Commission recommends that the Scottish

Parliament be allocated tax levers enabling it to raise the greater part of its own spending.

- Powers over income tax, bands and rates.
- Powers over inheritance tax and capital gains tax. Combined with income tax and existing powers over stamp duty the Scottish Parliament would have control over substantial tax levers on income and wealth.
- Control by the Scottish Parliament of the aggregates levy and air passenger duty to broaden the powers on the environment and transport that the Scottish Parliament already exercises.

The importance of retaining the single United Kingdom market and unified systems to help business is promoted throughout these recommendations.

- Laws and regulations affecting companies and employment kept at a UK-wide level.
- An additional power for the Scottish Government to highlight specific intra-Scotland competition matters to the United Kingdom competition authorities.
- The proceeds of corporation tax to be assigned to the Scottish Parliament to give it a stake in the fruits of improved economic performance.

Fiscal federalism would be assisted by a new needs-based payment system, to be agreed by the federal United Kingdom Government, the Scottish Parliament and the relevant assemblies to ensure fiscal equity across the UK. The report accepts that the Barnett Formula would continue to operate until a new formula is agreed.

New borrowing powers would allow the Scottish Government to balance the economic cycle and take long-term decisions on investment.

The Commission highlights the importance of the single regime for North Sea oil and gas extraction for the global industry and retains this regime at a United Kingdom level but encourages the establishment of an oil fund, when fiscal conditions improve, for investment across the UK.

The Commission also endorses the retention of a single United Kingdom welfare and pensions system, supporting free movement and residency across the United Kingdom with a common set of living standards and entitlements. The general proposals for partnership-working are enhanced through the idea of a strategic review of welfare provision involving all governments, and by recommending that the Scottish

Government acts as an agent for the United Kingdom Government for much of the work of JobCentre Plus and the Work Programme.

Further recommendations promote partnership-working within a federal United Kingdom on matters such as Europe, and provide for powers for the Scottish Parliament to determine its own electoral system.

Empowering communities

The Commission strengthens its recommendations on the decentralisation of power by proposing extensive autonomy for local government and for local communities.

- Financial freedoms for local authorities;
- Removal of the powers of ministers to overrule local authorities;
- Powers over council tax and business rates handed back to local authorities;
- A general power of competence for local government, allowing councils to set their own plans, reflecting the priorities of their electorates.

These changes would result in local authorities being able to raise roughly half of the money that they spend with a system of grant funding for the remainder to ensure equity across Scotland.

The Commission goes further in recommending new rights for local communities to take over services in their areas and to require the co-operation of councils, national government and quangos to do so. The recommendations also offer the opportunity to local communities to establish new burgh councils or other mechanisms if they want to put in place clear local control of services.

The final recommendation entrenches local government as envisaged by the original constitutional convention.

CHAPTER 1:

A hundred years supporting home rule

1. Where should power reside? How is power shared? How are the institutions of government best shaped to deal with the huge challenges of a complex world? How can we best make sure that individuals and communities get the freedoms to control the circumstances of their own lives for the benefit of themselves, their families and their communities?
2. These are questions that have occupied the minds of Scottish Liberal Democrats and Scottish Liberals for generations.
3. Liberals and Liberal Democrats, almost uniquely amongst the major political parties, have stood up for individual and community power and distrusted the alleged wisdom of distant authority – the ‘man from the ministry’.
4. Over recent generations the United Kingdom has become one of the most centralised countries in the world.
5. Since 1997 the creation of parliaments and assemblies in Scotland, Wales, Northern Ireland and London has meant major progress on decentralisation, but the United Kingdom still remains a deeply centralised state.
6. A Scottish Parliament now controls most domestic functions in Scotland. Even so, there is still a government drive to create bigger authorities over which ministers are better able to exert control, rather than open up opportunities for smaller communities to bring creativity, innovation and efficiency to the public realm in their neighbourhood.
7. Scottish Liberal Democrats have for a hundred years supported ‘home rule’ for Scotland but accept that it needs to be re-defined for the 21st century.
8. Since the early 1970s there has been a growing sense that our political institutions were no longer up to the job, that the changing sense of personal and national identity in Scotland required a modern political framework in which to flourish.
9. The campaign grew during the 1980s and the establishment of the Scottish Parliament in 1999 went some way to meet the need identified 30 years ago.

10. But Liberal Democrats always recognised that devolution would only ever be a halfway house to a more permanent modern constitutional framework.

A strong, positive future for Scotland

11. The Scottish Parliament and the devolved assemblies have changed the UK constitutional picture permanently.
12. The key question that faces our nation is whether Scotland should remain part of the United Kingdom. This question must be resolved so that the people of Scotland can focus on the challenges that face our society, whether economic, social or environmental.
13. Scotland benefits from being part of the UK and the UK benefits from having Scotland within it. For over 300 years, the United Kingdom has brought people together in a successful multi-national state.
14. The United Kingdom is one of the biggest economies in the world and our combined strength has helped us to weather the recent economic turmoil. As part of the United Kingdom, Scotland itself is better protected from economic shocks. The United Kingdom enabled the creation and funding of the NHS and the pensions and benefits system; this enables Scots to move throughout the United Kingdom to live, work and retire without worrying about the availability of social protection. In cultural terms Scotland is part of a complex web, including institutions such as the BBC and shared interests in sport, that binds all parts of the United Kingdom together in a way that would not be possible if Scotland were separated.
15. As internationalists we believe that, as part of the UK, Scotland benefits from a prominent role on the world stage: represented at a permanent seat on the UN Security Council; part of one of the leading members of the European Union, G8 and NATO; reserved positions on the International Monetary Fund and World Bank. Through the UK, Scotland is able to have meaningful impact on issues as diverse as climate change, the fight for international justice, the operation of the global trading system and arms control. Scotland's voice is louder through the UK than it would be alone: we have the weight to argue our case and fight for a fair deal for ourselves and others. Even in non-political international organisations, such as those concerned with sport, science or culture, the combined weight of the United Kingdom will always be greater than the sum of its parts.

16. The Steel Commission set out the case for the UK. It said:

'The United Kingdom has been one of the great success stories of the world.

The United Kingdom as a whole has a greater punch internationally than any of its constituent parts separately;

The United Kingdom as a whole has financial resources that can be directed to areas of need across Britain;

The ability of the United Kingdom to make common provision across the UK for pensions and social security benefits acts as an automatic support for those in greatest need, bringing the resources of the Union to bear in a way which supports areas of greatest economic and social need.'

17. A new constitutional settlement should reflect a modern purpose, meaning and aspiration for the United Kingdom. It should be built on an inclusive basis commanding wide and continuing support from its people – something which neither a narrow unionism nor a restricting separatism can do. It must, above all, reflect national and individual identities in a way which people are happy with.
18. The purpose of the reformed United Kingdom should be to provide a strong and sustainable basis on which to tackle the unprecedented challenges of our age, empowering local communities, supporting a sense of place in an increasingly mobile and fractured world.
19. Scotland is not and should not be merely another small state on the periphery of Europe, lacking influence in the world. As part of the United Kingdom, Scotland has played a major part in the world. A federal partnership between Scotland and the rest of United Kingdom will further stimulate innovation and energy and be a robust basis on which to deal with the problems of our age.
20. The new settlement has, at its heart, a vision of Scotland's place in the world, of citizens and communities having greater control over their own life circumstances and over the increasingly powerful forces which influence them. The need for effective mechanisms to counterbalance enormous global forces is surely the biggest lesson of the recent banking crisis.

The case for federalism

21. The United Kingdom has a value for Scotland. And Scotland has a value to the United Kingdom. Scotland can and should get the best of both worlds: strong domestic powers, working in partnership with the other parts of the UK, yet punching above its weight on the world stage.
22. In 2006 the Steel Commission set out how a federal solution could accommodate the multiple identities of people who live in the United Kingdom – simultaneously Scottish and British, never forced to choose between them. It allows all people in the United Kingdom to share the risks and rewards in an uncertain world.
23. Across the world federalism is a system of government where power is exercised by central federal governments and parliaments alongside state or provincial governments and parliaments. Together they form the component parts of the federal union. The people of Australia, Brazil, Canada, Germany, Switzerland and the United States of America would not consider the idea of federalism to be unusual, radical or difficult. Federalism is a normal way of running complex countries.
24. In a federal union the federal bodies and the state bodies have equality of standing and each has powers that are theirs and theirs alone. It is this balance at the heart of a federal constitution that gives a federal system the stability and flexibility that would be of such value to the whole United Kingdom.
25. This Commission believes that the best future for Scotland can best be achieved within such a federal structure for the United Kingdom. A federal future for the United Kingdom would enable the people of England, Wales and Northern Ireland also to become responsible for many of their own affairs to the extent proposed for Scotland, even if they move towards them at a different pace. Federalism is 'home rule all round' rather than just home rule for Scotland.
26. Across these islands there are signs that there is more support for a federal solution for the UK than ever before. Federalism goes with the grain of what people instinctively want for their country and reflects more satisfactorily than other constitutional options the multiple identities described so eloquently in the report of the Steel Commission.
27. A federal system for the United Kingdom has five main advantages:

- It gives real democratic choice to the voters of each of the four jurisdictions to decide, within a broad fiscal pact, the nature and extent of public services and how they are delivered. This is particularly important to the people of Scotland at present, but pressure is growing in Wales and Northern Ireland for the greater autonomy of action that would flow from home rule in a federal system.
 - It retains the many advantages of the United Kingdom: in fiscal terms; in its single market in capital, labour, enterprise and services; in the operation of some public services at a federal level; and at an international level.
 - It retains the ability to deploy the resources of the whole of the United Kingdom to tackle poverty, not least through a UK-wide system of pensions and benefits.
 - Unlike the current devolution arrangements, or the centralised system in place before 1999, a federal system would be a permanent and stable solution. It would stand the test of time and contains natural checks and balances that are missing from the UK's current constitutional arrangements.
 - It solves the West Lothian Question by creating a system that allows local public policy choices in each jurisdiction to be made autonomously by those elected in that jurisdiction. This remains a major concern amongst English MPs and one that must be addressed in the interest of the stability of the United Kingdom as a whole.
28. Even nationalists now accept that an independent Scotland would still rely on the rest of the UK for many things. One of the strengths of federalism over independence is that it gives the people of Scotland an equal and continuing voice in UK decisions, whereas independence removes the Scottish voice from the UK and from influence over these key decisions. A separate Scotland would have no say over the Bank of England or the financial services authorities and no ability to help shape the fiscal arrangements supporting Sterling. An independent Scotland would also have to accept immigration rules laid down for the rest of the United Kingdom if it wished to retain a common travel area with England, Wales, Northern Ireland and the Republic of Ireland. By contrast, under home rule, people in Scotland would continue to have an effective say over these matters as part of a federal United Kingdom.
29. With a federal United Kingdom, the constituent parts would have power to make laws and have responsible governments as they see fit on 'home rule

matters', that is domestic matters that have been agreed not to be retained at a federal (whole UK) level.

