

Transitioning to a new Scottish state

Immediate set-up costs, how the handover will work, and the
long-run viability of Scottish government

By Professor Patrick Dunleavy, with Sean Kippin and Joel Suss



About this e-book

Democratic Audit and the LSE Politics and Policy blog have both covered the Scottish independence referendum extensively, offering expert academic analysis of the economic, policy and geopolitical implications. This e-book aims to contribute further to debate about the much discussed question: how much will it cost to transition to a new Scottish state?

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Published by Democratic Audit
And LSE Politics and Policy
Twitter: @democraticaudit
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Executive Summary

An independent Scotland would face immediate set-up costs of up to £200 million in creating new administrative structures that duplicate UK institutions, but could also streamline many public bodies. During the transition process, the Scottish government could agree contracts or service deals with London to maintain existing back office support system (mainly involving IT) in collecting taxes, paying benefits and organizing complex defence systems. In the medium term (by 2018 to 2021) Scotland would need to build its own, new IT systems to allow policy control to be fully exercised from Edinburgh, in each of these areas. These tasks would certainly cost several hundred million pounds, but they would also be investments in modern systems, and not just “set up” costs. Significant policy savings may also accrue, and offset some of this burden.

A key influence on Scotland’s costs would be the conduct of negotiations between Scottish ministers and the remaining UK (rUK) government. A hostile approach by London ministers would force rapid changes and greatly add to Scotland’s costs. A more careful, phased approach would make these costs a lot less.

Every transition to a new state has some uncertainty and a degree of risk. But there are no bases for extreme anxiety about an independence transition in Scotland. The Scottish government’s record in public management is a good one, its published plans for transition are relatively specific and reasonable, and the long-run viability of a Scottish state looks strong. The main current uncertainties arise from the London government’s apparent reluctance to do any planning for, or to make clear to Scottish voters, how a transition to independence would be handled at their end.

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On 18 September this year, voters in Scotland face a momentous choice. Much of the discussion has been dominated by questions of economics, with bodies such as the London-based Institute for Fiscal Studies projecting public spending, tax receipts and GDP far into the future. And the Yes and No campaigns have swapped widely different economic pictures of the consequences of independence.

Yet many politically momentous events lie between now and these kinds of outcomes – not just the referendum itself, but also the writing of a Scottish constitution by a Constitutional Convention, the holding of the first post-independence general election, and the formation of a new Scottish government. Both the make-up of this Parliament and of the government may very well be different from the current SNP majority government. And of course, up to 2016, and long after that also, how Scotland progressively separates its government from the rest of the UK (hereafter, rUK) will be critical for the nascent Scottish state.

Above all, voters in Scotland are not choosing at the referendum what kind of economy to develop, or what kind of welfare state or tax regime to live under. Those decisions will come later and be decided or varied at multiple stages. At the independence vote the *only* choice on offer is about what kind of *state* to live under, whether the status quo of the current UK, or the model of a fully independent Scottish state offered by Alex Salmond and the Scottish government.

How the UK state operates is well known to Scotland's voters. But how would a Scottish state work? How costly would it be to establish new institutions in the short term? How feasible is the transition process proposed? And how long would it take, and at what cost, to achieve the separation of Scottish governance completely from the UK? Above all, what are the long-term prospects for a Scottish state? How viable could it be, and where would it face its greatest challenges?

These issues have only so far been addressed in the Scottish government's White Paper [Scotland's Future](#) (in a rather fragmented way), and in a series of UK civil service briefings discussing various detailed problems that an independent Scotland might face. The public debate has not really addressed these issues in a clear way. A UK Treasury briefing in late May 2014 did not help, containing as it did some spectacularly wrong information, which greatly muddied the waters.

A subsequent rather visceral debate has been dominated by the pursuit of information from the Scottish government on the alleged 'set-up costs' of independence. Both the unionist parties in the Scottish Parliament, and UK ministers like Danny Alexander, have demanded that Alex Salmond produce cost data for things that could only have numbers attached to them by someone with the prophetic powers of the Delphi oracle.

What we try to do here instead is to show what definite costs we can estimate will be incurred in the short term – these are genuine "set-up costs". We also look at the longer term costs of achieving a transition to Scottish independence – using the timetables and commitments included in the Scottish government's White Paper (which are the only ones available).¹ Finally we offer voters a detailed estimate of the longer term viability of the Scottish state, based on the most up to date research in state theory.

¹ There are grounds for arguing that the swift transition envisaged from a Yes vote to an independent Scotland by March 2016 is unrealistic or unlikely to happen, and that some of the other, later timings envisaged would benefit from longer phasing. But so far the UK government has not made such arguments – only insisted that voters in Scotland will say No, and so the issues here are academic.

1. The key tasks in achieving a smooth transition

The Scottish government have pledged to voters that their top priority will be to achieve a smooth transition to independence by March 2016. What that means in concrete terms is summed up in Figure 1 where the seven really big things Scotland must do for itself are in the left-hand column.

Figure 1: Major new departments or capabilities needed in an independent Scotland

New Top-level departments or agencies needed	Other Scottish equivalent agencies needed (or radical expansion of existing functions)
Defence Department plus Scottish Defence Force	Single Economic Regulator (covering a wide range of markets)
Scottish Security and Intelligence Agency	Scottish Debt Management Office
Foreign Affairs department, plus Embassies and diplomatic service	Rural Payments Agency, and agriculture policy-making competency
Scottish Revenue	Expanded Government Procurement capability
Scottish version of Department of Work and Pensions (hereafter, DWP)	Scottish Export Finance capability
Scottish Passport Office	Civil Aviation Authority equivalent
	Oil and Pipelines Agency capability
<i>Contested need for: Scottish central bank</i>	BBC or Public broadcasting capability

The kernel of a new Scottish Defence Force (incorporating army, navy and air force units) would need to be established. This will probably include around 10,000 personnel, plus a new Defence Directorate inside the Scottish government, perhaps involving around 3,000 staff (current Ministry of Defence staff in Scotland is somewhat more than this).

