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Learning lessons for the future of devolved finance in the United Kingdom from its past: proposals and policies from Irish Home Rule to the devolution acts of 1998

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The process of devolution within the United Kingdom has led to increasing scrutiny of the method by which the devolved governments receive their financial resources. This is largely by grant allocation from central government in Westminster. Academic commentators and an increasingly large band of politicians of all hues have questioned whether it is appropriate for elected assemblies and a parliament to be funded in this way. Much of the attention turns understandably on the Barnett formula and its implications (see Midwinter (1999) and Bell (2000) for descriptions and analyses of the operation of the formula). Other works focus on alternatives to the Barnett formula, drawing both from economic theory and the experiences of other countries (Darby, Muscatelli and Roy, 2002; Hallwood and McDonald, 2004 & 2006; Steel Commission, 2006). This paper seeks to show what lessons can be learned from previous attempts to devolve power from Westminster to the nations, and in Northern Ireland's case the entity, that have formed the United Kingdom in its different guises. The rich history of proposals and policies concerning devolved finances within the United Kingdom has largely been ignored in the debate to date and yet it offers a bountiful source of information on the successes and failures of various finance systems. It has the crucial advantage of being set within the United Kingdom's constitutional constraints.

The proposal for Home Rule to Ireland in 1886 was the first legislative attempt at transferring responsibility within the United Kingdom from Westminster back to national capitals since the Acts of Union.[1] However, the process was not motivated by financial concerns. The appropriate devolution of powers and responsibilities was sought to solve some of the grievances of Ireland within the United Kingdom[2] and importantly to free Westminster to deal with what were considered more pressing matters of Empire: financial considerations, as will be seen in all subsequent devolution movements, only became important once the proposals were formulated, they hadn't driven its introduction. The granting of dominion and commonwealth status to Canada, Australia and New Zealand had demonstrated that orderly

[1] The previous year the Liberal government had introduced the Secretary of Scotland Act (1885) to provide a minister to carry out duties for Scotland that had previously been conducted by a number of ministries across Whitehall. However, the post was administrative and continued to be based in London until after it was elevated to that of a Secretary of State in 1926.

[2] The Disestablishment Act (1869) and Land Act (1870 &1881) had already been introduced in an attempt to solve long-standing concerns surrounding the position of the Church of Ireland and land ownership.

diminution of British authority within parts of the Empire was politically feasible under the correct conditions. However, Ireland was different. Ireland was represented in the Imperial Parliament at Westminster, it had been under British, and previously English, control for centuries, it now paid its taxes to London and had its spending authorised by it, but perhaps most importantly it was geographically close to Great Britain. This proximity determined not only the powers that could safely be devolved, but the visibility of the impact of any diminution, perceived or real, in the sovereignty of Westminster.

This paper examines proposals for devolution finance from Gladstone's first Home Rule Bill for Ireland in 1883, through to the successful devolution proposals of the late 1990s. It does not attempt to address why devolution was sought, but instead only to give that historical background necessary to understand the financial implications of the proposals.[3] Nor does it look at every suggested devolution scheme, but instead concentrates on the principle attempts to devolve power from Westminster. These are the Government of Ireland Bills of 1886 and 1893, the Government of Ireland Acts of 1914 and 1920, and especially how the 1920 Act compared with the reality of devolution finance in Northern Ireland until 1972[4,] , the Scotland and Wales Acts of 1978 and finally the successful devolution proposals enacted for Scotland, Wales and (intermittently) Northern Ireland in 1998.[5] The paper concludes with a discussion of what can be learned from the United Kingdom's experience of financial devolution.

Devolution for Ireland

The first Government of Ireland Bill was introduced to Parliament on 6th April 1886 and allowed for an Irish government to retain both direct and some indirect taxation gathered in Ireland. Customs and excise duties would continue to be set by Westminster, but all duty paid in Ireland, irrespective of where the goods were subsequently consumed, would be taken as revenue to Ireland. Taxes were to be paid

[3] There are numerous accounts and analyses of devolution within the UK that cover the history and politics of devolution. Excellent starting points are Bogdanor (2001), Jackson (2003) and O'Day (1998).
[4] Although the Parliament of Northern Ireland was suspended in 1972 the financial relations between Northern Ireland and the United Kingdom were those outlined in the Act until 1980, when the Barnett formula system replaced them.
[5] Devolution to London is not discussed because of its limited financial system.

to an Imperial Receiver[6] and an Ireland Consolidated Fund was to be established. All taxes raised in Ireland, whether set in Dublin or London were to be paid initially to an imperial fund in London. From this fund Ireland's Imperial contribution, a payment to represent Ireland's share of funding expenditure to maintain the empire, would be paid. The Bill made clear (s15&16) that the Imperial contribution was the first call on the Irish Consolidated Fund and that only the remainder would be available for expenditure by the Irish Government. The Imperial contribution was, however, to be fixed at its upper limit, although variable downwards, for thirty years following the introduction of the Act. This system led to two areas for financial debate: how much should be Ireland's Imperial contribution and how much taxation could Ireland raise?

After the Act of Union in 1801 there remained a separate exchequer for Ireland until 1817, after which there was only one exchequer for the whole of the United Kingdom – a situation that was to last until 1919 (Kendle, 1989). As a result there was no reliable estimate of the taxable capacity of Ireland and therefore no definite figures on which to base an appropriate Imperial contribution. A House of Commons committee was established in 1864 to inquire into Ireland's taxation, 'but it led to no useful result' (Whelby, 1971). Gladstone's initial view was that Ireland should contribute one-twelfth of imperial expenditure. A series of papers was prepared on Irish finance and recommended that something closer to one-twentieth was more appropriate. Gladstone finally accepted one-fifteenth, judging it important to set Ireland off on a sound financial footing, something he thought this financial concession would achieve (Loughlin, 1986, Welby, 1971)[7]. However, Parnell, the leader of the Irish Nationalists, believed that 'without a right budget all would go wrong from the start' (Loughlin, 1986, p69) and was determined that such a figure was unacceptable (Kendle, 1989).

The economist Robert Giffen believed not only that Ireland was over-taxed, to the extent that it paid twice as much in taxation as it should, but also that the government of Ireland incurred excessive expenditure, perhaps as much as £3m too much (Loughlin, 1986). Ireland's excessive expenditure was largely the result of managing

[6] This position was to be created under Gladstone's Land Purchase Bill, introduced in the same year, and a vital component of his home rule plans.

a difficult territory through an extensive administrative system backed by the Royal Irish Constabulary. Excessive taxation, as far as Giffen was concerned, was a combination of poverty and inappropriate tax bases and rates.

Following the amalgamation of Exchequers in 1817 there had been a movement, although a slow one, towards harmonisation of fiscal policy as between Great Britain and Ireland. However there were a multitude of cases where taxes either did not apply in one country while being applied in another, or were applied at a lower rate in Ireland than in Great Britain.[8] The impact of this was not clear because separate revenue accounts were not gathered, but was likely to be felt especially in excise and duty on consumables, which in Ireland represented a higher share of aggregate household expenditure than was the case in Great Britain.

However, Giffen's concerns over Gladstone's plans were based on the belief that Ireland's revenues and expenditures would be similar to those outlined in the Bill. This would appear not to have been Gladstone's intent since the Bill contained a number of features, or perhaps more accurately financial fixes, to Ireland's benefit (Whelby, 1971). But these ultimately created deep flaws within the system.