30. A United Kingdom Parliament would be elected by voters across the UK and the UK Government would represent our country internationally and deal with what are presently termed 'reserved matters' but which would become 'federal matters'. In a federal system, the United Kingdom Parliament would be unable to legislate for areas within the competencies of the home rule legislatures – of which the Scottish Parliament would be the first. That clear division of power and responsibilities between the federal and home rule layers of government is an important feature and advantage of a federal system.

Federalism is best for Scotland

31. People in Scotland expect the Scottish Parliament to control and fund most of Scotland's domestic concerns, and deliver most of the services which affect their day-to-day lives, whilst sharing the risks, rewards and protections, and the greater clout that comes from membership of the family of communities and nations which make up the United Kingdom.
32. More devolution alone will not do the job. More devolution will not be the stable long-term solution that our country needs. Constant fiddling with the balance of power and responsibilities does not bring stability.
33. The best solution for Scotland is to combine the existing wide-ranging policy and legislative responsibilities of the Scottish Parliament with substantial revenue-raising powers, all set within the structure of a reformed United Kingdom where the home rule powers are respected and entrenched. That solution is a federal United Kingdom.
34. At their conference in October 2011 the Scottish Liberal Democrats asked this Commission to look at 'home rule' in the context of Scotland. We have concluded that this is best delivered by what Liberals at the start of the 20th century called 'home rule all round'. Today that means a modern federal United Kingdom.
35. The time has come to reassert that Scottish Liberal Democrats are federalists. We are for home rule, within a strong and federal United Kingdom.

Recommendation 1: the Scottish Liberal Democrats should reassert that they are federalists: in favour of home rule, within a strong and federal United Kingdom.

The route map to change

36. Scottish Liberal Democrats state in the party's constitution that:

'sovereignty rests with the people and ... authority in a democracy derives from them.'

37. The key principle from the Scottish Constitutional Convention is the right of the Scottish people to self-determination – a right enshrined in the United Nations Charter and in the International Covenant on Civil and Political Rights. Accordingly it is a matter of fundamental, liberal principle that the Scottish people can decide to remain in or withdraw from the United Kingdom.
38. However, the United Kingdom is a union of nations and the people of Scotland cannot change the terms of that union alone. Scotland cannot unilaterally impose federalism on the rest of the UK. Reform of the United Kingdom also requires the consent and co-operation of the people of England, Wales and Northern Ireland.
39. For that reason voters were asked through party manifestos across the UK in the 1997 General Election if they backed devolution to Scotland. They did so, and this was implemented in the Scotland Act 1998. More recently the Calman Commission's proposals for greater financial powers for the Scottish Parliament were backed by voters across the UK in the 2010 General Election and implemented in the Scotland Act 2012.
40. The idea of Scots voting alone and unilaterally to change the nature of the union is a constitutional nonsense.
41. This Commission makes its report to the autumn 2012 conference of the Scottish Liberal Democrats. If the recommendations are adopted by the party there, and at a federal level, its principles will form part of the Liberal Democrat manifesto to be put to the electorate across Britain in the general election of 2015. That will seek a mandate approving of Scotland acquiring full home rule status, and will hope to persuade people across the UK that a more federal structure will serve them best, whichever part of the country they live in.

Recommendation 2: the proposals for home rule for Scotland and federalism across the UK should be included in the Liberal Democrat manifesto across the UK at the 2015 general election.

The referendum opens the door to change

42. If the referendum on Scotland's future due in 2014 reinforces the commitment of people in Scotland to the United Kingdom then it will open the door to change across the whole of the UK. Scotland will have sent a powerful message that we see our future as a continuing partner in the United Kingdom – but a United Kingdom remade for our age, which treats its constituent parts equitably.
43. A rejection of independence will enable Scotland to continue down the track towards a modern, pluralist and federal relationship with the other parts of the United Kingdom.
44. The 2015 UK general election would be a good way for political parties across the UK to gain endorsement of changes to take place across the whole UK.
45. People in Scotland have twice in the past fifteen years given support to UK political parties that have backed proposals created in Scotland for greater powers for Scotland and seen those proposals implemented. The 2015 general election six months after the 2014 referendum is the right time for the people of the United Kingdom to make a decision about the future of the United Kingdom.

Recommendation 3: Liberal Democrats across the United Kingdom should seek a political mandate for a 'route map' to a federal constitution at the 2015 General Election.

CHAPTER 2:

The shape of a federal United Kingdom

46. A commission established by the Scottish Liberal Democrats to make recommendations for Scottish matters cannot tell the people of Wales, Northern Ireland or England how to manage their affairs. Nevertheless, it is entirely appropriate for Scotland and Scottish politicians to propose reforms which will put the United Kingdom on track to become a federal union. While further devolution for Scotland alone may have advantages, the persistence of an asymmetrical constitution across the United Kingdom is likely to be unsatisfactory and unstable in the longer term.
47. The biggest hurdle in moving to a federal solution for the UK is the position of England and the lack of appetite, until recently, to discuss and decide how matters of purely English concern should be dealt with. The commission established at Westminster to consider the West Lothian Question may help focus the debate, but English civic society needs to engage with this issue and to come together to debate how electors in England can hold to account those who plan and deliver the public services upon which they rely.
48. Scotland can be expected to contribute to the terms of that debate, but, in essence, it is for England and the people of England to determine how they wish their own national, city, county and regional identities to be expressed and the extent to which that process should be separate from the institutions of the whole United Kingdom.
49. The Commission supports the work of the new federal Liberal Democrat working group on political and constitutional reform, whose remit includes examination of the future status of England and of decentralisation within England, as well as the implications for UK governance of the devolution settlement. This work will inform the party manifesto for the 2015 elections.

Recommendation 4: Political parties and civic society should progress debate on proposals for a reformed UK constitution, including how purely English matters should be determined.

Practicalities of the move to federalism

50. The proposals for home rule all round and federalism do not have to be achieved in one leap. The priority is to secure and entrench a broader home rule settlement for Scotland and this could be delivered independently of a wider move towards federalism. But this would best be accompanied by major change at Westminster that would deliver the longer-term goal of a federal settlement for the United Kingdom.
51. The Scotland Act 2012 contains a programme of incremental change in the taxation and fiscal powers of the Scottish Parliament. Some of these changes have already taken effect. Significant increased powers over taxation will take effect between now and 2016. This Commission proposes the allocation of additional taxation powers to the Scottish Parliament as part of the move towards home rule. The Commission envisages that an electoral mandate for home rule in 2015 will enable a smooth completion of the home rule project for Scotland in the next Westminster Parliament. If there is a similar mandate for home rule in Wales, then the dynamic for change will be wider and, if English politicians and civil society can agree on reform in England, the move towards federalism would be unstoppable.
52. The practical reforms proposed in this report can work for Scotland alone but will be for the greater good of all parts of the United Kingdom.
53. Under a federal structure people living in each part of the UK would elect representatives to the UK Parliament, in addition to their own domestic parliament or assembly dealing with home rule matters.
54. A federal United Kingdom Government would retain major areas of competency – foreign and defence affairs, the currency, national emergency, immigration, trade and competition, pensions and welfare, macro-economic policy and the preservation of the UK single market for business, as described later in this report.
55. It is important to consider how the federal government and Westminster Parliament would operate in their relations with the Scottish Government and the Scottish Parliament and other legislatures.
56. Home rule should be one of the guiding principles at the heart of the federal government. The complementary powers of the federal and state governments

should be recognised. All governmental organs should respect the spirit and the letter of the constitutional settlement.

Recommendation 5: The concept of mutual respect, already endorsed as the principle governing relationships between the UK and Scottish governments, should be incorporated as a constitutional obligation on federal and state governments to respect and support each other's role.

57. A number of specific federal institutions should have a special status under the constitution. These include Her Majesty's Revenue and Customs, the home civil service, HM Treasury and its associated agencies, the competition authorities, the research councils and the Post Office. Some will have a role more independent of government, some will serve government at various levels, some will have a wide national significance across the UK. Other bodies, such as the Office of National Statistics, will have to improve the quality of the information they provide to serve the new structure.

Recommendation 6: The status and functions of certain UK-wide institutions – notably Her Majesty's Revenue and Customs – should be given a protected and more independent constitutional position in recognition of the fact that they will be expected to serve all parliaments and jurisdictions within the UK.

58. There will come a point when it will be possible to declare that the United Kingdom is a federal union. It would be natural to follow that declaration by a process to produce a comprehensive written constitution for a federal United Kingdom, as is normal across the world.
59. Until that time, the reform of the United Kingdom remains 'work in progress' and Scotland will require a strong voice in the House of Commons and the UK Government to ensure that reform continues in a way advantageous to Scotland and in accordance with the principles of home rule and subsidiarity required.

Recommendation 7: the present level of Scottish representation at Westminster should be retained until a federal structure for the UK has been delivered.

60. In a federal United Kingdom the powers and responsibilities of each domestic jurisdiction and of the federal government and parliament would be clear and complementary. At that point there could be a strong case for the Scotland Office to be absorbed into a department for constitutional affairs responsible for all nations and regions.

Recommendation 8: The role of the Scotland Office should be reviewed as the United Kingdom moves towards a federal union. Until the move to a federal state is well underway the Scotland Office should remain as Scotland will need the safeguard of a Secretary of State in Cabinet to look after its interests during the transition.