A new, integrated Scottish Security and Intelligence Agency (SSIA) would need to be set up also, covering internal security, overseas intelligence gathering and electronic and cyber security. Following the Scandinavian pattern, it would work closely the national police force for Scotland, already established by the SNP government.

Scotland would also need to create a foreign ministry and a core group of overseas embassies covering major countries, probably building out from existing overseas Scottish government offices. A full embassy network covering about 50 countries would come later. Initially many Scottish embassies might sit in UK or other EU countries' embassies.

These are the only brand new agencies that Scotland will need. But in addition a large number of staff would transfer from the UK to the Scottish government. Just under 8,000 people work for the UK’s tax agency HMRC in Scotland (not all on Scottish taxes) – they would need to be incorporated into a greatly expanded Scottish Finance and Economy directorate.

Some 9,500 staff work for the UK’s Department of Work and Pensions in Scotland, again not all on Scottish benefits alone. They would come under a greatly expanded Scottish government directorate covering social welfare alongside wellbeing and NHS in Scotland (already devolved).

And finally the currently beleaguered UK Passport Office would need to transfer its Glasgow staff over to Scottish government control.

Of course, modern government is not just about central government departments directly controlled by ministers. A lot of routine or technical work also goes on in agencies, separated from main departments, or in arms-length public bodies handling professional issues that we don’t want ministers to interfere in directly. So the big changes above are only part of the picture, and the rest is shown in the first two columns of Figure 2.

Figure 2: Assessing the overall scale of reorganization involved in creating an independent Scotland state

<i>Types of organizations</i>	<i>UK bodies relevant to Scotland</i>	<i>Scottish bodies needed</i>
Top-level departments/agencies	8	6
Other major bodies	6	6
Medium scale bodies	49	40
Small or tiny bodies	61	45
Already operating on shared basis	39	
Clearly or probably not needed	43	
<i>Total bodies</i>	<i>206</i>	<i>136</i>

Source: LSE Public Policy Group analysis of bodies listed at <https://www.gov.uk/government/publications/uk-public-bodies-that-operate-in-scotland>

This covers 206 departments, agencies and bodies that the UK government says currently handle Scotland matters. We have categorized these organizations as shown. The medium scale bodies spend some significant amount of money or implement services. The small or tiny bodies make up a third of the total – they do specialist tasks, or are just advisory committees. Many bodies are already operating on a shared basis with Scotland’s devolved government and so do not need major reorganization, as with most UK-level NHS bodies.

Much of UK government is highly elaborate and long-lived, however – so it is not at all clear that a Scottish government would need all these bodies. In fact, we have carefully considered the full list and concluded that 43 of them would not need Scottish government equivalents. We are also clear in some cases that issues handled by multiple bodies at UK level would require only one Scottish body.

Our judgements in Figure 2 are not in any way the official choices of the Scottish government – but they do at least suggest that there is a considerable scope for ‘streamlining’ what gets done north of the border, compared to UK practice. In fact, we think that the 206 bodies listed would need no more than 136 Scottish bodies, of which less than 60 would be new and of any significant size at all.

What will all this mean for central government within Scotland? Figure 3 shows that there is a big change in the scale of civil service, but not that much change in how it operates.

Figure 3: The transformation of Scotland’s central government

Scottish government now
 – Six directorates, with 5,000 civil servants

Permanent Secretary			Joint services		
Strategy & External Affairs	Finance	Communities	Learning & Justice	Enterprise, Environment, Innovation	Health & social care

Scottish government in 2016
 – Nine directorates, with perhaps 27,000 civil servants

Office of the First Minister (including transition issues)	Finance and the Economy	Health, Wellbeing and Social Welfare	Education, Skills and Employment	Law Officers
Justice, Security and Home Affairs	Environment, Rural Scotland, Energy and Resources	Culture, Communications and Digital	International Relations and Defence	

Currently the policy-making Scottish government operates with just 5,000 civil servants, using a modern and effective way of organizing called ‘directorates’, devised by Sir John Eldridge. In contrast to the deeply embedded ‘silos’ of Whitehall departments, Scottish government is currently run as a single organization using the same human resources and IT systems, but with six directorates. Beyond this core, there are other major agencies doing discrete tasks (like the Scottish prisons) that are separately managed.

Each of the Scottish directorates usually works for several ministers with different policy briefs. The most senior ministers are called Cabinet Secretaries and always attend cabinet, while other ministers go as needed based on the day’s business. Most current Scottish cabinet meetings have around ten ministers present, and there are only a couple of sub-committees. This has proved a very effective pattern of government, with staff numbers held down, spending controls well managed and policy development generally at least as good as that in the UK.

After independence the Scottish government plan to maintain their directorates, but to enlarge the number from five to nine, with the First Minister running a small policy directorate handling transition negotiations, and eight others. One of these will be wholly new (covering defence and foreign affairs). Three others are greatly expanded but drawing on some existing experience (foreign affairs, finance and tax, and social security). On the face of it, these plans are clear and modest, drawing on existing strengths and developing them.

The Scottish cabinet would also be somewhat bigger, with probably around 15 people sitting around the table from 2016 instead of ten, and somewhat more sub-committees. But compared with all other OECD governments, which generally have around 15 separate ministries, Scotland’s nine directorates answering to around 9 top rank Cabinet Secretaries (and more ministers) still looks lean. It contrasts with the UK government that includes 120 ministers, with a cabinet of now 25.

