HOUSE OF COMMONS

Scottish Affairs Committee

Oral evidence: The Referendum on Separation for Scotland, HC 140 xxii

Tuesday 6 May 2014

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Watch the meeting

Members present: Mr Ian Davidson (Chair); Graeme Morrice; Pamela Nash; Sir James Paice; Mr Alan Reid; Lindsay Roy

Questions 5450 - 5615

Witnesses: **Rt Hon David Mundell MP**, Parliamentary Under-Secretary of State for Scotland, Scotland Office, and **Steve Webb MP**, Minister of State for Pensions, Department for Work and Pensions, gave evidence.

Q5450 Chair: I welcome everybody to this meeting of the Scottish Affairs Select Committee. As you will probably be aware, we are conducting a series of hearings into various aspects of the consequences of separation. Today we are looking at the Government's "Scotland analysis: Work and pensions" paper. As ever, we have with us David Mundell from the Scotland Office. He has a special friend with him today—another special friend—Steve Webb, who is dealing with pensions, so big questions.

One of the key arguments in the paper is that higher social security in Scotland is more affordable if we remain part of the United Kingdom. Could you clarify why you believe that is the case?

Steve Webb: One of the things about social security is that it is done well at scale, particularly given the cyclical nature of the demand for working-age social security. We have recessions, growth spurts, banking crises and all the rest of it, so the bigger the base on which you are trying to build a system, the more robust it is and the more stable it will be for the citizens. Trying to do anything on the basis of a population a tenth of the size simply gives you greater volatility. That is the first thing.

The second, therefore, on the pensions side—which is more my area—is that the whole infrastructure that we have put in place for UK pensions policy works at scale. We have a Pension Protection Fund to protect your pension when companies go to the wall. The scale at which we can do that means that, if a big firm goes to the wall, it bounces off—it is small relative to the whole thing. If you try to do it at a tenth of the scale—if a big Scottish employer goes to the wall and you have a Scottish protection fund—it is much more volatile and has a much bigger hit. Risk pooling, risk sharing and scale are a key advantage for the citizens of the United Kingdom.

Q5451 Chair: A word like "volatility" does not necessarily mean a great deal to people in the street. What does volatility mean in that context?

Steve Webb: For example, if you have a sudden downturn, across the UK the economy as a whole can absorb that, so taxes do not suddenly have to go up or benefits do not suddenly have to be cut; you can take the long-term view. If you are operating at a tenth of the scale and something goes wrong—if there is a hit and a big company goes down—suddenly there is a big hole in the finances relative to the tax base, which could mean a sudden tax increase or a sudden cut in spending somewhere else, just to keep things on an even keel.

Q5452 Graeme Morrice: Good afternoon, gentlemen. What about the argument that is sometimes made that in an independent Scotland pensions would be cheaper because the life expectancy of pensioners is lower compared with the rest of the UK? How would you respond to that?

Steve Webb: The baseline, taking account of the point you have made and given lower average life expectancies in Scotland—of course, those vary hugely across Scotland, as you know—is that Scotland has a slightly higher proportion of pensioners to begin with than the UK a whole. The worldwide factors of increasing longevity are at least as true in Scotland as they are in England. For example, over the period from 2010—the most recent figures are for 2010—to 2030, the life expectancy of a man at 65 will rise by 2.5 years in England and 2.6 years in Scotland. The cost pressure is just as great—if not greater—on the demographic side, and the working-age base to pay for it is less favourable, because a lot of the adult population of working age in Scotland are in the 50-to-65 bracket. You are going to lose those people from the working-age population. The cost pressure is just as great and the tax base to fund it is less robust.

Graeme Morrice: That is very useful.

Q5453 Chair: It has been argued that it is simply more affordable in Scotland to drop the pension level because people die quicker. On the face of it, that seems to be a not unreasonable point. Surely you can have a lower starting age if you have to pay it for a less long period. In those circumstances, surely it would be feasible for Scotland to drop the pension age compared with the rest of the UK.

Steve Webb: We are saying that if you look across the whole of social security spending in Scotland compared with the UK, in the current system, taking account of lower Scottish life expectancies, we are already paying slightly more per head of working age in Scotland than we are in the rest of the UK. There is a whole raft of different factors. That baseline situation will deteriorate substantially. To meet those long-term demographic pressures, the UK Government are having to do things like raise state pension ages. If Scotland did not do that, they would have to find far more money from the working-age population. Starting from where we are, Scottish life expectancies will improve just as fast as in the rest of the UK, and Scotland's ability to pay will not improve relative to the rest of the UK.

Q5454 Chair: Can I clarify whether or not your argument is that it would be possible for pensions, if dealt with in isolation, to be treated differently? It is taking all the other benefits together with pensions that would make dealing with pensions separately difficult.