Partnership-working

61. Under federalism the home rule governments across the UK would normally work on matters of their own responsibilities. But the strength of a federal union is that they could also come together to agree action on matters of combined interest.
62. For Scotland, in some areas of government, a policy function allocated to either the UK or the Scottish Government might have significant impact on legitimate functions within the remit of the other government. Manifestly such a policy area requires a joined-up approach by the two governments in the public interest and this is best done as part of a federal system. The Steel Commission devised the idea that there should be a requirement for 'partnership-working' between different levels of government in such matters.
63. The Steel Commission suggested the need to move beyond non-statutory concordats to a statutory basis for defined partnership-working. This might, it was suggested, include a legal requirement to consult the Scottish Government and Parliament before going beyond specific legislative changes, allowing appropriate timing mechanisms and giving more weight to the dispute resolution process.
64. The underlying rationale was that such formalised mechanisms would give Scotland a statutory underpinning in its discussions with UK ministers in relevant areas. It would strengthen current practice and put it on a statutory and codified basis.
65. Around the world, this is normal practice in federal systems. The German Basic Law provides for specific forms of co-operation between the federal government and the Länder (states) which has led, for example, to the Joint Science Conference and collaboration on research and innovation. Canada has bilateral Labour Market Development Agreements with the provinces and other arrangements to support skills and employment.

66. In Australia, the Commonwealth Government and the state and territory governments agreed a National Reform Agenda to improve productivity and promote future economic growth.
67. The Commission believes that partnership-working between the UK, Scottish and other home rule governments should build on such models, which would prove far more beneficial to Scotland than political stand-off between governments or the simplistic view that policy areas where these situations arise should simply be transferred to the Scottish Parliament.

Recommendation 9: Some functions of government should constitute a third category – additional to ‘reserved’ and ‘devolved’ powers – namely ‘partnership powers’, which require the co-operation of both home rule and federal governments.

68. Areas of partnership powers would include skills and employment, research and innovation, strategic planning of welfare services, energy resources, election law and administration, marine policy and cross-border transport. Such policy areas might be legitimately and properly within the policy lead allocated to one tier of government but impact to a substantial degree on the work of the other tier.

Recommendation 10: In addition to a general constitutional obligation of mutual respect, policy functions in areas of ‘partnership powers’ should impose a legal duty on one government – more normally the federal government – to consult the other government on a partnership basis.

69. For example, changes proposed by the UK Government in housing benefit would require a process of formal consultation with the Scottish Government.
70. There is a case for giving each government a ‘power of initiation’. This would let it develop a proposal within its own sphere of competence and confer the right to ask the other government for support (within its competence) to implement it where this would bring benefits. The other government would have a duty to consider and facilitate such support, if it was reasonable to do so.

Recommendation 11: Each tier of government should have a formal ‘power of initiation’, enabling it to request the other tier to take some specific action to facilitate policy objectives in an area where the other government has the policy lead.

71. For example, such a power might be relevant if the Scottish Government wished to change the system of local government finance, which is within its jurisdiction to do but requires consequential changes in benefits or in tax collection arrangements which are currently reserved to Westminster.

72. The duty of consultation and the power of initiation should carry a broad presumption that reasonable and legitimate requests by one government for action by the other in areas of partnership-working will be addressed and that if one government wishes to invite another government to introduce a new policy or service it should be prepared to make available funding for it.
73. The need for oversight of areas of partnership-working can be met by formal arrangements to allow joint committees of Scottish and Westminster parliamentarians to scrutinise the work of both UK and Scottish governments and report to both parliaments.
74. Considerable collaboration between the Scottish and UK governments is already required in financial areas as a result of the reforms of the Scotland Act 2012 which set up the Joint Exchequer Committee. This is leading to the development of embryonic procedures and golden rules on such matters as the limits on borrowing powers and the development of new taxes. The role of the Joint Exchequer Committee should be influential and develop over time. These are necessary mechanisms to the effective functioning of quasi-federal arrangements. The logical way forward is to entrench them in a basis of greater equality between the UK and Scottish governments.
75. A further aspect of partnership-working might be where the Scottish Government acts as an agent for Westminster on specific projects. For example, it might make sense for a particular Department for Work and Pensions programme on welfare to be run by the Scottish Government, utilising its local agencies and services to make it more effective.
76. Addressing issues of poverty, lack of opportunity, inequality and deprivation are increasingly central to the operation of government and to building a fairer and more liberal society. They are important objectives for all levels of government, and require the full resources of government as well as close partnership with civil society partners such as the Big Lottery and the voluntary sector to make the necessary impact for success.
77. One way to approach this issue is to consider the issue of strategic planning of welfare services. Both the Scottish Constitutional Convention and the Steel Commission believed that the Scottish Government should have a role in this.

Recommendation 12: The strategic planning of welfare services should be considered for joint working combined with a constitutional duty to tackle poverty through efforts at every level of government.

Dispute resolution

78. Inevitably there will be disagreements between the UK federal government and the Scottish Government about specific issues. One of the advantages of the United Kingdom is the ability of ministers and civil servants at UK and other levels to have regular and informal contact on a variety of day-to-day issues. These smooth the workings of, and understanding of, each other's role.
79. The two governments consult and work together in a variety of ways on many functions, mostly without attracting publicity. Smooth working on such matters is a distinct advantage of a home rule arrangement and should be retained and encouraged. However, there will be issues where difficulties and disagreements arise.
80. The existence of effective working concordats on how inter-governmental relations are conducted can be of great assistance in avoiding areas of difficulty, or resolving them if they arise. Most inter-governmental disputes are resolvable by agreement, even where different political parties are in power but some, by their nature, are more intractable.
81. Under a federal settlement, where governments are obliged to consult other governments or respond to 'powers of initiation', a formal dispute resolution mechanism will be required.
82. The UK Supreme Court already has a role in dealing with devolution issues under the acts setting up the Scottish Parliament and National Assembly for Wales, although only one dispute between the UK Government and a devolved government has actually been taken to the Supreme Court.

Recommendation 13: The Supreme Court should exercise jurisdiction in relation to dispute resolution, whilst maintaining that it is not the role of the court to determine substantive political disputes.

Entrenchment and a written constitution

83. A new federal relationship for the future between the different parts of the United Kingdom amounts to nothing less than a remodelling of the United Kingdom for the modern age. A new set of constitutional arrangements would replace the treaties of union between England and Scotland, and between Great Britain and what has become Northern Ireland.

84. Nevertheless, the Commission recognises that constitutional change in this country tends to be incremental and untidy rather than revolutionary. This is a strength, as new arrangements build on the practice and successes of the past.
85. The new relationship might be presaged by a 'Declaration of Federal Union' which would be more significant than drafting a federal constitution – not least because political institutions for England will need time and space to develop. The prestige of the federal constitution would be enhanced by a document that spoke eloquently of the purposes and principles of the United Kingdom, which was timeless and well-expressed and which would be seen as inspirational.
86. The declaration could go as far as to impose a duty on government at all levels to work for the elimination of poverty and of Beveridge's other 'giants' – squalor, ignorance, want, idleness and disease. It would be a modern British equivalent to the American Declaration of Independence or the French Declaration of the Rights of Man – or indeed of our own Declaration of Arbroath or Magna Carta.
87. The declaration would include a provision to end the power of the Westminster Parliament to legislate in areas of home rule competence without the consent of the relevant home rule legislature, embodying the principles of the Sewel Convention.
88. Home rule all round or federalism must be politically and legally entrenched. This remains a difficult concept for British constitutional theory, but this Commission believes that the Declaration of a Federal Union would go a long way to make progress to a federal system irreversible.
89. It is likely, however, that the initial priority would be to further entrench the home rule Scottish Parliament. This, to a large extent, has been done to date by adherence to the Sewel Convention, which itself has robustly demonstrated its current strength during the passage of the Scotland Act 2012. Entrenchment could be enhanced by a formal declaration by the UK Parliament to the same effect as the declaration proposed for the whole UK above.

Recommendation 14: The UK Parliament should commit to a declaration that entrenches home rule and the Scottish Parliament in advance of a full federal settlement.

CHAPTER 3:

Fiscal federalism

90. Fiscal federalism was the term used by the Steel Commission to describe the financial underpinning of the move to a more federal UK. It concluded that it was the logical accompaniment to a federal system:

‘Fiscal federalism is the financial underpinning of the move to a more federal United Kingdom.

Such a system will be a practical, stable and adaptable foundation for Scotland’s reformed relationships within the United Kingdom.’

91. Fiscal federalism is a way of describing the equitable allocation of fiscal responsibilities and powers to different tiers of government across the United Kingdom.
92. The Steel Commission recognised that such a system retains the ability of the United Kingdom as a whole to support equity across the UK, both at a governmental level and at an individual level.

‘Fiscal equity is a crucial principle in any federal system. Academics are clear that no industrialised countries have opted for full fiscal autonomy. The reason for this is clear: to do so strikes against the principle of unity within states that sees an element of redistribution between areas with different levels of income and wealth.

‘All federal states include some form of intergovernmental transfers. It forms part of the social pact and in many cases the written legal constitution that binds the constituent parts of the state together. It recognises the benefits to all of the federal union and the need for solidarity.’

93. And the Steel Commission expanded on this in its case for the UK:

‘The ability of the United Kingdom Government to make common provision across the UK for pensions and social security benefits acts as an automatic support for those in greatest need, bringing

the resources of the union to bear in a way which supports areas of greatest economic and social need.'

94. The Home Rule and Community Rule Commission makes recommendations on the allocation of tax powers and responsibilities to different tiers of government, the retention of a balancing payment system across the UK for social equity and a UK-wide system of social protection.
95. The Commission also looks at the importance of the UK single market, for the benefit of Scottish business and economic success.
96. The Commission has examined effective ways to achieve an equitable fiscal relationship between the various parts of the United Kingdom. Since the Steel Commission published its report, the Scotland Act 2012 has substantially changed the fiscal relationship, allocating powers over a share of income tax and other taxes to the Scottish Parliament. As a nation we are now substantially more aware of the importance of fiscal prudence and the need to manage the nation's deficit.
97. This process should be built on to allow the Scottish Parliament to raise the majority of its resources by taxes it levies itself. This better balance will equip the Scottish Parliament – and other jurisdictions within a federal UK in due course – with a set of responsibilities that match federal systems across the world and yet retain the ability of the UK Government to act in support of social equity.

Taxes on income and wealth

Recommendation 15: Income tax paid by Scottish taxpayers should be almost entirely the responsibility of the Scottish Parliament.