The Imperial contribution within the Bill (s 13(1)) was to consist of £1,466,000 towards the national debt, £1,666,000 to the army and navy, £110,000 towards the imperial civil expenditure of the United Kingdom, £360,000 as a sinking fund for capital debt and £1m for the Royal Irish Constabulary and the Dublin Metropolitan Police. While not mentioned in the Bill, Irish civil charges were reckoned at £2,510,000 with £834,000 estimated as the cost of revenue collection. Total expenditure was expected to be £7,946,000. Revenue was forecast to be £6,180,000 for imperial taxes, £1,150,000 in Irish taxes and £1,020,000 in Post Office receipts. This meant total receipts of £8,350,000 and a surplus of £404,000. From this sum the expenditure of the Irish government, net of civil and judicial salaries and pensions would have to be met.

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[7] At the time Ireland's population accounted for between 1/6th and 1/7th of the United Kingdom population.

In fact the surplus would be much larger. There was scope for the Imperial contribution to be cut if imperial and defence expenditures were less than fifteen times Ireland's contribution in any year. Gladstone determined that all customs and excise revenue collected in Ireland should be counted as Irish, irrespective of where the goods were consumed. Since the export of duty paid goods was greater from Ireland to the UK than the reverse this worked in Ireland's favour, a sum Whelby (1971) reckoned could be as high as £1,400,000. Further, a sum of £500,000 was to be paid to Ireland as a contribution to policing costs. Therefore the principle of Imperial contribution behind the Bill was fudged to ensure an outcome that was likely to benefit Ireland, and thus the chances of Home Rule succeeding.

The legislative structure of the fiscal settlement was flawed because it left Ireland bearing all the risk. The UK exchequer was guaranteed Ireland's Imperial contribution while Ireland was left with whatever surplus was available from taxation minus its contribution. The problem was compounded as under Gladstone's plans Ireland had no representation at Westminster and so no say in setting customs and excise duty: any cut in excise rates would reduce Ireland's tax receipts without reducing its financial obligations. Ireland's budget also remained at the whim of importers. Gladstone's policy of permitting the keeping of all duties gathered in Ireland may have raised more funds for the Irish Exchequer, but a change in the importing practices of UK businesses could have seen large changes in receipts year on year. While it may have raised less funds, crediting Ireland with the duties gathered on goods consumed *in* Ireland would have provided a more secure source of revenue.

In order to guarantee sufficient funds to meet its domestic obligations the Irish government had only direct taxation as a fiscal instrument, with scope limited to income and local taxes and those collected from the Post Office. The effect of fiscal gearing, the impact of a marginal change in one form of taxation on the required change in other taxes in order to maintain a given revenue, would have opened the possibility to either large variations in Irish government disposable revenue or in annual tax rates.

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[8] - A detailed analysis of financial relations between Great Britain and Ireland from the Union in 1800

The description above implies a degree of choice by Gladstone in the settlement that didn't exist. Political necessity led to the Imperial contribution being based on judgement rather than fact[9] and also influenced the allocation of fiscal responsibility and control. No practical way could be found to allow Ireland to collect only customs and excise revenues on those goods consumed in Ireland, rather than on those goods charged in Ireland but consumed in Great Britain, without imposing customs barriers. This was a step Gladstone knew unionists would not stand for (Loughlin, 1986).

Fiscal reckoning was obscured because of the differences in the level at which income tax, death duties and inheritance tax were paid in Ireland as compared to Great Britain. This made it almost impossible to determine accurately how much money Ireland could raise, but there was to be no doubt over the extent of the contribution it was to make to imperial resources. As the argument above shows, this presented Ireland with all the risk, but the simplicity of the tax structure of the 1880s makes it difficult to imagine options available today such as base or rate sharing between government levels were considered.

The lack of provision for Irish representation at Westminster in the Bill's original form was of great concern to both Irish nationalists and Unionists. While this is not a strictly financial issue, the impact of the measure had important ramifications for any financial settlement and is echoed in some of the territorial financial debates within the United Kingdom today. The Bill was charged with proposing taxation without representation and Gladstone soon agreed to alter it to allow Irish attendance at Westminster for votes which may have altered the taxation burden on Ireland. But this suggested that Irish members should also attend for matters connected with the Crown, foreign affairs or defence. This was a fore-runner of the West Lothian question, as while nationalists were unwilling to accept taxation without representation, unionists led by Chamberlain were unwilling to allow Irish MPs to sit at Westminster and speak and vote on matters that affected only Great Britain. However, deciding what issues did and didn't would have been far from easy.

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through both of the first two Home Rule Bills can be found in Murray (1970).

[9] The Bill was introduced in April and the government formed only in February, so even if a considered analysis of Irish revenues and expenditure had been desired there would have been little time to complete it.

Gladstone wrestled as unsuccessfully with this problem as politicians do when discussing solutions to the West Lothian question today.

In short, the concern that Ireland should have the resources for self-government in domestic affairs was muddied by three factors. First, there was a misunderstanding of the financial situation. Second there was a desire to arrive at a system of payments and receipts capable of being enshrined in legislation that would be acceptable to Parliament. Third there was a failure to address the issue of how Ireland was to have a say in determining its imperial burden.

The system was certainly a bold attempt at change and drew heavily on the experience learned from the British North America Act of 1867 and the powers it gave to Canada, but Ireland was so very different from Canada. Ireland was to remain a part of the United Kingdom, not just the British Empire, and it was to pay taxes to Westminster and vote there too. It was never intended to give Ireland the financial independence of Canada and the difficulties of finding a solution are clear in the failure of the Bill at its second reading: the Nationalists would accept the proposal making clear they would press for more; the Unionists could never accept it for fear that it would be the beginning of the end for the Union.

The second serious attempt at home rule was introduced in 1893, again by Gladstone. The new legislation was based around the unsuccessful proposals of 1886, and represented Gladstone's last realistic opportunity to introduce home rule (he was 83 at the time of the Bill's first reading). The intervening years of Conservative government had altered the situation in Ireland with increased government expenditure seeking to 'kill Home Rule with kindness', but there remained a strong demand for some form of self-government.

The most significant constitutional difference between the two pieces of legislation was recognition that if Ireland was to pay an Imperial contribution and be subject to taxes set at Westminster it would have to be granted continued representation. Representation was to be cut from one-hundred and three MPs to eighty and they were not to vote on matters solely affecting Great Britain or on taxation that would not be levied in Ireland. This probably unworkable proposal was dropped by June of

1893 in favour of allowing Irish MPs to vote on all issues, though Gladstone admitted this was an act of expediency rather than principle (Loughlin, 1986).

For the first time devolution was prefaced as an efficiency improvement, as Gladstone was keen to stress. Local rule would be cheaper rule. Since Ireland cost twice as much per head to run as the rest of the United Kingdom, home rule offered the prospect of savings. However Irish home rulers did not want home rule introduced to *cut* expenditure. As O'Day (1998, p164) comments, 'Home Rulers…were intent upon control over the administration, not its reduction. For them the plums of patronage were a rich pudding not to be cast aside lightly'.

The financial clauses of the new Bill (s12) determined that rather than pay a set proportion of imperial expenditure, Ireland would pass all customs and excise duties collected in Ireland to the imperial exchequer as its Imperial contribution. This condition would last for fifteen years. However if rates were to go above those in place on 1st March 1893 then the difference would go to the UK exchequer. If the rates were cut the UK government would meet the deficiency.