2. The timetable of transition

The single best attested lesson of all public management is that the costs (and other risks) of a speedy or forced transition are always greater than those changes that are properly planned, trialled and phased, so that effective implementation can take place at each stage.

In a 2010 study we undertook of changes to Whitehall departments across 30 years we heard many horror stories of the incredible behaviour of UK Prime Ministers in forcing through badly designed changes of departments over a weekend. In one extreme case a top minister was two minutes away from arriving at his new department during a cabinet reshuffle and Whitehall reorganization, when the department was suddenly merged by the PM with another one. The minister had to be made Foreign Secretary to compensate him for the shock of it all. Especially under Tony Blair and Gordon Brown the pace of Whitehall changes became severely dysfunctional.

In the Scottish case the government has actually set out in its White Paper a reasonable timetable for implementing changes, shown in Figure 4. The key decision that Salmond and colleagues have made is to move rather briskly from a Yes vote to independence, but to focus on just the key tasks already set out above. By 2016 Scotland will have policy control of some of the biggest issues, but even in defence its capability will only just be beginning, and no complete separation from UK systems is envisaged.

Even in important areas like defence planning, back office and procurement, and some taxes, it will take a considerable time for Scotland to build up its own systems. And in some technical areas, that matter a lot less for Scottish policymaking, the transition will take more than seven years. For instance, Figure 4 shows that the registering of vehicles and licensing of drivers carried out by DVLA and three other UK agencies will continue to be based in Swansea until at least 2021.

So what would happen with things that have not been moved over to full Scottish control? The Scottish government will obviously want to brand and manage all its communications with citizens – so websites and forms would now carry the Saltire and contact details for staff based in Scotland. But behind the scenes, for some years the ‘back office’ systems for both tax systems and benefits would need to run through the existing, very complicated computer and IT set-ups in the HMRC and DWP. And only when these systems were fully replaced with new Scottish ones would ministers in Edinburgh gain the full freedom to vary benefits for Scottish citizens (planned for 2018) and personal taxes in Scotland (planned for 2020).

Throughout these longer transition periods then, how would Scotland continue to get the continuing services it needs from Whitehall? The details would need to be negotiated with the rUK, but in every case Scotland would have to pay the existing costs for these services, plus a small addition:

- Either via a *financial agreement* between the two governments for whole sets of services to be provided. This would be the cheapest to agree on.
- Or by Scotland *contracting* with the UK to get specific tasks carried out. This could be somewhat more expensive, since writing contracts in detail and then monitoring performance adds to costs.
- Or by Scotland *leasing* whole sets of equipment, and even associated operating staff and support staff, for defined periods of time.

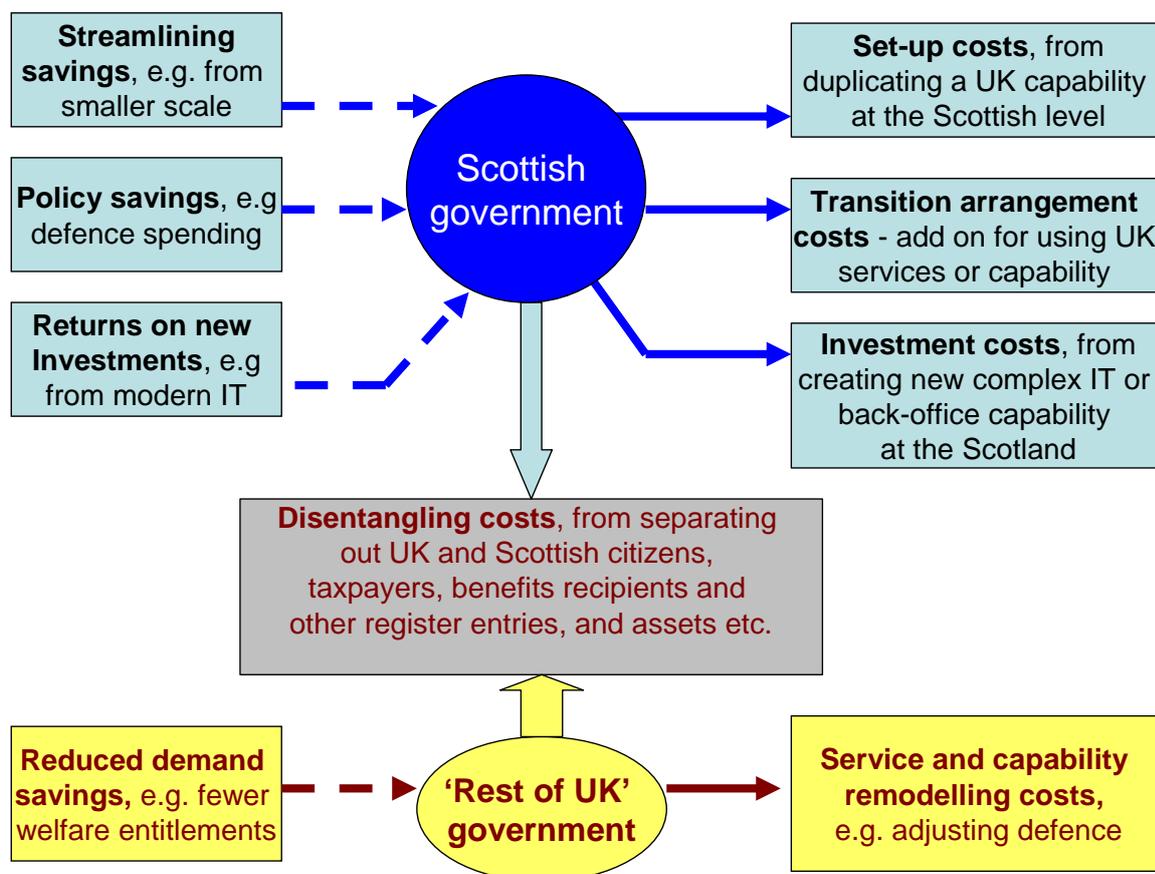
Figure 4: Timetable for the handover of functions to a Scottish state