98. The Commission considered the provisions of the Scotland Act 2012 in the light of concern from the Steel Commission that:

'often tax sharing can be confusing'.

99. There is a strong case to retain an integrated United Kingdom income tax system operated by Her Majesty's Revenue and Customs to support the UK single market in capital and labour. But, building on the provisions of the Scotland Act 2012, it is now sensible for the income tax paid by Scottish taxpayers to be the responsibility of the Scottish Parliament.

100. In order to retain a single administrative system for income tax across the United Kingdom – even if the rates of tax differ in different jurisdictions – the system of allowances and reliefs that an individual is allowed to make against income tax should be the same across the UK. The same provisions should operate for self-employed persons as for those on PAYE.
101. The biggest allowable deduction is for pension contributions. The Commission supports a single system of pensions across the UK and it makes sense for allowable tax deductions for pensions to be considered on a UK-wide basis.
102. Within that single UK income tax system the Scottish Parliament would set the rates and bands of income tax paid by Scottish taxpayers with two exceptions.
103. The first would be the thresholds at which an individual starts to pay tax. One of the successes of the Liberal Democrats in the UK Government has been the increases in the personal tax allowance up to £10,000. This removes two million people across the UK from paying income tax. The starting threshold of tax needs to be taken into account when addressing social welfare provision and tackling poverty and social injustice.
104. This Commission has recommended that the pensions and benefits system remain a responsibility of the United Kingdom or federal government, and for that reason it makes sense for the personal allowance for all UK taxpayers to be set by the Westminster Parliament. For similar reasons of broad policy, the age-related personal allowances, the blind person's allowance and the historic Married Couple's allowance for those born before 6 April 1935 should be set for the whole UK by the Westminster Parliament.
105. The starting threshold of tax and the provision of social welfare will be part of the partnership work that the Commission envisages taking place, to help all governments address poverty and social injustice.
106. This work will especially need to focus on the new Universal Credit, which contains a number of different existing benefits which straddle current Westminster and Holyrood responsibilities.
107. The second exception would involve the continuation of the current provision of the Scotland Act that power over the Scottish rate of income tax should not extend to the taxation of income from savings and investments. Given the importance of a single market in financial services across the UK and the need for free movement of capital across the UK, this Commission considers that the

case has not been made to pass control of tax paid at source on personal income from savings and investments to the Scottish Parliament. An estimated share of the Scottish proceeds should be allocated to the Scottish Parliament.

Recommendation 16: Income tax payable on savings and dividends should continue to be levied on a uniform basis across the UK, be deducted at source and a proportion of the UK receipts allocated to the Scottish Parliament.

108. The two exceptions mean that, in practice, Her Majesty's Revenue and Customs would perform a simple calculation on a uniform basis across the UK for each individual to determine the amount of an individual's earned income that was taxable. It would then apply the tax rates as determined by the Scottish Parliament and in due course the other home rule legislatures as part of a federal United Kingdom.
109. The Commission recognises that Capital Gains Tax operates in many ways as an additional tax on 'one-off' income from investments received by individuals. Given the increasing relative scale of likely revenues from income tax and Capital Gains Tax paid by Scottish taxpayers the Commission considers that there is a strong case for the Scottish Parliament to control the rates of Capital Gains Tax paid by Scottish taxpayers within a continuing UK system. As a result Scottish rates of Capital Gains Tax would be payable by Scottish taxpayers, irrespective of the location of the capital gain.

Recommendation 17: Powers over Capital Gains Tax should be allocated to the Scottish Parliament.

110. The separate nature of the Scottish legal system means that the law of wills, succession, confirmation and executors differs significantly between Scotland and the rest of the UK. Inheritance Tax is currently a tax on the estate of persons domiciled in the UK, those deemed to be domiciled in the UK and the UK assets of those domiciled outside the UK. Given the close link between the confirmation of executors and the payment of Inheritance Tax, subject to provisions to prevent double taxation of estates, there is a clear case for the power to tax the transfer of estates to be entirely the responsibility of the Scottish Parliament. Under such an arrangement everyone domiciled or deemed to be domiciled in Scotland would pay the Scottish Inheritance Tax on their estates and provision would be made for the taxation of the Scottish estates of non-domiciles.

Recommendation 18: Control of Inheritance Tax should be allocated to the Scottish Parliament.

111. When combined with the powers over Stamp Duty Land Tax that were allocated to the Scottish Parliament by the Scotland Act 2012, these recommendations give powerful tools for social justice and equity to the Scottish Parliament. They comprise a substantial and tangible proportion of the taxes on income and wealth paid by individuals and would be important levers of economic and social policy.

Recommendation 19: Responsibility for the Aggregates Levy should be allocated to the Scottish Parliament, subject to the outcome of the current European Union dispute, complementing the existing powers on the environment and recycling.

Recommendation 20: Responsibility for Air Passenger Duty for flights from Scottish airports should be allocated to the Scottish Parliament, to complement existing powers on the environment, transport and economic development.

112. There is a wide public association between National Insurance, entitlement to contributory benefits and other welfare matters. Elsewhere in this report are recommendations that the pensions and benefits system remain a responsibility of the United Kingdom or federal government. National Insurance has, historically, been the means to pay for much of the social welfare system and it makes sense for that to be retained – alongside such provision – at a UK level.

Recommendation 21: Powers over the National Insurance system should be allocated to the UK, and subsequently federal level of government.

The importance of the UK single market

113. In theory, under the European single market, it should be as straightforward for a Scottish business to expand and open new branches in Bratislava or Dalarna as it is in Birmingham or Durham. But natural geography, shared language and the common institutions of our 300-year union make the UK the most important single market for Scottish business.
114. Indeed, few now propose to separate macroeconomic policy or to have a different currency arrangement between Scotland and the rest of the UK.

115. And, across Europe, progress is being made to have more uniform arrangements to support business and consumers, and create a level playing-field in the market rather than more variability and fragmentation.
116. The smooth operation of that single UK market is vital and this Commission is keen to avoid making proposals that will put additional regulation and costs on businesses active across the UK.

Recommendation 22: Business, employment and financial regulation, serving the single market and supporting employees and consumers should be retained at the UK level.

117. The European Union Treaty and other technical arrangements make it impossible to vary the rates of Value Added Tax and alcohol and tobacco excise duties within the United Kingdom.

Recommendation 23: VAT and customs and excise duties on alcohol and tobacco should naturally remain the responsibility of the UK Parliament.

118. When considering Corporation Tax the Commission has been concerned not to disrupt the UK single market or add to the burdens on business by requiring them to change the way they account for their profits and to allocate them to geographical areas. The Commission is also concerned that variable rates or regimes for Corporation Tax across the United Kingdom could encourage businesses simply to switch their registered offices between jurisdictions to no overall economic benefit.
119. However the Commission believes that assigning the proceeds of Corporation Tax raised in Scotland to the Scottish Parliament would give an additional incentive to improve the economic position of Scotland, add to the Scottish tax basket and reduce reliance on an equalising payment from the United Kingdom Government. The Commission is aware that there are technical issues in identifying the appropriate figure and that Corporation Tax receipts can be volatile over the economic cycle, but does not consider these sufficient arguments against the principle of assignation of the proceeds of Corporation Tax to the Scottish Parliament.

Recommendation 24: Corporation Tax should continue to be operated and collected at the UK level, but the proceeds raised in Scotland should be assigned to the Scottish Parliament.

The Scottish tax basket

120. The Commission's recommendations on the allocation of tax powers and responsibilities gives responsibility to the Scottish Parliament for the following taxes which raised the estimated amounts shown in 2010–11 according to the Scottish Government's GERS figures and accepting the acknowledged limitations of that exercise: Income tax £10,634m, Business rates £1,891m, Council tax £1,986m, Stamp Duty £330m, Landfill tax £99m, Capital Gains Tax £244m, Inheritance Tax £159m, Aggregates Levy £54m, Air Passenger Duty £183m, Corporation Tax £3,114m.
121. The total tax basket under home rule would have generated £18,694m in 2010–11. This represents the greater part of the total spending during this period of the Scottish Government, of £34,234m.
122. This is a snap-shot example and the average of the period 2002–11 shows that this share is exceeded when tax revenues are more buoyant.
123. This means that the greater part of the expenditure by the Scottish Parliament will be covered by taxes levied by or assigned to the Scottish Parliament. This is an entirely normal and typical percentage in federal systems across the world. It addresses the complaint of the Steel Commission:

'No self-respecting parliament should expect to exist permanently on 100% hand-outs determined by another parliament, nor should it be responsible for massive public expenditure without any responsibility for raising revenue in a manner accountable to its electorate.'
124. The balance would be funded by an equalising payment from the UK Treasury which would be funded from its revenues from a wide range of taxes and duties including VAT, alcohol, tobacco and betting duties and National Insurance.
125. The recommendations on tax strike two balances. They balance equity across the United Kingdom with the desire for greater decision-making powers and incentives for the Scottish Parliament. And they balance the freedom to adopt different taxation policies in different parts of the UK against the need to minimise the risks of tax avoidance by those with the wealth to exploit such differences.

Recommendation 25: The remaining funds required to fund the Scottish Government's annual programme should come from an equalising payment from the UK Treasury as recommended by the Steel Commission.

Social and economic equity across the UK

126. The Commission strongly endorses the Steel Commission's view that Scotland and the United Kingdom benefit from the ability of the United Kingdom to act to address fiscal inequality and would wish to retain a system of balancing payments between different parts of the UK to help support common living standards and to share the risks and rewards in an uncertain world.

'Fiscal federalism should also be based on an equitable distribution of resources between different parts of the country based on their respective needs.'

127. Across the world, it is normal practice for federal governments to meet the gaps between a lower tier of government's spending needs and that tier's ability to raise the money locally, and that is why a continued block payment from the UK Treasury will continue to be necessary in a federal system.

128. The balancing payment could, of course, continue to be paid under the existing Barnett formula. This is already happening in response to the tax changes under the Scotland Act 2012 and would allow time for a transition period to be agreed across the UK in the move to a new formula.

129. Under the Scotland Act 2012 a detailed calculation is applied to income tax revenues to arrive at the adjustment to the block grant needed to balance the new power over 10p of income tax.

130. In other countries where major changes like this have been made, a transitional period of five to eight years has usually been found prudent to avoid unnecessary spikes in public revenue for the state or provincial government.