Ireland was to be given freedom to vary and collect all taxes, other than postage, and from them meet its domestic obligations of police charges, civil servants and pensions. In the short term the Royal Irish Constabulary and Dublin Metropolitan Police would remain under the control of the Lord Lieutenant. The Irish government would contribute a fixed sum of £1m from its own revenue as police funding, a rebate of £500,000 to the total cost of £1.5m would be paid by Westminster to recognise that the Royal Irish Constabulary remained a largely Imperial force. Two Exchequer Judges would hear cases on alleged breaches of the financial clauses of the legislation. It was estimated that this system would lead to a net surplus available to the government of Ireland of £500,000.

This proposal was hastily withdrawn seven weeks after the Bill was introduced when it was questioned in committee and subsequently shown that the stated level of customs and excise revenue would not be reached and that 'the financial considerations were based on erroneous calculations' (O'Day, 1998, p163). As a result of this Gladstone decided to amend the Bill's financial clauses completely. He proposed instead that customs and excise duties should be collected as part of Ireland's revenue, with one-third of total Irish revenue then taken as the Imperial contribution. The remainder would be returned to the Irish exchequer. The conditions of the Bill would last for six years, after which they would be reviewed. However, the scope for independent taxation by the Irish government was this time to be severely curtailed as almost all taxation powers were to rest with Westminster. Whelby (1971) reckoned that Irish imposed taxation would account for £138,000 of total income collected in Ireland of £6,992,000 or approximately two percent.

The change in structure between the first and second drafts of the Bill was dramatic. The initial proposal was a rather extreme variant of one often found in federations, where taxes on the movement of goods are reserved to the federal government with other taxes controlled at the state level. The subsequent proposal had a system much more familiar in devolved states where sub-national governments are given a sum to spend, but have no control over the size of that sum.

The system was never tested as while the Bill passed through the Commons it fell in the Lords. It was 1914 before a devolution bill for Ireland was successful, and only then because of the enactment of the Parliament Act in 1911. This Act sought to overcome the constitutional crisis caused by the House of Lords' rejection of the 1909 budget. It restricted the power of the House of Lords to delaying a measure supported by the House of Commons for three years before their objection was over-ruled and the Bill enacted. This measure allowed the Conservative majority in the House of Lords against home rule to be overcome and the Home Rule Bill introduced in 1912 finally passed into law as the Government of Ireland Act 1914.

However, the Act's introduction was delayed until the completion of the Great War, at that time thought to be no later than Christmas 1914. The war, of course, lasted much longer and the Easter Rising in Dublin in 1916 and the dominance of the nationalist Sinn Fein in the 1918 general election made the Act redundant. But the financial clauses of the Act were both much more complicated than previous proposals and also outlined many of the conditions that were later to govern financial relations between London and Belfast for half of the century.

Government’s role had expanded significantly between Gladstone’s final attempt at home rule in 1893 and Asquith’s bill in 1912. Old-age pensions and national insurance added to expenditure and had to be matched by taxation. Ireland was still a relatively poor country and if the conditions of the developing state sector were to be maintained in Ireland at the level of the United Kingdom as a whole, then the financial settlement required to be designed in such a way as to permit that level of expenditure to be sustained. It was clear that whole-United Kingdom taxation rates allowing Ireland to retain revenue raised within its borders would be insufficient to meet expenditure requirements. This was partly because of Ireland’s smaller tax base, but also because expenditure per head in Ireland was so much higher than in the rest of the United Kingdom. Oldham (1920) calculated the deficit between Irish true revenue (i.e. excluding duties paid on goods not consumed in Ireland and tax raised in Ireland for non-residents) and expenditure at £1,222,500 in 1913-14, the year before the Act was passed.

The solution to this problem was two-fold. Firstly, the power of taxation and the collection of revenues was retained as a Westminster function. Secondly, certain items of expenditure and control were reserved to Westminster and so funded from general United Kingdom taxation rather than considered part of Ireland’s financial burden. Initially these reserved services were to be: matters relating to the Land Purchases Acts, National Insurance Act, Old Age Pensions Acts, Labour Exchanges Acts, the Royal Irish Constabulary and savings banks. These services would eventually be transferred to Irish control when mutually agreeable.

Ireland did have certain revenue raising powers and could impose additional rates on existing taxes, although these increments were limited in the case of customs and death duties and income taxes. The revenue raised in Ireland by both whole United Kingdom taxation and additional Irish taxation was to be returned to Ireland for expenditure on Irish services. However, given the deficit of expenditure over income, two short-term concessions were made in addition to retaining some services under London control. First, initially Ireland would not receive the revenue raised by taxation within its borders but a sum equivalent to the costs of Irish services net of Post Office revenues, which were to be retained in Dublin. This sum was to be determined by a Joint Exchequer Board of officials from both British and Irish governments. Second, £500,000 was to be paid by Whitehall to Dublin to cover the costs of the establishment of an Irish government. This payment was to be reduced by £50,000 each year until the amount transferred was £200,000. As such it was hoped to provide sufficient financial leeway to permit the assignment of some responsibility for expenditure to Ireland, followed later by further expenditure powers and taxation to match.

It is clear that this system, unlike its predecessors, was designed on an expenditure rather than revenue basis. That is to say, it took the level of expenditure as given and sought to find ways in which to raise sufficient revenue. The problems discussed above as regards Ireland’s over taxation still applied, but then so too did the massively excessive per capita expenditure. The London government hoped that Ireland run largely from Dublin would lead to cuts in this expenditure and therefore that revenue raised in Ireland would be sufficient to pay for services in Ireland without central grants. However, a cold-turkey financial change does not appear to have been considered and Ireland was to be very slowly weaned from high expenditure.

The issue of unitary taxation rates and bases would still remain. Ireland still had different consumption patterns to the rest of the United Kingdom. Therefore unitary tax rates and bases were unlikely to be sustainable in the long term unless consumption patterns were to start to converge. Another issue that could no long go unaddressed was the lack of an Imperial contribution. While Ireland was a part of the United Kingdom it was reasonably expected to contribute to whole-United Kingdom and imperial expenditure.

There was no scope for that to happen in the initial design of the Act. The £500,000 subsidy, retention of some services for the United Kingdom government and expected short-term replacement of transferred taxation revenue with an expenditure grant clearly indicated the problem of expenditure in excess of revenue. However, this could not have gone on indefinitely. Oldham’s (1920) figures show that subsequent war taxation of Ireland generated a significant surplus of £5,332,000 as early as 1915-16. However, this level of taxation would not have been tolerated in peace time and so Ireland’s deficit would have returned.

The Act was something of a gamble that governing Ireland from Ireland would lead to considerable cuts in expenditure. This time it was crucial that the system was well designed since the Parliament Act assured it would be passed, and it is not clear what would have been the reaction were Ireland always to have been a deficit part of the United Kingdom.

This system was very similar to the one proposed after the Great War for Ireland to be divided north and south and passed as the Government of Ireland Act 1920. Southern Ireland subsequently became the Irish Free State and financially separate from the United Kingdom. Only in Northern Ireland did the conditions of the 1920 Act apply, and as will be discussed below, they applied only in the very loosest sense. The issues of concern in the financial management of Northern Ireland due to the 1920 Act are very similar to those that would have quickly become apparent had the 1914 Act been implemented. The only difference would have been that the force of the 1914 Act would have been more keenly felt in London as it attempted to maintain a Great Britain level of expenditure across the whole of Ireland, rather than in just one part of it.