> ***Steve Webb***: There is ring-fencing pensions, which is your question. There are pressures arising on the state pension side, but there are also pressures arising on the public service pension side. Because we are linking public service pension ages to state pension ages, if you eased off or reduced Scottish state pension ages, that would have a knock-on effect on the public service pension schemes as well, and they are already in deficit in Scotland.
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> If I may, I will give you a couple of figures that I have dug out specifically for Scotland. If you look at the NHS and the teachers' pension schemes, and the Scottish members of those schemes, both of those, as the Committee will know, are unfunded. There is no pot; today's working teachers and nurses are paying for today's retired teachers and nurses. In the year that has just ended—2013-14—the Westminster Government subbed the Scottish teachers and nurses £300 million. The Westminster Government paid out, or the schemes paid out £2 billion to Scottish retired teachers and nurses, but got in £1.7 billion from the workers and their employers, so there was a £300 million hole last year. By 2018, that hole will be double—it will be £600 million.
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> In the UK context, the UK Exchequer will have to find that. If it is in a Scottish context, there will be unfunded promises, or Scottish teachers and nurses will have to pay more, or there will be less money for nurses in the Scottish NHS or for schools. If you look at all of those unfunded pressures together, they mean that reducing or not increasing the state pension age would be completely unsustainable.

Q5455 Chair: Can I clarify the point that you made about there being a £300 million hole that, as you put it, is subbed from the Treasury? Is it only Scotland that is subbed from the Treasury, or is the rest of the UK subbed from the Treasury as well?

> ***Steve Webb***: Absolutely. That is the Scottish share of the sub from the Treasury to the whole UK system.

Q5456 Chair: Is the Scottish sub bigger proportionately than the rest of the UK's sub? You can understand the argument. If everybody is subbed, the argument will be that Scotland separated would not be comparatively worse off—leaving aside the issues about sharing and so on.

> ***Steve Webb***: I am pretty sure that the doubling in five years that I mentioned is particularly acute; you are doubling from £300 million to £600 million. I will supply the Committee with the UK-wide figures, but I am pretty sure it is particularly acute, for the reasons we have talked about—the faster ageing of the Scottish population.

Q5457 Mr Reid: In the event of separation, how would you decide whose pension will come in the future from the Scottish Government and whose pension will come from the UK Government? I am talking about the state pension.

Steve Webb: We already have rules about what happens to pensions where somebody has, for example, spent some time in the UK and spent some time working in another EU country. They are complicated. If you have worked in France, some of your French contributions count a bit and some do not; it is messy and complicated. There would have to be a negotiation—a conversation—about that.

The classic issue would be people who had worked in both countries. If I have worked in Scotland and in England and I retire in one or the other, how are the rights I built up in the other scheme valued and transferred? That would all have to be negotiated. One of the things people want with pensions is certainty. They want to be able to plan ahead for their retirement—to know what they are going to get and when they are going to get it. For me, creating separation casts a whole lot of uncertainty and doubt on people's retirement planning. It is all subject to the outcome of negotiations—and we just do not know.

Q5458 Mr Reid: What about somebody who has worked for all of their working life based in Scotland but for a company whose head office is in England, and their pay cheque came from that head office? How do you work out where their pension comes from?

Steve Webb: That is a very good question. If the company is headquartered in England and you have worked in Scotland, on the company side of it there will be cross-border schemes. The European Union looked at this issue. There was some suggestion that they might back off—they didn't—on the rules on funding cross-border schemes, so there is a rule that says that, within two years from the point of creation, those schemes have to be fully funded. If you work for a firm that suddenly has to fill a hole in its pension scheme, where does that money come from? Potentially, employers will suddenly have to find money to fill gaps in their pension scheme or close pension schemes. Again, it is a cost and an uncertainty that I am sure Scottish workers would rather not face.

Q5459 Mr Reid: In terms of the state pension, what you are saying is that there are no rules or guidelines; it would simply be two Governments sitting down and negotiating.

Steve Webb: Yes. If you leave the UK and retire to Spain, say, we pay you your UK pension in Spain. That is not problematic. But if you have done some of your working life in Spain, and some of your contributions are Spanish contributions, there are all sorts of convoluted rules, which can differ between EU and non-EU and all the rest of it. It is convoluted and difficult, and the outcome of those negotiations is unclear to me.

Q5460 Mr Reid: Let us look at the state pension aspect of the person who worked in Scotland but for a company that was based in England. You as the UK Pension Service will have no records saying where that person's place of work was, so how do you decide who is responsible for his state pension?

Steve Webb: That is right. They will have put UK national insurance contributions into a pot. Currently we do not record, or have any reason to record, on our systems the location of the workplace and of the head office. We do not need that information. Trying to disentangle all of that would be exceptionally difficult.