131. The Liberal Democrats have long believed that the Barnett Formula should be replaced by a genuine needs-based assessment. Given the remote nature of many of Scotland's communities, the distances involved and some of the historic problems, particularly in urban areas, with the quality of housing stock, this exercise would be helpful. It would also open the possibility of equitable funding for other parts of the UK, such as the English regions, to be accommodated through a similar exercise.

Recommendation 26: The UK should move to an independent, transparent, needs-based formula to serve all parts of the UK well and allow fiscal federalism to be sustained in the long term, recognising that the Barnett Formula was only ever intended to be a temporary measure at the end of the 1970s.

Recommendation 27: For transparency reasons, such a needs-based payment system should be based on recommendations by an independent fiscal agency separate from the UK Treasury.

132. Since the time of the Steel Commission report, the Coalition Government has created the Office of Budget Responsibility and the Joint Exchequer Board. These two institutions are potential vehicles for the task.

133. These recommendations would meet the concerns of the Steel Commission:

‘A new needs-based equalisation formula should be established to allocate grant funding across the UK, recognising the advantages to the UK of ensuring that all areas benefit from being part of the union.

‘The new system should take current expenditure levels as the base point, thereby ensuring stability of public finances for a defined period. This should include a federal safety net which would guarantee expenditure levels during the transition period.’

134. An expansion of the proportion of the expenditure of the Scottish Parliament that is met by the Scottish basket of taxes naturally increases the risk that a shortfall in tax revenue would leave the Scottish Government in deficit during part of the economic cycle, even taking account of the continued payment from the UK Treasury.

135. The Commission was impressed by the recommendations of the Holtham Commission in Wales that it would be important to make sure that the grant mechanism could adjust sensibly to deal with external global shocks to, say, the economy but would still leave the consequences and risks from variation in tax and policy choices across the UK with the parliament that sanctioned those choices.

‘It can surely be agreed that risks consequent on the actions of the Assembly Government should be borne by its budget, and risks consequent on the action of the UK Government should be borne

by UK budgets. Exogenous risks arising from elsewhere should be pooled across the union.'

136. It would be important for the Scottish Government (and others under a federal system) to have sufficient powers to borrow to cover cyclical revenue shortfalls. The Scotland Act 2012 already equips the Scottish Government with £500m of borrowing power to cover external shocks to its present revenue base of around £10bn.

Recommendation 28: The borrowing limit available to the Scottish Government to cover cyclical variations in tax revenue should be extended to £1bn to cover shocks to the proposed revenue base of around £20bn. This money would continue to be borrowed from the Treasury, as under the Scotland Act provisions.

137. The Commission notes that since the Steel Commission reported in 2006 the world has gained a greater appreciation of the risks of sovereign debt, sub-sovereign debt, of the power of credit rating agencies and of the importance of fiscal prudence. A significant benefit from these proposals – retained from the current devolution settlement – is that borrowing to cover cyclical revenue shortfalls is done from the UK Treasury, which benefits from the strong international credit reputation of the United Kingdom.

Recommendation 29: A fiscal pact should be agreed between the Scottish Government and UK Government under home rule, or all home rule governments in a federal United Kingdom, to define limits on borrowing and fiscal action. Tax cuts and extra borrowing require to be paid for – there is no 'free ride'. Home rule all round should mean responsible government all round.

138. The provision of greater borrowing powers to meet a cyclical deficit would enable the Scottish Government to balance its budget over the economic cycle, and where these borrowing powers were insufficient to meet a catastrophic shock, such as the global collapse of 2008, then the establishment of a fiscal pact will give all governments the opportunity to make an exceptional case for joint action to address what would be an overall UK deficit and challenge.
139. In a federal system all parts of the country gain strength from being part of the United Kingdom in adversity.

Borrowing to invest

Recommendation 30: The Scottish Government, and other home rule governments under a federal system, should be permitted to borrow for capital investment under the prudential regime.

140. At its heart this permits borrowing as long as it can be demonstrated that a revenue stream exists, or can be created, to meet the repayments.
141. This will not necessarily need to be formally limited by the UK Government but the possibility should remain open – mindful of the examples across Europe where imprudence by lower tiers of government has adversely affected the credit rating of a higher tier.
142. The Calman Commission made a similar recommendation:

‘Scottish Ministers should be given an additional power to borrow to increase capital investment in any one year. There should be an overall limit to such borrowing, similar to the prudential regime for local authorities. The amount allowed should take account of capacity to repay debt based on future tax and other receipts. Borrowing should be from the National Loans Fund or Public Works Loans Board.’
143. These powers were introduced through the Scotland Act 2012.
144. There is merit in examining whether, in future, the Treasury could remove the revenue/capital split in its grant payments. This would allow the Scottish Parliament to decide the appropriate mix of revenue and capital, consistent with the prudential borrowing regime.

Oil and gas revenues

145. The Commission is strongly of the view that the worldwide oil and gas industry views the UK continental shelf as a single administration and judges that it should remain a single entity from the point of view of the industry. The biggest benefit to Scotland from oil and gas continues to be the jobs and the associated wealth that come from them. Any disruption to the coherence of the industry on the UK continental shelf puts these jobs at risk.

146. It is important to appreciate that over the past thirty-five years the UK has operated an overall cumulative total budget deficit. This has also been true for Scotland. The huge revenues from the continental shelf have been spent to fund deficits and, as a result, there could never have been an oil fund for the UK or for Scotland unless public spending had been cut to eliminate the deficit that the oil revenue funded.
147. This is a matter of regret, not least because Liberals at the very start of North Sea oil extraction proposed efforts to establish an oil fund. The Steel Commission noted:

'Back in the 1970s, the Scottish Liberal Party and our then Leader, Russell Johnston MP, called for the setting up of a Scottish Oil Development Corporation to provide an investment fund for Scottish industry, funded by a share of the oil revenues. The opportunity was missed (except by Shetland Islands Council) and the money failed to make an impact as the country fell into recession and manufacturing decline. There is a case for looking again at how Scotland shares in the revenues from the North Sea.'

148. The Commission believes that the UK as a whole should reconsider how it views oil and gas revenues. These are resources that will, eventually, come to an end. They are a finite resource and should be treated as such. The proceeds from oil can still, in future, be used to pay for investment that will allow the economy to grow, wealth to be created and well-being to be assured after oil and gas end.
149. This won't be easy. There have been UK revenue deficits of more than £100bn in recent years. But we should plan for better times ahead.

Recommendation 31: Oil and gas revenues should continue to be treated on a UK-wide basis, preserving the single taxation regime for the UK's North Sea sector. Consideration should be given to the establishment of an oil fund, when the deficit situation has been brought under control, allocating the proceeds to the benefit of Scotland, England, Wales and Northern Ireland on federal principles.

The policy responsibilities of home rule Scotland

150. Most of the domestic powers are already allocated to the Scottish Parliament. Indeed, in legislative terms, the Scottish Parliament is one of the most

powerful in the world and already has substantial powers to improve the lives of its citizens.

151. The Calman Commission reviewed the powers reserved to Westminster and made recommendations which have recently been enacted through the Scotland Act 2012.
152. People expect to be able to retire to any part of the UK and receive the same guarantee of the state pension. People expect to accumulate an equal entitlement to the state pension wherever they work within the United Kingdom. People looking for work, or caring for relatives, expect to receive equal treatment wherever they live in the United Kingdom.
153. People want common minimum living standards across the UK with automatic support to people in need, irrespective of their location.
154. This is achieved by making welfare payments the responsibility of the UK Government.
155. As referred to earlier, this has implications for National Insurance payments, which are widely accepted to be the driver of the welfare state in the UK.
156. An area where closer joint working will be of benefit to people in Scotland is that of skills and training.

Recommendation 32: Social protection, pensions and welfare payments should be allocated to the UK (and subsequently federal) level.

Recommendation 33: The Scottish Government should act as the agent for the UK Government in Scotland on much of the work of JobCentre Plus and the Work Programme.

157. This proposal would encourage partnership-working and should be supported by a provision to recognise that the operation of this aspect of the welfare system requires partnership-working between the Scottish Government and UK Government.
158. The cash payments to those seeking work would continue to be made by the UK Government but full responsibility for skills and training would pass to the Scottish Government.

Putting partnership-working into practice

159. In considering the other policy powers that need to be allocated, the Commission is keen to foster a culture of co-operation and partnership between the different tiers of government.
160. In some cases, the best approach will be for a policy power to be deployed at a UK level, entirely by the UK Government.
161. For other policy powers, the idea of different kinds of partnership-working gives scope for greater benefits.
162. The Commission has been struck by the importance of the UK single market. Trade between the different parts of the UK is something that happens naturally and without barriers. The business community attaches huge importance to the continuation of the UK single market.
163. It is not wise to disrupt that market and to add to the burdens of those transacting business across the UK.

Recommendation 34: Health and safety legislation, competition laws and employment law should be allocated to the UK (and then federal) level.

164. Scrutiny of any particularly Scottish implications from those powers should be the responsibility of Scottish MPs at Westminster.
165. There is a case for additional powers for the Scottish Parliament in relation to competition matters where there is a demonstrable issue of competition within Scotland, that is different to the situation elsewhere within the United Kingdom.

Recommendation 35: Competition law should remain a UK responsibility, but the Scottish Government should be empowered, after similar consultation to that currently required by the UK minister, to request the Competition and Markets Authority (as it will be in 2014) to investigate an issue of failing markets or potential monopolies within Scotland.

166. This would allow consideration of monopoly and competition issues, not just within the UK market but in response to a Scottish test that a strengthened Competition and Markets Authority should address.

Recommendation 36: Rather than continue a seemingly endless process of revisiting the list of reserved matters, the future federal, United Kingdom should take seriously

the recommendation of the Steel Commission to establish a new constitutional category for partnership-working.

‘One of the key principles of a federal union would be support for partnership-working between different levels of government. A constitutional provision supporting joint working might be a powerful tool for innovative practice in good government.

‘In a number of new areas, this would include a legal requirement to consult the Government and Parliament before progressing beyond specific legislative stages. There would be further provision to ensure that appropriate timing mechanisms are agreed to allow the Scottish Government and Parliament time to consider properly the impact of policy proposals from the UK Government.’