Northern Ireland

The establishment of the Irish Free State meant that the provisions of the Government of Ireland Act 1920 were never applied to what the Act defined as Southern Ireland. However, they did apply to the new government of Northern Ireland, and were to influence, although ultimately not determine, the financial relations between Northern Ireland and Great Britain until 1980[10]. Northern Ireland was expected to make a contribution to Imperial expenditure, known as the excepted services, on the basis of a broadly balanced budget.

At the time of partition Ulster was by far the richest of the four provinces of Ireland and Northern Ireland inherited that relative wealth. But it was a wealth relative only to the rest of Ireland. Moreover, Belfast, as the centre of heavy industry in Ireland,

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[10] As the longest lasting period of devolution in the UK, a full examination of the development of financial relations between Stormont and Westminster is beyond the scope of this paper. Gibson (1995) and Mitchell (2006) offer excellent analysis of this topic.

suffered badly during the economic depression of the 1920s when for the first time the financial conditions of a devolution settlement were tested. As will be seen, the rapid advances in the welfare state after the Second World War, the desire for rough equality of service across the whole of the United Kingdom even before the war and Northern Ireland's relative poverty meant that the formal mechanisms of the Act were quickly replaced by political practicality.

Sections 20 to 34 of the Government of Ireland Act 1920 determined the financial conditions for the government of Northern Ireland. The scope for devolved taxation was limited, but representation for Northern Ireland was to continue at Westminster. Taxation bases and rates for reserved taxes were determined by the UK government and revenue collected from them was retained on Northern Ireland's account. These funds would then be spent on Northern Ireland's services, both those provided by the Westminster and Stormont governments, and Northern Ireland's share of Imperial costs.

Changes to tax rates could be made to transferred taxes but not to the tax bases. Only in those areas in which there was not substantially similar central taxation did the Stormont government have the power to determine tax bases, and the scope for this was heavily limited. This condition almost negated the opportunity for own-source revenue.

Northern Ireland's share of reserved taxes minus the cost of excepted and reserved services was to be decided by a Joint Exchequer Board. The Board, after the establishment of the Irish Free State, was to have one representative from the United Kingdom government, one from the government of Northern Ireland and a Crown appointed chairman. Mitchell (2006) outlines the issues in finding a replacement chairman whenever the post required to be filled. A seeming independence and, more crucially, a willingness to avoid controversy and too much involvement in the process were key qualifications. The Act had assumed, prior to partition, that the governments of both parts of Ireland would run roughly balanced budgets. The reality was that Northern Ireland had little hope of doing so due to poor economic performance and both internal and external pressures for conformity with UK service provision.

Mitchell (2006) highlights the paradox of granting devolution to Northern Ireland, the most unionist part of the Union, and persisting with it even when Southern Ireland became the Irish Free State. He notes that 'the conflict of choice versus equality, at least at the macro level…was resolved largely in favour of the latter, though differences were evident in the provision of public services' (Mitchell, 2006, p. 58). Sir Arthur Quekett, Parliamentary Draftsman to the Government of Northern Ireland, observed that a separate parliament and government in Northern Ireland was leading to more uniformity not less. Mitchell (2006, p. 58) interprets this as reflecting the fact that 'maintaining the union was the paramount objective.'

This was a mutually agreeable outcome, but still provided scope for tension. The government of Northern Ireland placed pressure on the government in London to ensure that Northern Ireland was not the poor relation of the United Kingdom. Equally, the government in London did not want significant divergence in public services to raise awkward questions about the appropriate provision in the rest of the UK. When the Stormont government wished to diverge London sought to apply pressure to conform, but when conformity was financially difficult, Stormont was able to extract concessions from London.

Two examples highlight this relationship. The first occurred during the depression of the 1920s. Growing unemployment support payments were one of many financial crises to shape relations between Northern Ireland and Great Britain. To keep unemployment benefits at the level of the rest of the United Kingdom placed a huge burden on the Northern Ireland Exchequer. Initially the deficits created by this expenditure were funded by borrowing, but this was unsustainable as the recurring deficit would have been huge in relation to the total budget (Green, 1979) and would have placed the Northern Irish government in a position of being unable to fund debt requirements.

An agreement was reached with the Treasury that it would fund three-quarters of the difference of the unemployment fund to ensure similar payment levels could be met. The desire for broad equality of provision was set out even although the recently passed Government of Ireland Act had devolved unemployment payments to Belfast. It would be a mistake to think that both sides were motivated purely by a unionist spirit of equality. Political pragmatism dictated that the Westminster government sought to stop unemployed economic migrants leaving Northern Ireland to seek higher unemployment payments in Great Britain and the Stormont government was happy to fund services to a standard they would have been incapable of achieving from their own finances alone. However, there remained a need for Northern Ireland's finances to at least appear in someway independent of Westminster and based on a sense of efficiency. This was met by the requirement for Belfast to meet twenty-five percent of any shortfall.

The second, and highly significant, example is an agreement reached in 1938 that agricultural supports, if they were justified for the benefit of the United Kingdom as a whole, would be met by the Treasury, even though agricultural support was a devolved function (Green, 1979). The significance was not just the impact on agricultural policy, although with a large agricultural sector in Northern Ireland that in itself was doubtless important, but that it was part of a larger, and publicly stated, movement towards parity. Sir John Simon, the Home Secretary, placed a memorandum before the House of Commons announcing that after discussions with the government of Northern Ireland,

> "[A] deficit on the Northern Ireland budget which was not the result of a standard of social expenditure higher than that of Great Britain, nor the result of a standard of taxation lower than that of Great Britain, the United Kingdom Government agree that it would be equitable that means should be found to make good this deficit in such a way as to ensure that Northern Ireland should be in a financial position to continue to enjoy the same social services and have the same standards as Great Britain."
> [House of Commons, 12th May 1938, Col 1708-1709]

This announcement formalised the changing nature of Northern Ireland's finances and therefore the role of the Joint Exchequer Board. While the Joint Exchequer Board was intended to play a constitutional, as well as practical, role, in fact its operation was reduced largely to window-dressing, and although that role had political significance it had little practical influence on finances.

The Government of Ireland Act 1920 had envisaged a revenue-based system where taxes set by both the United Kingdom and Northern Ireland governments would pay for excepted services (essentially Northern Ireland's share of the costs of running the empire), reserved services and devolved services to leave a roughly balanced budget. The Board's role would be to set the contribution after having regard to Northern Ireland's taxable capacity. What developed was an expenditure based system where Northern Ireland's revenue collection and expenditure needs determined how much was available as an Imperial contribution (Mitchell, 2006).

The pressures from social payments, even before the introduction of the welfare state and Northern Ireland's relatively poor economic performance, meant that the scope for a contribution was increasingly limited. Maintaining a system based around revenue collection could have worked, financially if not politically, but would not have permitted anything approaching service parity, while an expenditure-based system requires an expectation of the appropriate level of expenditure to undertake. With parity as the appropriate expenditure level then the financial system contained within the Government of Ireland Act could not operate.