Date	Major changes
18 September 2014	Work begins on creating the Scottish Security and Intelligence Agency, the Scottish Defence Force and Defence policy capability, and a foreign ministry and embassy network
September 2014 to 2015	Work on Scottish Constitutional Convention and on handover of staff, assets and transition arrangements
Early 2015	Scottish government reorganized into nine directorates
24 March 2016	First election to independent Scotland Parliament. New government formed and announces policies for tax and welfare, plus priorities for transition.
	Scottish Security and Intelligence Agency takes over most responsibilities from rUK counterparts
	Scottish Defence Force in being with initial set of forces and agreed co-financing of some rUK services
	Scottish Defence Department capability operating, and growing Scottish foreign ministry in being and foreign service operating in around 50 countries initially
By end 2018	Scottish directorate assumes full control over Scotland welfare benefits system, including new IT systems
April 2020	Scottish Revenue now has full control of personal income taxes system in Scotland, including new IT systems
	Scottish Defence Force nearing permanent configuration. Defence hierarchy and directorate has full control (or a full role in joint NATO control) of all essential systems
May 2020	Second election to independent Scotland Parliament. New government formed and announces policies.
2022	Scottish Motor Services Agency takes over DVLA and other UK motor related regulatory functions
2020-22	Remaining tax functions and IT systems now fully controlled by Scottish Revenue

3. The costs of transition (and possible offsetting savings)

The current debate about ‘set up costs’ for a Scottish state has been marked by the UK Treasury lumping together and in some cases grossly over-stating a range of very disparate kinds of administrative costs (and potential savings). As Figure 5 shows there are five main types of costs (and also potential savings) involved for Scotland here.

Figure 5: The main types of costs (and offsetting savings) borne by Scotland and the rest of the UK during Scotland’s transition to independence



Source: PPG discussion with Scottish Government and Treasury officials

Set-up costs

are those incurred by Scotland only, in the early transition period (especially from a Yes vote to March 2016) in duplicating a capacity that already exists in the UK. These costs are unavoidable, one-off costs of transition that create no additional or offsetting welfare gain for Scotland's citizens. It's important to note that set-up costs are just any increment *added on* to the existing costs of running equivalent UK services in or for Scotland. They cover just the legal costs of setting up a department, agency or public body, and any extra initial accommodation/IT costs, plus hiring in staff not needed before. They don't cover the costs already incurred by the UK on running things in Scotland, because these costs are already being paid for by Scottish taxpayers. Most set-up costs will arise in defence, foreign affairs, tax and benefits. Based on detailed work on the costs of Whitehall reorganizations, and our analysis of major tasks set out above, we have estimated the set-up costs for Scottish government as being in the range from £150 million to £200 million – that is £30 to £40 per person.

By the same token, if Scotland can do the job the UK apparatus does with fewer or smaller bodies, then it can generate *streamlining savings* (to offset the set-up costs) of the kind outlined in Figure 2.

Disentangling costs

arise because current UK-run processes treat Scotland and rUK citizens in a merged way. Following a Yes vote, governments on *both sides* of the border will need to de-merge data about citizens, taxpayers, benefits claimants, business taxpayers and so on, and perhaps change some back-office operational processes so as to re-allocate them. The rational thing for both Scotland and London governments is do each of these tasks only once, so that the costs involved would be shared between them. How would the costs be allocated here? A good deal for Scotland would be its share of total UK population, where it might pay 10% and rUK 90% of the cost. A good sharing outcome for London would be a 50:50 deal. The differences here are large - so negotiation are crucial to the eventual number of Scotland's costs here. Disentangling will likely generate some future savings by up-dating, modernizing, cleaning and authenticating data registers.

Transition costs

occur, as discussed above, when Scotland negotiates or contracts with rUK to keep doing part of processes that would cost too much to change during the transition period. Notice here though that only the *extra* cost of the contract negotiation and monitoring are new burdens borne by Scottish taxpayers – with unchanged systems the main bulk of services costs will be the same after independence as they were before.

Investment costs

have to be borne by Scotland in order for its policy makers to gain full control over the tax, benefits and defence areas, running all the back-office systems in a self-sufficient way. When the new Scottish government and Parliament has designed their tax and welfare policies for the long term, then Scotland can invest in modernized, purpose-built ICT and administration to permanently replace UK provision. And as the Scottish Defence Force builds up, they too can take over their own command and control, procurement and other complex back office functions.

The UK Treasury has not given any specific numbers for defence, but they have put forward some large numbers about two other areas. They say:

- the Scottish government would need to pay £400 million to create new IT systems and processes to handle all welfare benefits itself – which is targeted to happen by 2018 (see timetable above); and

- they would need to pay £500 million to create IT systems capable of handling all their tax administration – the main bulk of which is due to happen by 2020.

These estimates are not based on any careful analysis, but given prevailing IT and change costs they do not seem implausible.

However, these are not just ‘set-up costs’, because Scotland would be replacing older and complex legacy IT systems in each case, with newer, modern IT systems that would last for a long time (at least 10 years), and could well be cheaper and far more flexible to operate. Hence these are investments (not just set-up expenses) – like replacing an old desktop PC with modern iPad. The further down the track such changes are made, and the more tailored new systems are to Scottish ministers’ plans and priorities for tax and welfare, the more they have an investment and modernizing character.