167. This would mean that matters such as energy policy and transport policy could be dealt with by partnership-working, where the Scottish Parliament would enjoy freshly enhanced rights to influence decision on these matters.
168. Strategic decisions over the National Grid, energy planning and the security of energy supply, carbon trading and renewable developments are clearly of importance to both federal and Scottish Governments. A more federal structure lends itself to sensible decisions over the UK electricity market.
169. On the issue of nuclear power, for example, Holyrood and Westminster favoured different approaches in Scotland at the turn of the 21st century. This was resolved by pragmatic action rather than reallocation of powers. There are no new nuclear power stations planned for Scotland because the UK Government has taken notice of the objections of the Scottish Parliament and Government.
170. Much of transport policy is now under the jurisdiction of the Scottish Parliament, but there are major cross-border issues such as legislation affecting commercial vehicles, bus operators and trans-national rail which remain reserved to Westminster. Nevertheless, these issues almost always require a wider UK perspective, not a London-centric one. A good example is the issue of high speed rail link, which could have benefited from more effective input into its strategy and planning from the Scottish Government.

171. Similar partnership-working would serve the country well in maritime policy where there are complex layers of interests – coastguard, merchant fleet, fisheries and conservation.
172. As mentioned earlier in the report, this could be extended to social protection and welfare matters and to the drive to promote social justice and tackle poverty. The Commission believes that no single tier of government acting alone would be able to conquer these ills. The earlier recommendations on addressing social ills as part of the declaration of federal union would help.
173. Finally, the United Kingdom should have a unified system of electoral law and administration for different levels of election. This single culture of elections would be an issue for agreement between the UK Government and the home rule governments.

Recommendation 37: Control over the Scottish Parliament’s electoral system and franchise should be allocated to the Scottish Parliament to entrench its equality and authority within the UK. Electoral administration and law, together with the regulation of political parties and their funding should remain a matter for the UK Government.

174. For many other of the reserved areas – taking as examples science funding or the detailed rules governing embryology – the Commission views these as best dealt with at a UK level.
175. Similarly, the recent success on Team GB at the Olympics gives strength to the view that aspects of elite sport should continue to be funded and organised at a UK level.
176. There are legitimate issues surrounding the coverage by broadcasters of political and social issues in all parts of the UK. As a federal UK developed it would be important to ensure that these were addressed. Similarly, the location of production facilities for broadcasting needs to be seen to be equitable across the UK. The Commission believes that the BBC and the UK media market are successful because of the fact that they operate across the UK and reflect many different cultures and national and regional identities. We do not think the case is made for a separate Scottish Broadcasting Corporation.

Recommendation 38: Broadcasting should continue to be regulated at a UK level to reflect a single UK market, whilst encouraging steps to ensure equitable distribution of broadcasting and media jobs throughout the United Kingdom.

Recommendation 39: On EU matters, protocols and practices should be revised to reflect the need to negotiate and act on an agreed UK position where devolved responsibilities such as fishing or agriculture are concerned – particularly at the Council of Ministers level. Scottish ministers should be fully involved, to make sure that an agreed UK position is established, sustained and represented at meetings.

177. The Commission notes, however, that on the issue of visas for overseas students, the views of Scottish universities, in common with many in England, have not been accommodated by the UK Government. This shows that not all issues will be resolved to everyone's satisfaction and demonstrates the need for more integrated decision-making through greater partnership.

CHAPTER 4:

Localism

178. Scotland is a geographically diverse and complex country. The communities which make up our nation have different needs, capacities and priorities. A strong and effective system of local government responsive to local needs and the diverse demands of the people of Scotland is essential.
179. Liberal Democrats believe that decisions should be taken as closely as possible to the citizen – wherever possible by the citizen or by local communities. Home rule for Scotland is part of this process but, by itself, insufficient. An entrenchment of strong communities wielding effective local powers and initiative is also vital.
180. A liberal democracy that is serious about giving power to individuals and communities will need to transfer power out of the capital city – whether London or Edinburgh – and into local communities. That is a principle of subsidiarity.
181. In 1995 the Scottish Constitutional Convention declared, in *Scotland's Parliament, Scotland's Right*:
- 'The value of local government stems from three essential attributes: first, it provides for the dispersal of power both to bring the reality of government nearer to the people and also to prevent the concentration of power at the centre; second, participation, local government is government by local communities rather – as in the case of non-elected bodies – of local communities; and thirdly, responsiveness, through which it contributes to meeting local needs by delivering services.'*
182. At present Scottish local authorities have almost no independent revenue-raising mechanism that can support the public services they provide; a situation that is almost unique in Europe. Local authorities and communities across Scotland should have substantial democratic choice and opportunities in the way they plan and deliver the services on which the public relies.

Recommendation 40: Local authorities should raise around half of the money they spend locally in order to improve accountability and local power.

183. Public services in Scotland are increasingly centralised in the hands of Scottish ministers in Edinburgh. Since 2007 the effect of the concordat, single outcome agreements, the council tax freeze and the end of three-year budgeting has been to force local authorities to deliver the services that Scottish ministers desire. The nationalisation of the fire and police services will substantially weaken the possibility of local services operating in a way that matches local need rather than national plans.
184. Local authorities must, of course, be efficient custodians of public funds. But the sharing of common services must be done in a way that enhances local accountability and allows communities to choose the solutions and services that suit their needs. Recent national projects, such as joint procurement, lead commissioning of social care services and the national road maintenance review show how national efficiency drives can reduce local accountability.
185. The Scottish Constitutional Convention had a vision of a strong and accountable system of local government in Scotland after devolution. These ambitious proposals were not fully implemented and as a result Scottish ministers, whilst subject to the controls of the Scottish Parliament, have effectively the same potential power of patronage and financial control over local government as the Secretary of State for Scotland had prior to 1999.
186. This report proposes a range of reforms to return power to local authorities and the communities that make up Scotland. These are:
- increased financial autonomy for local authorities;
 - clear powers of general competence for local authorities;
 - a system of local burgh councils where there is demand;
 - a greater role for community action and community planning;
 - the application of the principle of subsidiarity to the relationship between local authorities and Holyrood, and between local communities and councils.

Financial autonomy for local government

187. It is right for the Scottish Parliament to raise a significant proportion of the revenue it requires to fund public services in Scotland. A similar principle of responsible government should apply to local authorities as well.
188. Local authorities currently receive a revenue grant from Scottish ministers which amounts to around 85% of their revenue expenditure, with the remainder funded largely from local taxation and charges. This effectively means that there is little connection between the efforts that a council can make to improve public services, support enterprise or reduce deprivation, and the resources it has at its disposal.

Recommendation 41: New legislation should prevent Scottish ministers from linking local authority funding levels to the rates of council tax and other taxes and charges levied by councils. The rates of council tax and other locally controlled taxes in each council should be under the control of locally elected councillors, who would be accountable to their electorates.

189. Councillors should have responsibility for the decisions that affect their communities. Some areas of national policy are best driven nationally, but implemented locally. The funding of these projects often distorts the local government funding settlement and confuses questions of local accountability.
190. Where a truly national challenge requires to be addressed by local action Scottish ministers should establish a national fund, set priorities and leave local decision-makers to determine how that national funding is spent in their communities. The most important example of such a challenge is the scandalous level of multiple deprivation in Scotland.
191. Scottish ministers should identify revenue funding levels specifically required by councils to address the problem of multiple deprivation.

Recommendation 42: The Scottish Parliament should establish a 'One Scotland Fund', separated from current local government revenue grant, to enable Scottish ministers to award funding to local authorities that require support to tackle multiple deprivation. The 'One Scotland Fund' should provide a separate funding stream from general Scottish Government funding to local government to address deprivation in each area.

192. Many communities in Scotland are blighted by lack of economic opportunity. Local authorities should be encouraged to improve the business environment in their communities by receiving the revenue benefits from improvements in their local economy.
193. Restoration of the direct connection between the payment of business taxes and the funding of individual local authorities will help to encourage a focus on sustainable economic development.
194. Business rates are one of the most significant taxes paid by businesses, and local authorities should be able to implement a system of locally funded reliefs to support regeneration of high streets and town centres and other economic and environmental priorities.

Recommendation 43: Local authorities should set the business rate poundage and retain the entire revenue from business rates in their areas.

195. In order to balance the competing benefits of local autonomy and a single local business tax system, the valuation system and structure of business rates should continue to be the same across Scotland, but local authorities should set the poundage and be empowered to fund specific reliefs for particular classes of business deemed vital for their communities as part of their wider economic development powers.
196. The Scottish Government should continue to fund reliefs of their choosing – such as for smaller businesses – by making the appropriate payments to the councils.
197. The process of negotiating the distribution of revenue grant for local government continues to be a source of conflict between local authorities and Scottish ministers. The proposal to separate funding to tackle multiple deprivation from revenue grant will remove some of the distortions inherent in the present system.

Recommendation 44: The operation of a new assessment for the allocation of funding between local authorities should be based on recommendations to Scottish ministers from a new Local Government Finance Commission.

198. The Finance Commission should be accountable to ministers and the Scottish Parliament, which would approve the recommended revenue grants to local authorities.

199. Under this proposal Scottish ministers would decide the total funding allocated for local government revenue funding, but the independent commission would identify the criteria for funding distribution, consult widely on its methodology and produce a proposed distribution of funding between local authorities in an open and accountable manner. The Scottish Parliament would continue to approve that distribution by affirmative resolution of the Parliament.
200. The effect of these proposed reforms would be to increase the autonomy of local authorities and increase their accountability by linking more closely the funding of local services to revenue collected within local authority areas.
201. Government figures show total local authority revenue spending at around £17bn. Under the proposals in this report the council tax would raise £2.2bn, locally set business rates £2.1bn and local authority income from fees, charges and specific grants for services provided would raise up to a further £4bn depending on how the calculation is performed. This meets the aim of roughly half of funding coming from locally sourced money.
202. The Commission accepts that there will be circumstances where changes to local tax bases could have the effect of reducing the funding available to particular local authorities over the medium term. Just as Scotland gains security against such changes by being part of the United Kingdom, every council should be protected from being left too far behind the Scottish average by being part of Scotland.
203. There is merit in a periodic review – perhaps every five years – of the level of central funding received by councils to ensure they are treated fairly in relation to matters outwith their control – particularly changes to the size of their local tax base.
204. For the start of the new system of local business rates, the level of supporting grants given to each authority should be adjusted to ensure that no council is better or worse off in the first year. This maintains the principle of equalisation across Scotland.