The problems of the financial settlement went beyond the parity principle to the details of revenue raising and expenditure responsibility. The 1920 Act reserved the power to determine the base and rate of the principal forms of taxation: income, capital and customs and excise. Northern Ireland was to be credited with the revenue raised from within its boundaries. Even without regard to expenditure responsibilities this raises a number of issues. It is difficult to assign the receipts of taxation on mobile factors such as financial capital and goods. The value added from production may be carried out in Northern Ireland, but the company may be registered and have its headquarters in another part of the UK and so have its profits taxed there. While identical rates across the UK would stop transfer pricing - the seeking out of the lowest tax incidence for corporate taxation - tax transfer makes it difficult to determine the sum generated in any one area. The Act also limited Northern Ireland to raising revenue from devolved taxes or from those areas where no similar UK tax was levied. These taxes, such as death duties and vehicle taxation had limited revenue raising power, but the freedom to vary them placed additional impetus upon them.

However, such is the effect of gearing that these small additional taxes could never make up a shortfall between expected revenue and that passed from the UK government.

These shortcomings in fiscal allocation could have been overcome by compensating equalisation payments, but there was no statutory scope to make them, although, as shown above, they became effective by reductions in the Imperial contribution and by the Westminster government's accepting responsibility for costs that were properly devolved responsibilities. The significant failure in the legislation was to assign taxation and then also to devolve social transfers such as unemployment payments. Northern Ireland's poorer economic performance meant that taxable capacity was below that of the rest of the United Kingdom and therefore revenue raised per capita was lower. Labour, as a mobile factor of production, is liable to migrate to those areas where returns are highest, and that includes returns to unemployment as well as employment. The UK government feared that lower rates of unemployment insurance payments in Northern Ireland would lead to migration to the UK, while employers in Northern Ireland were concerned that a standard UK allowance was too attractive in Northern Ireland, where living standards were lower, and therefore limited individuals' incentives to return to employment (Gibson, 1995). The combination of assigned taxation, but an acceptance by both Westminster and Stormont of rough equality of service provision, reduced the financial clauses of the 1920 Act to a broad framework to be interpreted pragmatically.

The ability of the system to work in such circumstances, without requiring legislative change, are many and not least Northern Ireland's financial insignificance in comparison to total United Kingdom government expenditure. Of perhaps more importance was that both parties to the agreement wanted the system to work. The Northern Ireland government was staunchly unionist and would not place the union in jeopardy. The United Kingdom government too wished to preserve the union, but wished to do so by keeping Northern Ireland's awkward politics in Northern Ireland in a manner that only devolution could achieve. Were the relationship not to have been so, then the system would have fallen apart much sooner than the collapse driven by the civil unrest of the late 1960s and early 1970s.

The Kilbrandon Commission and Devolution to Scotland and Wales

The Kilbrandon Commission[11] was appointed in 1969 to examine the functions of all levels of government, how they affected the different parts of the UK and what changes, if any, should be made. The Commission took over four years to reach its conclusions, including a memorandum of dissent signed by two members, and is the only study of its kind undertaken by government in the UK. It was driven by two by-election victories, those of Gwynfr Evans for Plaid Cymru in Carmarthen in 1966 and a year later for the SNP's Winnie Ewing in Hamilton. These results demonstrated a growth of nationalism within Scotland and Wales that the Labour government believed threatened the stability of the Union. The Commission took evidence through to 1974. This period spanned devolution in Northern Ireland and its ending, the Sunningdale talks and agreement, and the Northern Ireland Assembly of 1974. This period presented the Commission the chance to observe a form of devolution in practice, its failure and the subsequent failure to find an alternative to direct rule.

The Commission's report is an extensive document providing background chapters on the history of each part of the United Kingdom, the nature and perceived dissatisfaction with government in the UK, and issues surrounding devolution, federation and separatism. The Commission concluded, by majority, that a form of legislative devolution should be offered to Scotland and Wales. The minority report favoured a form of regional government for England in addition.

Neither of these proposals were accepted by the government, which instead issues its own devolution plans within the White Papers *Devolution within the UK* (HMSO, 1974), *Democracy and Devolution* (HMSO, 1975), *Our Changing Democracy* (HMSO, 1975), and *Devolution to Scotland and Wales* (HMSO, 1976). The culmination of this process was the passing in 1978 of the Scotland Act and the Wales Act. Amendments to these Acts requiring forty percent thresholds of electors in Scotland and Wales in favour of each Act in referenda to be held in Scotland and Wales had been inserted during debate. These referenda were held in 1979, but failed to achieve both these thresholds and the Acts were repealed. Although the process failed, the financial clauses determining how the system was expected to work, bear investigation, not merely because they are strongly related to the suggestions made by the Kilbrandon Commission, but also because they still influence discussions of devolution finance today.

The Commission concluded that devolution finance presented the problem 'to devise a scheme for a fair distribution of funds to the regions while permitting them to exercise their devolved powers without undue influence from the centre' (HMSO, 1973, p475). It believed the solution to this problem was to establish an independent body to operate between the regions and the centre, termed the Regional Exchequer Board (REB). Its duty would be to ensure a fair distribution of funds to meet UK-wide standards, but independence of action for the regions would be maintained by allowing them to spend the allocated funds as they saw fit.

The influence of the Joint Exchequer Board is obvious, but this is where the similarity ends. The Commission believed that taxation could be shared or devolved, but that it was more likely taxation would be a central function and that funding would be through grants. The REB, rather than central government and therefore most likely the Treasury, would determine a UK standard of service for all devolved services and the sums required to achieve equality for each region, but once the region received those funds they would be free to spend them as they chose.

Not all funding was to be variable, given that each region already had an existing level of expenditure and it would have been financially difficult to alter budgets significantly over a short period. Instead, it was proposed that around ninety-five percent of budgets be historically based and the remaining five percent subject to change. It was believed that this system would ensure budgets could be met while encouraging regions to compete over the remaining allocation and so ensure efficiency.

When the Scotland Bill and the Wales Bill were introduced in 1978 both set out the method by which funds would be made available to the Assemblies through the

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[11] The Commission was formally titled 'Royal Commission on the Constitution' and was known as the

Scottish and Welsh Consolidated Funds, but nothing on how those funds were to be determined. Both Bills state (s 46(1)) that,

> "The Secretary of State shall from time to time make out of moneys provided by Parliament payments into the Scottish [Welsh] Consolidated Fund such sums as he may determine by order made with the consent of the Treasury."

Borrowing was to be permitted within constraints to ensure macroeconomic management, but taxation was not to be devolved. Unlike previous devolution bills this system would be based on an expenditure rather than revenue basis. This demanded that some system be determined to allocate resources to Scotland and Wales. These plans were laid out in *Devolution: Financing the Devolved Services* (HMSO, 1977) and *Needs Assessment Study: Report* (HM Treasury, 1979). The latter document was published after the devolution bills had failed their referenda test, but set out a new system, based in part on the suggestions of the Kilbrandon Commission, to determine the funds required for devolution finance on the basis of need.

The study focused on those services that were to be devolved under the 1978 Acts. It stated that,

> "it is a long-established principle that all areas of the United Kingdom are entitled to broadly the same level of public services and that the expenditure on them should be allocated according to their relative need." (HM Treasury, 1979 para 2.9)

In calculating relative need, the report recognised what were termed "objective" and "subjective" factors. Objective factors would increase the cost of provision irrespective of the policy options chosen. Such factors included the extent of rural living and dispersed population in large parts of Scotland and Wales. Subjective factors were where cost was determined by choices made as to the level or quality of service.