Bear in mind also that big scale IT systems and contracts run out all the time, and have to be renewed – and that in the past this has been a very costly and often rather shambolic process in UK government. Fully a half of all the UK’s major government IT contracts are up for renewal in the same period. So that Scottish taxpayers may well have to pay for much the same modernization spending, whether the nation votes Yes or No.

Finally, there is good evidence around the world that supplying government IT is generally cheaper and more effective in small states of around 5 to 10 million people, than it is at UK scale (for 63 million people). New Scottish systems might well be smaller, more flexible and more modern than those in the UK – as they clearly are in Sweden, for instance.

Policy cost savings

would accrue to Scotland if they no longer needed to cover costs that have to be covered so long as they are in the UK, such as, the costs of running nuclear weapons systems. In 2013-14 the UK Ministry of Defence had costs of £47 billion (i.e. £thousand million), a sixth on which was capital spending, and the vast bulk on gross operating costs. The Scottish government anticipates spending only £2.5 billion a year on defence and intelligence combined. This is a lot less than Scotland’s population-proportional share of around £4 billion a year for MoD costs. Cumulated over a decade, such policy savings might quickly dwarf set-up costs.

On the other hand, the Treasury argues that a leaked paper from Scotland’s finance minister, John Swinney, included a passage estimated that the annual costs of running the Scottish tax systems would be around £600 million a year. This is actually far higher than Scotland’s population-proportional share of HMRC costs, which would be around £300 million. The evidence basis for the Swinney estimate seems to have been slender, derived from looking at the proportion of GDP spent on tax collection in Ireland and New Zealand. It seems highly unlikely that Scotland would need to double HMRC’s costs. For instance, in taking on collecting a version of stamp duty and landfill tax Revenue Scotland recently considered a bid from HMRC, but decided it could do the job more effectively and cheaply on its own. So it is possible the £600 million number in the Swinney memo is itself just a mistake.

Similarly there are one or two cases where the UK government has successfully pointed to higher *transactions costs*, a burden that would recur with each passing year. The most serious concerns the current easy co-operation between police forces on both sides of the border in pursuing and arresting criminals throughout the UK. After independence, current practice would become more cumbersome. English police forces pursuing criminals who have fled to Scotland would need to apply for European Arrest Warrants

(assuming that Scotland remains in the EU) to get them back, and vice versa for Scottish police pursuing suspects in England or Wales. At present the UK processes with other EU countries take a longer time and cost more to do. But since Scottish and rUK legal systems are much closer in their operations, the same might not be true with EAWs between the two. Similarly, it would be open to policy-makers on both sides of the border to consider new joint legislation to solve these problems if they proved serious.

Finally, for completeness, an immediately successful Scottish state might face burdens from its own success. For instance, around 700,000 people born in Scotland now live in England, and are entitled to Scottish citizenship. If a lot of them were to apply for Scottish citizenship in 2016-17 the new Scottish Passport Office could confront major initial problems in getting to a stable initial configuration for their staffing and IT systems.

4. Key examples of costs (and savings)

To get more of an idea of the practical problems involved in the transition, we briefly discuss some key examples.

The *Scottish Security and Intelligence Agency (SSIA)* is a priority area of spending for the Scottish government in 2014-16, and for the early years of independence (when Scotland may have difficulties spending its budget for defence). The new agency would replace three UK agencies in Scotland – MI5 handling internal security; SIS doing overseas espionage; and GCHQ doing electronic eavesdropping. In its early years the new agency would no doubt work closely with these rUK counterparts. And there are strong reasons on both sides of the border why intelligence co-operation should be good, e.g. on countering terrorist threats.

But the SSIA would also need to prove that it could be a reliable partner for intelligence agencies in the UK, and other countries like the USA, Canada, Australia and New Zealand (who form the “five eyes” collaboration network). Until SSIA could prove that it could keep important secrets and also generate reliable intelligence information of its own, it could not be a part of these links on the same basis as the UK. The operations of the Scottish constitution in intelligence matters would also need to be established. Perhaps five years of effective operation would be needed for this situation to change

On the other hand, Scotland’s risk profile in the intelligence area might well be much reduced compared to that of the UK. The Scottish government could draw on some significant talent in this area. And to start well it could afford to offer good pay and interesting opportunities to attract high calibre staff, and to fund state of the art equipment and facilities while its defence spending is building up. Finally Scotland’s national police force means that the SSIA would need to do a good deal less than MI5 in terms of homeland security.

The *Scottish Defence Force and Defence Directorate* would have perhaps the hardest tasks of any. Scotland’s defence needs are heavily concentrated in capital intensive areas of spending, a navy to patrol its long coastline and extensive sea areas and oilfields, and an airforce to cover the country’s huge land mass and big northern air sector. The Scottish government envisage starting out with essentially two frigates and one fast jet squadron and a maritime patrol capability, and with a small army. Over the first term of the new Scottish parliament to 2020, these capacities would essentially double in size, and Scotland

would progressively take over (or integrate within joint or NATO structures) more of the command and control, back office and procurement systems from rUK's Ministry of Defence.

The Scottish *Foreign Affairs* directorate would build on the existing small external affairs capability, and could draw immediately on an existing overseas network of 27 Scottish trade delegations, many of which might be upgraded into embassies. The priority for overseas representation would be for Scotland to start out with key representation in international organizations, such as the European Union, NATO, the United Nations and so on. There would be complex negotiations to secure Scotland's place in the EU and NATO, and the Scottish government could not assume that these would be easily or routinely assured. Equally appointing key ambassadors and getting overseas representation in 50 main countries would be a considerable challenge, but one for which Scotland could draw on an extensive talent pool.