The powers of local authorities

205. Prior to the establishment of the Scottish Parliament, the Constitutional Convention proposed that the provisions of Article 4 of the European Charter of Local Self Government should be implemented in Scotland. This provides that,

‘Local authorities shall, within the limits of the law, have full discretion to exercise their initiative with regard to any matter which is not excluded from their competence nor assigned to any other authority.’

206. The Commission considers that, in a number of areas, local authorities are compelled to implement Scottish Government policies rather than to respond to local needs and demands. Scottish ministers have the power to micro-manage and seem unable to resist the temptation to do so. In particular the Commission is concerned that the system of single outcome agreements between Scottish ministers and local authorities places too much control in the hands of ministers.

Recommendation 45: Single outcome agreements, currently subject to approval by ministers, should be replaced by true local community plans where every council takes responsibility for delivering a plan for its area that is generally aligned to what voters voted for in local elections, and what local people believe to be appropriate or relevant to their community.

207. In the Local Government in Scotland Act 2003 the Scottish Parliament gave local authorities the ‘power to advance the wellbeing’ of a council’s area. As legislated, this power is more restricted than the general power of competence provided for local authorities in England in the Localism Act 2011.
208. Providing a clearer and less restricted general power of competence would allow local authorities to act in the interest of their own communities and in their own financial interest to deliver efficiencies, secure value for money, raise funds by trading and charging and to provide any necessary guarantees and indemnities.

Recommendation 46: The local authority power to advance wellbeing should be replaced by a general power of competence along the lines of the power provided in Part 1 of the Localism Act 2011 in England.

209. The effective use of land is an essential tool in the sustainable development of Scotland’s communities. Too often ‘best value’ accounting rules prevent public land being effectively used for public good by bodies other than local authorities. It should be easier for local authorities to use land for purposes that are not necessarily ‘best value’ for the council, but have a higher value to the community which is served by the local authority.

Recommendation 47: The provisions of the general power of competence should include re-definition of Best Value that would allow land to be transferred by a local authority to a not-for-profit entity which is providing a public good.

210. The general power of competence would be more effective if combined with a simplified mechanism for local authorities to create by-laws.

Recommendation 48: To free local authorities to innovate, when a principal local authority proposes a by-law, unless it legislates for a reserved matter or is contrary to the European Convention of Human Rights, the consent of the Scottish ministers should not be unreasonably withheld.

21st-century burgh councils

211. There is a strong feeling in some parts of Scotland, not least away from the cities, that the local authorities established under the Local Government (Scotland) Act 1994 remain remote from local need. In the Highlands, parts of the north-east and the south-west of Scotland there is still a feeling that the old district councils were accessible and accountable in a way that is not the case for some of the large councils that have replaced them.
212. There is no case for a wholesale reform of local government or the re-establishment of two-tier local government, but there is a case for local burgh councils where communities demand change. Such new local community focused authorities would empower communities and give a true local focus to service delivery. The name of burgh council is a deliberate reference back to the old pre-1974 burghs, as such authorities may have most resonance to smaller towns, islands and communities that currently feel that they are at the periphery of existing local authorities.
213. The possibility of the creation of burgh councils would enhance the sense that our communities can make a difference to the lives of residents and can be more accountable than the existing local authority or Scottish ministers in Edinburgh. The possibility for the community to create a burgh council might be the pressure that encourages the existing local authority to pay great attention to local needs and demands in an otherwise overlooked part of their area.
214. In many areas existing structures of community planning, local associations and trusts, housing associations and continuing strong and effective community councils provide the local legitimacy that is an essential part of local democracy.

But in some parts of the country there may be a demand for new burgh councils to run local services, get real value from publicly owned assets and make land work in a sustainable way for the whole community.

215. New burgh councils may be most attractive in rural Scotland, but there is potential for their creation within urban Scotland if demand exists.

Recommendation 49: A mechanism should be established by which a community can bring forward a proposal for a burgh council to take over certain services provided by the principal local authority in the area. This could be funded by a precept on the council tax and/or business rates raised in the area, a proportion of the revenue support grant allocated to the existing local authority or by charges for the use of the services taken on by the burgh council. No new tax would be created.

216. Burgh councils should also be able take over specific responsibilities from existing local authorities, quangos and Scottish ministers.
217. With the support of local people burgh councils should be able to take over community facilities such as community and sports centres, libraries, parks, social housing, land for social housing, assets held in the common good or underused council-owned business premises. If local support exists, burgh councils should be able to take over responsibilities such as road maintenance, waste management, public transport, the delivery of social care, licensing and planning.

Recommendation 50: Legislation should impose upon local authorities a duty to co-operate with burgh councils established in their area about the services they provide.

218. The establishment of burgh councils should be subject to the approval of the residents of the area of the new burgh council in a referendum.
219. A new burgh council would not have a general power of competence. The new burgh council could take over the role of community council for its area or it could operate alongside community councils. It would be a matter for the charter of the new burgh council.
220. The powers of each burgh council would be set out in its charter, which would be a statutory instrument laid before the Scottish Parliament by Scottish ministers after a successful local referendum.

Greater power for communities

221. Localism is not just about the powers of existing local government. In recent years there have been many useful developments in community planning that have enabled communities to challenge the way that local services are delivered, hold local authorities and government agencies to account and develop plans and partnerships that have made a real difference. The Commission believes that this process should continue and that Scottish ministers and national quangos should do more to work with local authorities and the communities they serve.

Recommendation 51: Legislation should be introduced to impose upon Scottish ministers and quangos a duty to co-operate with local authorities about the services they provide in each authority's area.

Recommendation 52: Community Planning Partnerships should be required to publish records of the ownership of all public land in their area so that the public are aware of who owns what in the public sector.

222. In The Land Reform (Scotland) Act 2003, Labour and the Scottish Liberal Democrats introduced the community right to buy in rural areas. There is a strong case to say that in urban areas where a public organisation – whether local government, quango or Scottish ministers – fails to fully utilise land, the community should be able to step in and buy or take over that land for use by the community.

Recommendation 53: Local communities, whether represented by an independent trust, a trust associated with a community council, a burgh council or local authority should be enabled to take over underused public land or assets in their community for a specific not-for-profit purpose that is for the public benefit.

223. The Commission recognises the strong role housing associations play or can play in localism and community power. However, some associations are not making use of their current powers on local decision-making.

224. The role of housing associations should be enhanced to give them the opportunity to bid for public service delivery contracts and involve them in service planning processes.

225. Over the past decade there has been increased discussion and debate around both the status and use of common good lands and assets of the pre-1973

burghs and the role and accountability of the Crown Estate in Scotland. Experience shows that the ownership and sustainable development of property has been an effective economic development tool for many local authorities. The Commission is concerned that transfer of the control of the Crown Estate in Scotland to Scottish ministers would simply increase the power of central government at the expense of local, particularly coastal, communities. The principles of community rule and subsidiarity should encourage the transfer of the control of assets that are not in use for any great national purpose to the lowest level of local government to benefit local people and the environment. The Commission believes that there is a strong case for reforming both the common good system and the Crown Estate to endow Scotland's local authorities with an inheritance of land and property rights that can be used to benefit their communities.

Recommendation 54: Crown Estate assets and harbour, pier, foreshore and similar rights should be transferred to the control and benefit of local authorities, protected and sustained as 'common good' assets that cannot be disposed of.

Recommendation 55: Local authorities and burgh councils should be entitled to petition the Scottish Parliament for the transfer of underused public land to their common good fund so that the land can be used for sustainable local uses.

226. There is also a growing pot of potential community asset in the form of growing land value arising from planning gain. The development of innovative approaches to securing the economic benefit for local communities from the gains in land value because of planning decisions will be a further way to support local communities.

Protecting local government

227. The Commission believes that a secure and strong, effective and autonomous system of local government is essential for the good government of Scotland, but there are few practical restraints on the way that Scottish ministers can act in respect of local government. The restrictions in the Scotland Act and even the effect of the European Convention of Human Rights are of limited restraint on the powers of ministers over councils.
228. In *Scotland's Parliament, Scotland's Right* the Constitutional Convention envisaged that the Scotland Act should include a clause committing the Scottish Parliament to secure and maintain a strong and effective system of local

government and also embodying the principle of subsidiarity so as to guarantee the important role of local government in service delivery. Unfortunately, these provisions were not included in the Scotland Act 1998. It is notable that similar provisions were included in the Government of Wales Act 1998.

229. Protection for local authorities should extend to changes to their boundaries, which should require their consent.

Recommendation 56: The protection for local authorities such as those envisaged in *Scotland's Parliament, Scotland's Right to secure and maintain a strong and effective system of democratically elected local government should be enacted by the Scottish Parliament.*

Conclusion

230. Home rule and local community power are both part of the same Liberal Democrat aspiration: that the structures of government should be relevant to and accountable to the public; that democratic power stems from the people and should be operated at an effective level but, where possible, at the lowest appropriate level.
231. The recommendations in this report amount to a charter for the democratic renewal of our country at all levels, and for the creation of robust structures of governance which are fit for the modern age.

Members of the Commission

Sir Menzies Campbell MP is the Member of Parliament for North East Fife and a former leader of the Liberal Democrats.

Robert Brown is a Liberal Democrat councillor on South Lanarkshire Council. From 1999-2011 he was MSP for Glasgow, serving as Deputy Minister for Education and Young People from 2005-7. He was Scottish Liberal Democrat policy convener until 2007, and vice chair of the Steel Commission.

John Barnett has degrees in law and economics and was a member of the Steel Commission. After twenty years in the City of London in the field of international corporate and institutional banking, he returned to Scotland to work in the third sector. He currently has responsibility for the Scottish business of a leading UK social finance institution.

Fred Mackintosh is an advocate with a practice in the High Court of Justiciary Appeal Court. From 1999 to 2007 he was a City of Edinburgh councillor with a particular interest in community planning. In the 2010 General Election he was the Liberal Democrat candidate in the marginal constituency of Edinburgh South.

Audrey Findlay CBE was a Liberal Democrat councillor from 1988 when elected to Gordon District Council until 1996, and from then as leader of the new Aberdeenshire Council until 2007. She was convener of the Scottish Liberal Democrats from 2008-2010 and remains a member of the Executive Committee. She was also one of the Liberal Democrat members of the Calman Commission, along with Lord Wallace of Tankerness.