Crowther Commission until the death of Lord Crowther in 1972.

The report of the Kilbrandon Commission also acknowledged that it might be important to separate that which could be quantified from that which could not, since these factors were more likely to determine the practical identification of relative need than were the more notional concepts of objective and subjective factors. After taking account of all cost information it had available, the differences in the services devolved under the legislation and subjective and objective considerations, the study produced estimates for the revenue requirements of the to-be-devolved administrations. The Commission determined that in aggregate for every one hundred pounds spent per head in England on the functions that were to be devolved, Scotland would require £116, Wales £109 and Northern Ireland £131 to provide a similar service. These figures would have been used to determine the increments to devolved expenditure.

The system was never tested since the devolution legislation was repealed in July 1979 when the March referenda held in both countries failed to secure forty percent of the electorate in favour of either proposal[12]. Instead a supposedly make-shift system devised by Treasury officials was implemented to allocate increments in funding to Scotland and Wales on the basis of their population share and funding changes on similar services conducted by the UK government for England. This formula eventually became known as the Barnett formula after the Chief Secretary of the Treasury at the times of its devising and is the system still in use today. It was never enshrined in legislation and its existence was not publicly acknowledged for many years, but it has been the focus of discussions over devolution finance ever since (Kay, 1998; Bell, 2000; Christie and Swales, 2005).

That the needs assessment system was not introduced demonstrates some of the weaknesses in the system. The first failure is derived from the devolution legislation rather than the financial clauses. The 1978 Acts set out those functions that were to be devolved rather than those that were to be retained at Westminster. This limited system would have created a devolved settlement that could only be understood by

[12] While the forty percent threshold was not met in either country a narrow majority of those in Scotland who voted were in favour of the proposals. In Wales electors voted four to one against the proposals.

referring to the legislation defining those areas over which the Assembly was to have competency – as the legislation changed so too would the devolution settlement. The scope for challenge and disagreement between central and devolved government was large, and any disagreement about legislative competency would lead also to funding arguments about whether the scheme was to be classed as objective or merely a subjective policy choice. The needs assessment proposals drew a veil over the subject of such disagreement by suggesting that what was measurable was of more consequence. This was undoubtedly a rose-tinted, if not naïve, understanding of how devolution would operate.

Devolution is generally justified on the basis that decisions are more efficiently made closer to the people they are likely to effect since the local population have the best information concerning their own circumstances. This justification for what is more properly termed administrative *decentralisation* was already fulfilled by the Scottish and Welsh Offices. However, devolution designed to reflect different choices in the nature of public service provision and to allow policy changes offers the possibility, if not the inevitability, of policy divergence. The needs assessment exercise failed to account for the problems this would create.

The Kilbrandon Commission had foreseen difficulties in determining appropriate allocations between competing governments and proposed a Regional Exchequer Board. The government had discounted such a system as unwieldy and politically infeasible, since financial decisions would be one step removed from parliament. The result was that power was left in the hands of central government and therefore the Treasury. It is difficult to imagine how this process would not evolve into a bargained outcome rather than an objective measurement process, especially as devolution grew more established and policy divergences became more likely. We have argued elsewhere (Christie & Swales, 2005) that there are good reasons why Scotland and Wales may have been able to extract concessions from the Treasury and so secure above strict ‘objective’ allocations, but the outcome in such circumstances scarcely justifies establishing the process.

The 1978 proposals lack any devolved or attributed taxation element. The Kilbrandon Commission had acknowledged that most regions of the UK paid less in taxes than they received in public expenditure, and while that conclusion was drawn five years before the devolution legislation, it is unlikely that the situation had changed, or indeed that it has changed today. The increasingly complex nature of the economy and the taxation system narrows the scope for appropriate devolved taxes; even in 1886 there were concerns over the potential impact of devolving duty rates. The system was to rely entirely on transfers. While previous proposals had demonstrated the difficulty in determining how to allocate sufficient revenue raising resources to ensure the functions of government were provided for, the 1978 proposals showed that a switch from a revenue to expenditure based system doesn't solve the problem of appropriate allocation, it merely alters the nature of the arguments surrounding it.

Devolution to all in 1998

The election of the Labour party to government in 1997 moved devolution once more onto the legislative agenda. The previous Conservative government had been firmly against devolution, believing it threatened the stability, if not the continued existence, of the UK. All other major parties in Great Britain favoured constitutional change to allow greater powers to Scotland and Wales. Northern Ireland again proved the exception, with unionists generally against devolution and nationalists largely in favour of it. The government also favoured enhanced power to the English regions, although proposals for this would come after devolution to Scotland, Wales and Northern Ireland.

The proposals subsequently enacted as the Scotland Act 1998, the Government of Wales Act 1998 and the Northern Ireland Act 1998 proposed asymmetric transfers of power to a parliament in Edinburgh and assemblies in Belfast and Cardiff. Unlike the 1978 legislation, the 1998 Acts listed those areas reserved to the parliament at Westminster and devolved all other areas not specifically listed. Scotland and Northern Ireland were given the power to enact primary legislation; Wales was restricted to secondary legislation[13].

[13] Bogdanor (2001) comments that the reason for the difference has 'never been wholly clear', but suspects that governments have consistently seen Scotland as more suitable for primary legislative powers since it has a distinct legal system from the rest of the United Kingdom. The devolution settlement in Wales effectively transfers the powers previously held by the Secretary of State to the

Devolution did not alter the financial conditions from those prior to devolution, meaning the Barnett formula would continue to be used to allocate additional expenditure to Belfast, Cardiff and Edinburgh. The sole exception was for Scotland, where the Parliament was permitted to alter the basic rate of income tax by three pence. This power has not yet been exercised, and should it be used to reduce the basic rate the Treasury reserves the right to reduce Scotland's annual allocation by an amount equivalent to the foregone sum.

The financial relationship between the Treasury, as the dominant UK department, and the devolved legislatures was formalised in a 1999 publication *Funding the Scottish Parliament, National Assembly for Wales and Northern Ireland Assembly: A Statement of Funding Policy* (HM Treasury, 1999). For the first time a publication detailed how the Barnett formula operated for each country and how calculations were made. The publication was updated in 2000 and has been re-published biennially since.

As devolution did not alter this system the same arguments surrounding the formula, or any formula, as an appropriate allocation mechanism are relevant both pre- and post-devolution. An issue with the equity of the formula is that while it is based indirectly on need, it is the need for spending in England alone that is determined: the other parts of the UK merely receive a population and service comparability increment.

It can also be argued that a formula that conducts allocations mechanistically does not force those making spending decisions to face the opportunity cost of their decisions as they would had they to simultaneously make the taxation decisions required to balance expenditure. However, this argument has limited validity, in the sense that while they don't face the opportunity cost of the size of the public sector, but they do face the opportunity cost of competing claims for resources within it. Given that very little government expenditure is open to debate, having been

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National Assembly. Calls for primary legislative powers are growing and were recommended in the Richards Commission report (2004) committed to service provision in previous years, this opportunity cost remains a very real one.

Other criticisms of the formula system are peculiar to the Barnett formula. When the formula was introduced expenditure per head in each part of the UK was different. The Barnett formula, as correctly applied, allocates equal expenditure per head increments to each country within the UK. The effect of an identical increment on different starting positions is that all countries should tend towards the same level of expenditure per head.[14] This has led to accusations of a deliberate 'squeeze' in expenditure per head (Kay, 1998).