Taxes and benefits In many ways the most important problems might not lie with the brand new Scottish functions. Instead they might occur in the directorates controlling tax and social security, which would have large and often senior staffs used to the UK way of doing things, and not used to the Scottish government's organization patterns and culture. As with many company mergers, getting new and old organizational cultures to mesh together could be a challenge.

However, *Scottish Revenue* already exists as a new unit in Edinburgh and has already taken over the collection of a land fill tax and stamp duty equivalent. Equally, on benefits Scottish local authorities already handle all the administration of one of the most complex and costly of all welfare payments, namely housing benefits.

The *Debt Management Office for Scotland* is an example of a smaller agency that none the less has a key function. In addition to taxes, states raise long-run borrowing by issuing bonds in financial markets, especially to fund investment spending and capital projects. The Scottish government intends to take on a share of the UK's national debt (the size to be negotiated) and its DMO would at first undertake repayments and financing of these past liabilities. As it establishes a sound reputation in bond markets, and begins paying down its share of UK liabilities, so the DMO would be able to begin issuing new Scottish debt. Scotland has a great deal of financial expertise to draw on here.

On the wider range of *public bodies* it is worth looking at just a couple of examples. First, to fund university research projects, the UK runs six different research councils, four in the sciences, one each for social sciences and the humanities, and one to do the biggest capital projects. In Sweden by contrast (twice as large as Scotland) there is just a single Research Council that runs all the same functions as the UK in one organization. This is an example of a medium size agency remodelling and the streamlining that should be feasible with a fresh canvas.

Second, take a small public body like the Electoral Commission, which has a budget of £21 million and registers political parties and supervises how elections are conducted. Scotland would need only a very small equivalent body, a set of commissioners and a small staff, perhaps costing £2 million a year to run. There would be some set-up costs here, but they would be tiny – as for most of the public bodies covered in Figure 2 above.

5. Scotland's assets (and liabilities)

Before we leave financial numbers behind for broader issues, it is worth noting that after a Yes vote there would also have to be important negotiations between Scotland and London to divide up UK public assets (and also government liabilities like the national debt and pension costs). The general principles here are clear:

- Fixed assets (land, buildings etc.) will generally 'lie where they fall', so that Scotland would acquire at zero cost all the UK government buildings, bases and land etc. within Scotland's boundaries.
- Unfixed assets, and fixed assets located overseas outside the UK, would have to be divided and Scotland given a cash amount by rUK to compensate it for that share. What would the sharing arrangement be? It could be population proportional, with Scotland gaining 1/12th of the total. Scotland will seek to make a case for a higher share, recognizing the past importance of North Sea oil in creating the assets involved.

Some Yes campaign arguments have tended to link the issue of transition costs to Scotland accruing large-scale asset values. However, the point of government assets is to back up (provide a surety for) Scotland's future ability to raise long-run government funding and undertake borrowing on bond markets at reasonable costs. Linking assets gains to transition costs tends to undermine that connection of assets to long-run government funding potential. It might suggest that the process of independence would lead to an imprudent diminution of public assets to meet one-off needs (similar to financing current spending by means of asset sales).

Hence, the costs of transition and the dividing of assets should *never* be linked. Transition costs can be offset by savings in running costs (through streamlining, sound investment and modernization) and policy savings. Any cash-value receipts from rUK in respect of assets should be dedicated to long-run reinvestment that adds to Scotland's overall asset base for the future – perhaps via a dedicated fund, or even a sovereign wealth fund?

6. The importance of the post-referendum negotiations

When a UK general election looms, all the main parties with a chance of being in government get a degree of access to the civil service, and to government documents and statistics, so that they can be briefed on the realities they would face, should they come to power. The aim is to help them put well-costed policies in place, before they begin making election promises to voters.

Unfortunately, there has been no equivalent process for Scotland's referendum, despite its momentous implications. Westminster ministers have instead given no information at all to the Scottish government or their officials. Whitehall has been forbidden to discuss issues with Scottish officials and to do any contingency planning for independence, in case the conclusions suggest independence would not cause major problems. (The only exception here is the Bank of England, where Mervyn King gave permission for its officials to hold technical discussions with Scottish planners.)

Yet most of the information needed to understand the transition costs for an independent Scotland lies not in Edinburgh, but in London, where the reserved functions are administered. Indeed, how could it be

otherwise? By definition, none of the Scottish government's 5,000 civil servants is an expert in defence spending, or running a full-spectrum diplomatic service, or designing and contracting for complex IT systems in policy fields for which Scotland has no legal standing at present. The Scottish government has hired some generalist planners, and convened some strong expert committees to prepare for transition, but without having detailed information or interactions with Whitehall.

Ironically too, UK ministers like Danny Alexander, and unionist parties in the Scottish Parliament, have repeatedly pressed the Scottish government to specify transition costs that are many years down the track and will depend extensively on:

- how Scottish voters choose MSPs in 2016;
- which government is formed then;
- what policy decisions Scottish MPs then make.

Most important of all, these transition costs depend very heavily not just on the Scottish government, but on how the rUK conducts negotiations. London ministers could take a hard line that apparently cares little or nothing for the future welfare of Scottish citizens (as perhaps with their declared stance on monetary union). This would force through a complete transition quickly – even though such a course damages the rUK itself economically, maximizes costs in rUK government, and creates risks for rUK citizens. In this case Scotland's transition costs would be much higher, and the risks of service gaps opening up would be greater.