John Edward is the former head of the European Parliament's office in Scotland and currently works in Scottish education. Prior to that he was parliamentary manager for Scottish Enterprise, and previously worked at Scotland Europa and the European Policy Centre in Brussels. He was a member of the Steel Commission and has served on this Commission in a personal capacity.

Hugh Andrew is founder and managing director of Birlinn Ltd, one of Scotland's largest publishers. After a year with the National Trust he has worked in the Scottish book industry since his graduation from Oxford. He is a trustee of a number of charitable bodies. He lives and works in Edinburgh.

Shabnum Mustapha was a member of the Commission until her appointment as a special adviser to the Deputy Prime Minister in September 2012. She has ten years of experience working in policy, campaigns and media. She was Director of Amnesty International Scotland and on the board of directors of the Coalition for Racial Equality and Rights.

Matthew Clark provided secretariat services.

Remit of the Home Rule and Community Rule Commission

1. To describe a positive vision for the future of Scotland, based on the historic support of the Scottish Liberal Democrats and our predecessors for home rule.
2. To build on the report of the Steel Commission, which identified the benefits to Scotland and the United Kingdom of a federal structure.
3. To make specific recommendations on the way powers and responsibilities can be divided between local, Scottish, United Kingdom and European levels, using the principles established by the Steel Commission.
4. To define the powers and responsibilities necessary to sustain the social, economic, and political cohesion of the United Kingdom.
5. To ensure the proposed Home and Community Rule settlement gives a stable fiscal platform to enable substantial democratic choices and the opportunity for real change within Scotland.
6. To set out what changes to the constitution and governance of the UK can best help support home rule.

Furthermore, the Commission should:

7. Develop ideas and principles which would form the basis of a Scottish Localism Bill.
8. Consider what additional financial powers could be exercised by local authorities.

Summary of recommendations

Recommendation 1: the Scottish Liberal Democrats should reassert that they are federalists: in favour of home rule, within a strong and federal United Kingdom.

Recommendation 2: the proposals for home rule for Scotland and federalism across the UK should be included in the Liberal Democrat manifesto across the UK at the 2015 general election.

Recommendation 3: Liberal Democrats across the United Kingdom should seek a political mandate for a 'route map' to a federal constitution at the 2015 General Election.

Recommendation 4: Political parties and civic society should progress debate on proposals for a reformed UK constitution, including how purely English matters should be determined.

Recommendation 5: The concept of mutual respect, already endorsed as the principle governing relationships between the UK and Scottish governments, should be incorporated as a constitutional obligation on federal and state governments to respect and support each other's role.

Recommendation 6: The status and functions of certain UK-wide institutions – notably Her Majesty's Revenue and Customs – should be given a protected and more independent constitutional position in recognition of the fact that they will be expected to serve all parliaments and jurisdictions within the UK.

Recommendation 7: the present level of Scottish representation at Westminster should be retained until a federal structure for the UK has been delivered.

Recommendation 8: The role of the Scotland Office should be reviewed as the United Kingdom moves towards a federal union. Until the move to a federal state is well underway the Scotland Office should remain as Scotland will need the safeguard of a Secretary of State in Cabinet to look after its interests during the transition.

Recommendation 9: Some functions of government should constitute a third category – additional to 'reserved' and 'devolved' powers – namely 'partnership powers', which require the co-operation of both home rule and federal governments.

Recommendation 10: In addition to a general constitutional obligation of mutual respect, policy functions in areas of 'partnership powers' should impose a legal duty on

one government – more normally the federal government – to consult the other government on a partnership basis.

Recommendation 11: Each tier of government should have a formal ‘power of initiation’, enabling it to request the other tier to take some specific action to facilitate policy objectives in an area where the other government has the policy lead.

Recommendation 12: The strategic planning of welfare services should be considered for joint working combined with a constitutional duty to tackle poverty through efforts at every level of government.

Recommendation 13: The Supreme Court should exercise jurisdiction in relation to dispute resolution, whilst maintaining that it is not the role of the court to determine substantive political disputes.

Recommendation 14: The UK Parliament should commit to a declaration that entrenches home rule and the Scottish Parliament in advance of a full federal settlement.

Recommendation 15: Income tax paid by Scottish taxpayers should be almost entirely the responsibility of the Scottish Parliament.

Recommendation 16: Income tax payable on savings and dividends should continue to be levied on a uniform basis across the UK, be deducted at source and a proportion of the UK receipts allocated to the Scottish Parliament.

Recommendation 17: Powers over Capital Gains Tax should be allocated to the Scottish Parliament.

Recommendation 18: Control of Inheritance Tax should be allocated to the Scottish Parliament.

Recommendation 19: Responsibility for the Aggregates Levy should be allocated to the Scottish Parliament, subject to the outcome of the current European Union dispute, complementing the existing powers on the environment and recycling.

Recommendation 20: Responsibility for Air Passenger Duty for flights from Scottish airports should be allocated to the Scottish Parliament, to complement existing powers on the environment, transport and economic development.

Recommendation 21: Powers over the National Insurance system should be allocated to the UK, and subsequently federal level of government.

Recommendation 22: Business, employment and financial regulation, serving the single market and supporting employees and consumers should be retained at the UK level.

Recommendation 23: VAT and customs and excise duties on alcohol and tobacco should naturally remain the responsibility of the UK Parliament.

Recommendation 24: Corporation Tax should continue to be operated and collected at the UK level, but the proceeds raised in Scotland should be assigned to the Scottish Parliament.

Recommendation 25: The remaining funds required to fund the Scottish Government's annual programme should come from an equalising payment from the UK Treasury as recommended by the Steel Commission.

Recommendation 26: The UK should move to an independent, transparent, needs-based formula to serve all parts of the UK well and allow fiscal federalism to be sustained in the long term, recognising that the Barnett Formula was only ever intended to be a temporary measure at the end of the 1970s.

Recommendation 27: For transparency reasons, such a needs-based payment system should be based on recommendations by an independent fiscal agency separate from the UK Treasury.

Recommendation 28: The borrowing limit available to the Scottish Government to cover cyclical variations in tax revenue should be extended to £1bn to cover shocks to the proposed revenue base of around £20bn. This money would continue to be borrowed from the Treasury, as under the Scotland Act provisions.

Recommendation 29: A fiscal pact should be agreed between the Scottish Government and UK Government under home rule, or all home rule governments in a federal United Kingdom, to define limits on borrowing and fiscal action. Tax cuts and extra borrowing require to be paid for – there is no 'free ride'. Home rule all round should mean responsible government all round.

Recommendation 30: The Scottish Government, and other home rule governments under a federal system, should be permitted to borrow for capital investment under the prudential regime.

Recommendation 31: Oil and gas revenues should continue to be treated on a UK-wide basis, preserving the single taxation regime for the UK's North Sea sector. Consideration should be given to the establishment of an oil fund, when the deficit situation has been

brought under control, allocating the proceeds to the benefit of Scotland, England, Wales and Northern Ireland on federal principles.

Recommendation 32: Social protection, pensions and welfare payments should be allocated to the UK (and subsequently federal) level.

Recommendation 33: The Scottish Government should act as the agent for the UK Government in Scotland on much of the work of JobCentre Plus and the Work Programme.

Recommendation 34: Health and safety legislation, competition laws and employment law should be allocated to the UK (and then federal) level.

Recommendation 35: Competition law should remain a UK responsibility, but the Scottish Government should be empowered, after similar consultation to that currently required by the UK minister, to request the Competition and Markets Authority (as it will be in 2014) to investigate an issue of failing markets or potential monopolies within Scotland.

Recommendation 36: Rather than continue a seemingly endless process of revisiting the list of reserved matters, the future federal, United Kingdom should take seriously the recommendation of the Steel Commission to establish a new constitutional category for partnership-working.

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Recommendation 44: The operation of a new assessment for the allocation of funding between local authorities should be based on recommendations to Scottish ministers from a new Local Government Finance Commission.

Recommendation 45: Single outcome agreements, currently subject to approval by ministers, should be replaced by true local community plans where every council takes responsibility for delivering a plan for its area that is generally aligned to what voters voted for in local elections, and what local people believe to be appropriate or relevant to their community.

Recommendation 46: The local authority power to advance wellbeing should be replaced by a general power of competence along the lines of the power provided in Part 1 of the Localism Act 2011 in England.

Recommendation 47: The provisions of the general power of competence should include re-definition of Best Value that would allow land to be transferred by a local authority to a not-for-profit entity which is providing a public good.

Recommendation 48: To free local authorities to innovate, when a principal local authority proposes a by-law, unless it legislates for a reserved matter or is contrary to the European Convention of Human Rights, the consent of the Scottish ministers should not be unreasonably withheld.

Recommendation 49: A mechanism should be established by which a community can bring forward a proposal for a burgh council to take over certain services provided by the principal local authority in the area. This could be funded by a precept on the council tax and/or business rates raised in the area, a proportion of the revenue

support grant allocated to the existing local authority or by charges for the use of the services taken on by the burgh council. No new tax would be created.

Recommendation 50: Legislation should impose upon local authorities a duty to co-operate with burgh councils established in their area about the services they provide.

Recommendation 51: Legislation should be introduced to impose upon Scottish ministers and quangos a duty to co-operate with local authorities about the services they provide in each authority's area.

Recommendation 52: Community Planning Partnerships should be required to publish records of the ownership of all public land in their area so that the public are aware of who owns what in the public sector.

Recommendation 53: Local communities, whether represented by an independent trust, a trust associated with a community council, a burgh council or local authority should be enabled to take over underused public land or assets in their community for a specific not-for-profit purpose that is for the public benefit.

Recommendation 54: Crown Estate assets and harbour, pier, foreshore and similar rights should be transferred to the control and benefit of local authorities, protected and sustained as 'common good' assets that cannot be disposed of.

Recommendation 55: Local authorities and burgh councils should be entitled to petition the Scottish Parliament for the transfer of underused public land to their common good fund so that the land can be used for sustainable local uses.

Recommendation 56: The protection for local authorities such as those envisaged in *Scotland's Parliament, Scotland's Right* to secure and maintain a strong and effective system of democratically elected local government should be enacted by the Scottish Parliament.