Much of the focus has been against the counterfactual of the needs assessment study published by HM Treasury (1979). In this debate the relative expenditure indices calculated at that time have been interpreted as minimums. If funding in the devolved nations was to fall beneath these minimums, this is taken to mean that services would have to be cut. We have argued that we do not believe the formula operates as official published sources would make out. In particular there is, as yet, no clear evidence of converging expenditure per head under the Barnett formula (Christie & Swales, 2005). In addition, it is of little value to compare current and future expenditure levels with those calculated for a different set of devolved services nearly thirty years ago.

Of the devolved administrations only that in Scotland has the power to levy taxation. The power is limited to a three pence variation in the basic rate of income tax, but is estimated to have scope to raise around £800m. The Labour party announced during the inaugural elections to the Scottish Parliament in 1999 that it would not use the variable rate, while the *2003 Partnership Agreement for a Better Scotland* between the Labour party and the Liberal Democrats stated that ministers "will not use the income tax varying powers of the Scottish Parliament" (Scottish Executive, 2003, p45). The perceived political requirement to rule out the use of the statutory power, and the longer the power is not exercised, the more likely it is that it will be a power in name alone. There is a similarity with the power granted to Northern Ireland under

[14] Formally the situation is that with a static population the Barnet formula should maintain the nominal initial variations in expenditure per head across devolved nations. However, under inflation and

the Government of Ireland Act 1920 to levy taxation on those areas where no UK taxation was levied. The failure of the Stormont government to exercise the power of taxation early on under devolution made additional taxation increasingly difficult to introduce once the remit of the parliament was set in the minds of the electorate, the UK government and the government of Northern Ireland.

Lessons from devolution in the UK

Two recent publications, one by the Liberal Democrats (Steel Commission, 2006) and the other by Paul Halwood and Ronald MacDonald (2006) have suggested changes to the current system of territorial funding for the United Kingdom. Both papers focus on Scotland. They propose that Scotland should be given the power to raise more of its own revenue. Hallwood and MacDonald suggest Scotland should become fiscally independent of the United Kingdom and pay the Westminster government for those whole-United Kingdom services it provides for Scotland: primarily defence and foreign affairs. This is a modern version of the Imperial contribution. The Liberal Democrats (2006) suggest a more limited tax allocation system, where all taxes would be under the control of the Scottish Parliament except those specifically reserved to Westminster. In addition, they propose that more responsibilities would be passed from London to Edinburgh in measure with the greater fiscal powers, that a needs-based equalisation system would require to be implemented and that a Finance Commission for the Nations and Regions would oversee fiscal and financial relationships between the different parts of the United Kingdom. Meanwhile, the Conservative Party, since out of government, have suggested that only English MPs should vote on matters affecting England alone, although they continue to support the Barnett formula, for the time being at least.

The Liberal Democrats have acknowledged in their analysis that it is extremely difficult to remove any part of the United Kingdom from the whole-United Kingdom budgeting and taxation system without accompanying constitutional and institutional change (Steel Commission, 2006). Nothing to date has been proven a successful devolved fiscal system in the manner in which it was originally envisaged: the Bills of

increasing nominal government expenditure both the real aand proportionate variation in per capita

1886; 1893 and 1914 fell and the financial clauses of the 1920 Act bore only a passing resemblance to the system that in fact operated in Northern Ireland until 1980. Many of the issues raised and solutions proposed by Hallwood and MacDonald, the Liberal Democrats and the Conservatives have been seen before in the United Kingdom. This final section of the paper refers these issues back to previous United Kingdom experience and what can be learned from it. Importantly, it also shows that while lessons can be learned from the experience of other countries, the particular constitutional, political and geographical circumstances of the United Kingdom mean that overlooking the experiences of the past, as the current literature on options for the future of the United Kingdom's public financial system seems to do, runs the risk of making the same mistakes again.

A consistent feature of previous systems, both proposed and enacted, is that they have been designed with the intention of maintaining the United Kingdom. McLean and McMillan (2005) argue that devolution to Scotland may have taken much of the impetus from the separatists' cause, but that it is because the voting system employed in Scotland will make it very difficult for the SNP to win the parliamentary majority needed to hold an independence referendum rather than devolution killing independence stone dead[15]. As the system proposed for Southern Ireland in 1920 showed, devolution of financial and legislative powers is insufficient to maintain the Union where there is a strong desire for separation within any part of it, but by designing an electoral system under the control of the Westminster Parliament the Labour Party has put in place an effective constraint on separation that a financial solution on its own could not have achieved. The financial settlement is important, but there must be political acceptance of the shape of the United Kingdom before it can be mapped out.

Once a mutually agreeable, or at least not mutually disagreeable, shape for the United Kingdom is settled upon, economic practicalities will, in part, determine the financial system. Social security payment rates are probably unsuitable to be devolved in a country the size of the United Kingdom in any circumstances. The Liberal Democrats

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expenditure will fall.

[15] The claim that granting devolution to Scotland would kill independence stone dead was made by George Robertson, a former shadow Secretary of State for Scotland.

(Steel Commission, 2006) acknowledge this constraint, but Hallwood and MacDonald (2006) believe this is possible. The experience of Northern Ireland early in its devolved history shows the difficulty of having different unemployment payment levels and the possibility of extensive unemployment migration between territories to avoid the lowest unemployment payment. While migration within the European Union is similarly possible, the lack of a language barrier and a homogenous British culture within the United Kingdom makes it more of a concern. Redistributive expenditures are generally taken to be better dealt with centrally (Oates, 1999).

Northern Ireland's experience demonstrates the effects of a system based in statute. The legally defined system for Northern Ireland only worked because both sides to the agreement wanted it to work and were willing to make concessions, principally financial concessions by Westminster and policy concessions by Stormont. Had the relationship broken down and the system become one enforced by either side as stated in law, unlikely though that was, then Northern Ireland would have been in dire financial trouble. This would have placed the United Kingdom government of the day in the political quandary of trying to justify why it had abandoned that most unionist part of the United Kingdom.

At present the Barnett formula is not based on statute – its workings were not laid out officially until the Labour government was elected in 1997 – and it is this lack of transparency and resultant scrutiny, as we have argued elsewhere (Christie and Swales, 2005), that has secured its longevity. However, with a reduction in the formula's opacity scrutiny has increased. No replacement system will be permitted to have such leeway, and a replacement will have to be found at some point as the convergence outcome of a properly operated Barnett formula – and the formula is now closer to being properly operated than ever before - is neither sustainable nor desirable. While no system will be perfect in all circumstances and times, an alternative to the Barnett formula must be durable and enforceable by all sides if it is to be operable, since renegotiation is not costless.

None of the proposals of 1886, 1893, 1914 nor 1920 envisaged the need for some form of equalisation of either expenditure per head, or more usefully service provision per head, across different parts of the United Kingdom. The welfare state was in its infancy in 1914 and 1920, but the repercussions of different taxable capacities and the need for standard or very near standard unemployment policies in all parts of the United Kingdom led to the first crack in Northern Ireland's financial settlement. The extension of the welfare state following the Second World War has increased the necessity of approximate equality of service. This presents one of the difficulties of devolution and is not exclusive to the United Kingdom: how to achieve the equality of standard expected within a state while having devolution to permit different policies to satisfy different preferences within it.