Yet if negotiations do become a tough poker game, the Scottish government still has some big chips that it might play. For instance, Alex Salmond has insisted that the Faslane nuclear submarine base must close by 2020 – which he must know is an infeasible deadline for the rUK's Ministry of Defence to meet. Similarly, the UK government has already had to announce to bond markets that in the event of Scottish independence it guarantees the whole of the UK's existing public debt – so that (in theory) Scotland could launch debt-free as a nation.

Alternatively, in negotiations London ministers could agree to share services with Scotland during a well-phased and jointly planned transition period, disentangling services in an orderly sequence, with Scotland meeting the interim costs to UK taxpayers. This is what the Scottish government's planning and White Paper essentially assumes. In this case Scotland's transition costs would be much lower. It would have to spend mainly on new investments rather than on 'set-up costs', and the continuity of key services would be much better assured.

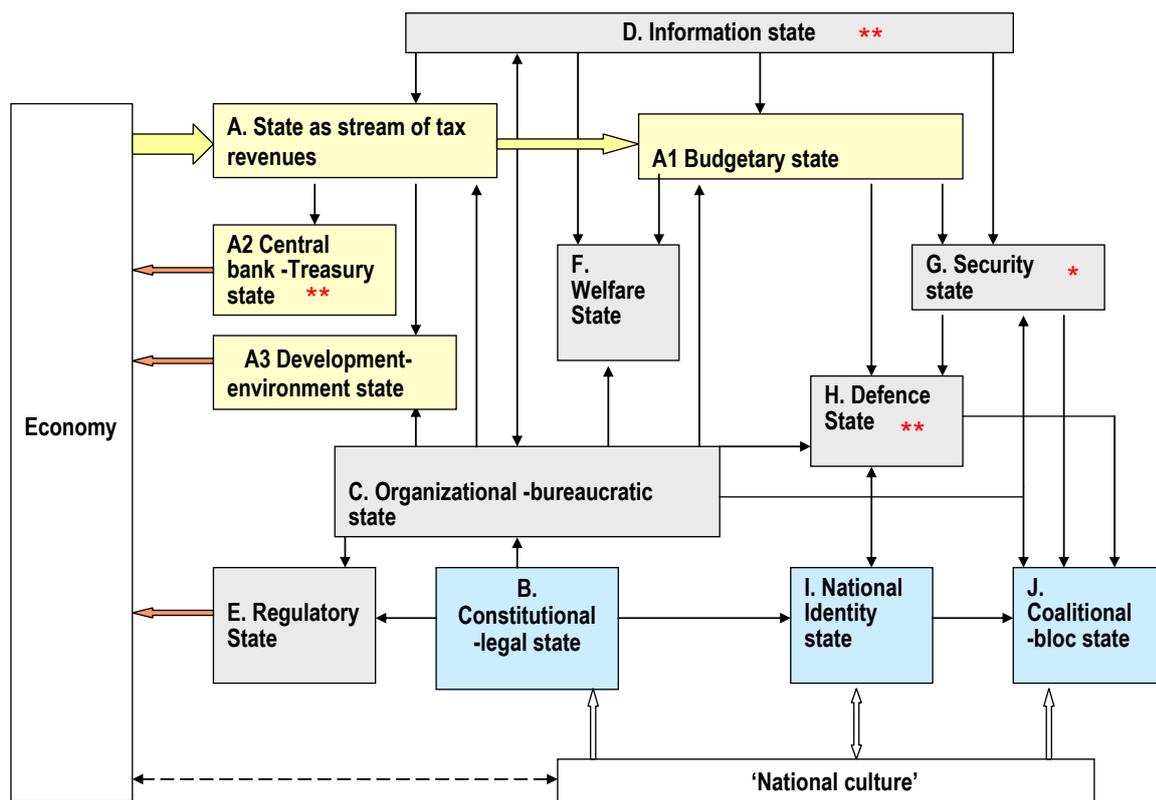
Voters in Scotland will need to make up their own minds how they believe that things will play out in negotiations if Scotland votes Yes. Perhaps with the closing of some opinion polls, the time is also overdue for UK ministers to come clean on what exactly London's stance would be if Scotland's voters do decide to choose independence.

7. The long-run viability of a Scottish state

Over many decades, how a state is set-up and how it works can have enormous implications for its society and economic well-being. In 1900 Argentina was one of two states with the highest levels of GDP per head in the world (the other was Australia). Yet decades of political corruption, Peronism, military coups and dictatorships and strong social inequality saw Argentina tumble down the GDP rankings throughout most of the twentieth century.

Modern political science shows that running an advanced state now involves all the thirteen critically important functions shown in Figure 6. All of these components must be in place if the state is to succeed and flourish. In Scotland’s case most of the boxes already look fine. Those that remain to be established are shown by one star (denoting some extra capacity needed) or two stars (denoting major capacity needed). We comment briefly on each of the elements.

Figure 6: Thirteen essential features of statehood – and the areas where Scotland needs to build up (shown by *s)



Notes: ** Large capability gap to be made up in Scottish government * Some capability improvement needed in Scotland
 Source: P. Dunleavy, 2014. Available at: <http://eprints.lse.ac.uk/56492/>

A. The state as a stream of tax revenues underpins everything a government machine does. In Scotland's case the Scottish accountants (ICAS) have produced a long academic report dwelling in a rather vague way on the complexities of running a tax system. But with a stable UK tax regime in place in the country for many decades, and plenty of strong expertise for the Scottish government to draw on, there seems every reason to believe that Scotland's revenue stream will continue as before. Indeed 'tax morale' (the willingness of citizens or businesses to pay taxes) is likely to rise after independence.