The model normally offered is from Australia, where the Commonwealth Grants Commission is charged with allocating resources amongst the states in order to achieve the possibility of a standard level of service, although the states are under no obligation to provide that service. The only experience in the United Kingdom of such a body is the Joint Exchequer Board established by the Government of Ireland Act 1920 to determine the contributions to the costs of Empire from the governments of Belfast and Dublin. It has been shown above that this body's operation was far removed from that intended, but some similar organisation would require to be established. The Liberal Democrats have acknowledged this (Steel Commission, 2006), but have presumed their system would operate within a federal United Kingdom, although this is not a necessary condition for such an extra-governmental body. Without some form of defendable independence from the central machinery of government, with the Treasury at the heart of that machinery, the system will depend on bargaining to achieve its outcome. The experience of the Stormont parliament has shown that a bargained system can work when the outcome is to the benefit of both parties, but mutual benefit is uncertain and a largely rules based system is superior.

Conclusion

The history of the United Kingdom's attempts to devise devolution settlements offers a rich source of evidence to inform any future financial settlement between the different territories of the United Kingdom. Most current analysis is centred on a now well established economic literature on fiscal decentralisation and the experience of other countries. These analyses are based principally around federal political systems. The importance of this fact is often overlooked, but it is crucial. The United Kingdom has not had a strictly enforced rules-based system of financial devolution where both parties to the agreement have been bound by transparent statute or rules. To create this would represent a significant change away from the enigmatic Barnett formula and represent a return to the Liberal financial proposals of the late 19th and early 20th centuries, where assigned and transferred taxes were contained in statute.

Northern Ireland showed the limitation to a system where the statute sets out a desirable system with an undesirable outcome. The experience of Gladstone's devolution bills of 1886 and 1893 demonstrated the difficulty of devolving finance and determining an appropriate contribution from the devolved governments while seeking to have a functioning parliament for the United Kingdom without having devolution for England. There are no easy answers to the problems these issues raised - history has shown that. But when discussing the future of the United Kingdom's fiscal and public finance systems these are the issues to which answers must be found. The experience of the United Kingdom to date adds more points to those raised by the literature focussing on decentralised fiscal theory and the experience of other countries, but these points require greater analysis and thought than the current debate has given them.

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Appendix 1 – Outline of discussed devolution proposals

Date	Financial Provision	Representation at Westminster	Result
1883	Custom and Excise duties set at Westminster, but the duty raised in Ireland would be taken as Irish revenue. Direct taxation set and gathered in Dublin. Imperial contribution first call on Irish revenue. Westminster to contribute £500,000 towards the cost of policing.	Initially none, but altered during Commons discussions to remain at existing level (103 seats) for issues concerning Irish taxation.	Failed at the second reading in the Commons by 311 votes to 341.
1893	Customs and Excise set by Westminster and passed to London as Ireland's Imperial contribution. Dublin would have freedom over all other rates and taxes other than postage charges. This plan was withdrawn during the committee stage. Financial clauses of the Bill changed so that the Imperial contribution would be one third of Irish revenue, with the Westminster government to retain power over taxation rates for six years. Dublin would be permitted only supplementary taxation powers. After six years the situation would be reviewed and Dublin was expected to take control over all taxation other than Customs and Excise duty, which would then be taken as the Imperial contribution.	Number of MPs cut from 103 to 80 (in line with Ireland's population share) and then only to vote on issues and taxation concerning Ireland. Latter changed to 80 MPs able to vote on any matters at Westminster.	Failed at first reading in the Lords by 41 votes to 419.
1912	Tax bases and rates to continue to be set at Westminster, with revenue raised in Ireland being returned to Dublin as the transferred sum.	Number of Irish MPs to be cut to 42.	Passed as the Government of Ireland Act 1914, but only after the use of the Parliament Act

	Irish government to have powers to add additional taxes to those applied by London, but not in competition to them and only within specified limits. Initially the sum transferred to Dublin was not to be determined by taxation raised in Ireland, but by a Joint Exchequer Board that would determine the level of resources required to meet Irish spending obligations. In the short-term this was augmented by a tapering grant of £500,000 from London plus the retention of some functions as United Kingdom services until such time as it was mutually agreeable that they should be transferred to Dublin. Post Office revenue raised in Ireland was to be retained there. No explicit Imperial contribution.		1911 to overcome the defeat in the House of Lords in 1913 by 326 votes to 69. Received Royal Assent in September 1914, but implementation was immediately postponed until after the completion of the War.
1920	Tax bases and rates were set at Westminster and revenue collected was held on Northern Ireland's account. Some taxes were under defined as transferred taxes where Westminster set the bases and Northern Ireland had control over rates. Only in areas where there was not substantially similar UK taxation could Belfast set both tax bases and rates. Northern Ireland's share of Imperial expenditure was determined by a Joint Exchequer board consisting of one representative of the UK government, one from the government of Northern Ireland and a chairman appointed by the	Irish MPs to be reduced to 42. Following the establishment of the Irish Free State there were 13 MPs returned from Northern Ireland.	Passed as the Government of Ireland Act 1920. Those parts of the Act referring to Southern Ireland were superseded by the civil war, Anglo-Irish Treaty and establishment of the Irish Free State.

	Crown. It would determine the contribution based on Northern Ireland's taxable capacity then pass the remainder collected on Northern Ireland's account at the Treasury from reserved and transferred taxation for expenditure on services in Northern Ireland provided by both the UK and Belfast governments.		
1978	Neither the Scotland Act 1978 nor the Wales Act 1978 contained any statements on the process of financial transfers other than that payments would be made by the Secretary of State to the appropriate Consolidated Fund with the consent of the Treasury. *Devolution: Financing the Devolved Services* and *Needs Assessment Study: Report* indicated that some form of objective assessment was to be undertaken on the basis of the costs of providing a standard level of service in all parts of the United Kingdom. Once determined those funds would be available to the assemblies to be spent as they saw fit. No taxation powers were to be available, although borrowing within limits to ensure macroeconomic stability would be permitted.	Representation retained at 71 existing seats in Scotland and 40 in Wales.	Passed in Parliament with the agreement to enact following a popular referendum, but an amendment required a minimum of 40% of Scotland's registered electors to vote in favour otherwise the Act would be repealed. This threshold was not reached as 51.6% of those voting were in favour but this represented only 32.9% of the electorate. The Act was repealed in 1979. The Wales Act was passed in Parliament, but the required referendum only gave support from 20.8% of those voting and the Act was repealed later in the year.
1998	Neither the Scotland Act 1998 nor the Government of Wales Act 1998 contained any statements on the process of financial transfers other than that	Initially 72MPs were retained, but following a recommendation from the Boundary	Both the Scotland Act 1998 and Government of Wales Act 1998 were passed by

	payments would be made by the Secretary of State to the appropriate Consolidated Fund with the consent of the Treasury. The existing block and formula system commonly known as the Barnett formula would be used to determine changes in the allocation of the budgets to the devolved administrations from Westminster. This represented a continuation of the pre-devolution system with payment being made to the devolved parliaments/assemblies rather than the Secretary of State.	Commission for Scotland the number was reduced to 59MPs, in line with the national average per head of the population. Wales retained 40MPs.	Parliament after popular consent had been indicated in referenda in 1997, although in Wales the majority in favour was only 0.6%. In Scotland 74.3% supported a Scottish Parliament and 63.5% supported tax raising powers.