A1 The budgetary state concerns a government's success in keeping spending in line with taxes and revenues for the long term. Scotland's record under devolution has been careful and financial planning has been accurate. The relatively small addition of functions is unlikely to make any difference here, except in the defence area where procurement creates some new risks that will need to be carefully managed by the 2020s.

A2 The central bank-Treasury state covers the behaviour of states in issuing debt, managing their monetary affairs and guarding against systemic risks (such as the 2008 financial crash and recession). The Scottish government have successfully addressed the debt management issue, but proposes to rely on the Bank of England still for central bank functions. This can only work if London ministers have strong confidence that Scotland has the self-same efficacy in guarding against creating systemic risks of bank collapses and financial instability as the remaining UK does.

A3 The development and environment state shapes both economic growth through infrastructure and environmental performance. Scotland has a good existing record on both fronts. If Scottish citizens become sole guardians of their world-famous environment we might expect 'green' consciousness and performance to improve relative to that of rUK.

B. The constitutional-legal state shapes how its institutions and operation evolve. Scotland already has very strong rule of law and constitutionalism traditions, a strong concentration of legal expertise and excellent courts and judges. Its Parliament and government institutions are modern and based on proportional representation. Its local government (previously often one-party controlled and sometimes somewhat corrupt) has also been modernized by PR elections. The new written constitution to be defined by a Constitutional Convention should mean an independent Scotland has a top rating here.

C. The organizational-bureaucratic state is also strong in Scotland, with strong public service and political impartiality traditions that have been stable for generations. Since devolution, governance arrangements have been stable and generally successful, with far less of the incessant 'reform churn' in England. Scotland has generally higher civil service morale (due to no redundancy guarantees in Scottish government), and a good overall record of maintaining efficiency, reducing public bodies and service modernizations (like the national police force). There seems every reason for this to continue.

D. The information state is crucial to modern public management, and the devolved government's performance has generally been solid if not spectacular. As we have seen, in taxation, benefits and defence a new Scottish state has key challenges to meet as discussed above, but also important opportunity to put in place more modern and flexible systems. For comparison, the UK's record on government IT over in recent decades has been poor, with complex, legacy IT systems, high costs and major cancellations and policy disasters – most recently on Universal Credit.

E. The regulatory state is well set-up in Scotland for almost all social and economic issues, reflecting its legal soundness and public service strengths. The Scottish government proposes to establish a single economic regulator, which should cut costs and improve policy cohesion. The only area of weakness concerns financial system macro-regulation (see A3 above).

F. The welfare state in Scotland is already mostly operated by the devolved government, drawing on strong UK traditions and with some modernization. Handling social security raises some new IT challenges and policy issues, but the DWP local offices on the ground will transfer across. Welfare issues become somewhat less complex at a smaller scale and in a more defined set of area contexts.

G. The security state is well established on the policing front, aided by recent reforms. Creating a new intelligence agency, and then developing its international reputation to grow co-operation with other countries are key challenges for an independent Scotland discussed above. The new written constitution might constrain the agency's efficacy. Alternatively, it might help citizen and business confidence, by resolving the myriad privacy rights etc left largely unresolved in the UK's uncodified constitution.

H. The defence state is the most important area where a new Scottish government needs to prove itself. Attracting service personnel to a smaller, integrated defence force may pose difficulties. Yet Scotland can also draw on strong military traditions and a considerable pool of talent and motivation.

I. The national identity state is crucially important for the coherence of a society around its governing system. Scotland's existing sense of national and identity is very strong indeed, with a distinctive social culture that is world famous and a characteristic politics with limited internal factionalism. Key unifying institutions, such as the monarchy, would remain. The likelihood seems strong also that after a somewhat divisive referendum campaign, Scots would strongly pull together in the event of a Yes vote.

J. The coalitional-bloc state is vitally important in modern world affairs, especially so for smaller states. Although great power incursions in Europe had seemed to largely recede, the recent Russian occupation of Crimea and destabilization of Ukraine over a long period show that significant threats remain for any isolated state, even in the modern world system. Scotland, however, has strong alliance positions within the EU and NATO, that will need to be renegotiated, but do not seem to be in any long term doubt

Summing up across all these dimensions, the future viability of a Scottish state generally seems high. Once some limited new capacities are developed, the prospects seem set fair for generally good governance over the long term.

Conclusions

We can say with some confidence that Scotland's immediate set-up costs are likely to be constrained – perhaps up to £200 million in creating new versions of a few but big existing UK department capabilities.

Beyond that, the UK Treasury has cited a report based on Canadian studies that suggests a range of other transition costs – from as little as £600 million at the low end (0.4 of 1 per cent of Scotland's GDP), up to £1.5 billion (1% of Scottish GDP) at the high end. This is a very wide margin, and the study itself was of Quebec some years ago, and not of Scotland now.

The UK Treasury has also suggested that Scotland could face disentangling costs, IT and new administration costs in taxation and benefits of perhaps as much as £900 million. But if anything like these amounts were to be incurred, it would be in a phased way by the Scottish government creating new and modernized IT and administrative systems that would endure for many years. They hence take on the character of investments, where future running cost savings would also be sought.

Scotland's transition costs are also likely to be significantly offset by:

- some significant 'streamlining' savings initially;
- the elimination of many 'legacy' complexities (such as the very tangled back-office computer networks in UK tax and benefits systems);
- the generally easier process of managing a smaller government machine;
- some substantial policy savings in areas such as defence.

The two absolutely critical influences on Scotland's likely transition costs are:

- the realism of Scottish government planning for independence, which generally seems high, but assumes a moderate and rationalist rUK stance; and
- the stance that London ministers would actually take in negotiations over the transition, which remains largely undefined.

The long-run viability of an independent Scottish state is generally high.