Q5461 Mr Reid: If there are no guidelines, clearly each party to the negotiations will want to come out of them paying out as little as possible. Have you any view as to how those negotiations would be conducted?

Steve Webb: I am guessing that I am not the first witness who has said to this Committee, "I have a feeling that the lawyers will have a field day." If anybody thinks that perhaps they have a smaller pension than they would have got, or something like that—

Q5462 Mr Reid: If somebody who is living in Scotland wants to keep their UK citizenship, will that have any impact on their pension, or is their pension purely to be determined by where they worked?

Steve Webb: At the moment, the only thing that determines how much pension you get is how much national insurance you paid in. You do not have to be British to get a British pension—you can be anything. If you have paid British national insurance and have satisfied the minimum contribution rules, you get a pension from the UK Government, whether you are a UK citizen or not. Citizenship does not matter from the point of view of paying pensions.

Q5463 Mr Reid: For winter fuel payments, presumably citizenship does matter.

Steve Webb: We have reviewed the rules on winter fuel payments; where you live is part of that story as well. We have excluded very hot places, which may be less of an issue in this context, but winter fuel payments are a tiny fraction of the total budget. The big budget item is the state pension.

Q5464 Mr Reid: If people living in Scotland chose to keep UK citizenship, would they be entitled to a UK winter fuel payment?

Steve Webb: My assumption would be that winter fuel payment policy would be a matter for the continuing UK Government for its own citizens. The Scottish Government would decide whether it wants a winter fuel payment system and wants to pay for it, according to the people living in Scotland when they reach the eligible age.

Q5465 Mr Reid: In summary, would it be fair to say that it is all very complicated and that you have no clue as to how these negotiations will go?

Steve Webb: Absolutely. You have got there ahead of me.

Q5466 Chair: Can I seek clarification on a couple of points? It seems to me that there are two areas of uncertainty. One is the question of who pays for a pension once it is settled—whether it comes out of Scotland's pot or out of the rest of the UK's pot. That is deeply boring. You have people in your Department who will specialise, no doubt, in those sorts of things.

I am not clear about whether that has any direct impact upon individuals, other than at one remove, in the sense of how much money is then available to Government; unless I am mistaken, it does not. What I am not entirely clear about is whether or not there would be any impact, as a result of this uncertainty about the rules, upon the amount that the individuals received, as distinct from the question of who was paying for it. Can you clarify for us whether or not there would be justifiable anxiety about what the amounts that people might receive would be?

> ***Steve Webb***: Yes. The continuing UK has a set of rules for converting past national insurance contributions into pension entitlements. In the event of separation, the first question will be how any years of service after separation convert into state pension rights. That will be a matter for the future Scottish Government, so we will not know what they are going to do with those.
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> Clearly, we will continue to apply our rules to people who stay in the UK. It's difficult. You would have to have a conversation about the way that past national insurance service turned into a pension right. As I said, you do not have to be a UK citizen to get a UK pension, so obviously we would pay a pension to the people who had put national insurance into our system, wherever they lived. Separation would not affect that, but what happened post-separation would be a matter for the future Scottish Government.

Q5467 Chair: Post-separation—going forward—I can see that the Scottish Government would have to devise a pension system; I understand that. If you are saying, as I think you are, something new—that if people had paid into the national insurance system they would, in a sense, inherit a payment from that national insurance system—presumably that would mean that the liabilities and assets would stay with the United Kingdom Government, rather than be divided.

> ***Steve Webb***: No. That would have to be a matter for negotiation. To give a simple example, if someone has worked all their life in England and retires to Scotland, can you just assume that the continuing UK Government will pay the whole cost of that pension? There is a liability to pay a pension—or they have built up an entitlement—but the split of funding of that is for negotiation.

Q5468 Chair: The split of funding is unclear only inasmuch as who actually pays it.

> ***Steve Webb***: Yes.

Q5469 Chair: It is not unclear as regards what people would get.

> ***Steve Webb***: Up to the period of separation. You could retire to France, and we would just pay you a pension. Where you end up is not material, because you have paid into the system.

Q5470 Chair: Fine. People in Scotland will be anxious about whether or not their pensions are secure in the event of separation. I think that you are saying to us that their pensions will be secure, because if they have paid in, they will get out. The question of whether or not that comes from a separate Scotland or the remaining UK will have to be devised by a scheme as yet undetermined, but the individual can be secure in the knowledge that they will get their money.

Steve Webb: I know that you know this, but I stress that we are talking about state pensions only. The position of private pensions and public service pensions—

Chair: That's right—we're sticking with the state pension.

Steve Webb: Just on the state pension, people have built up a right, wherever they retire, in respect of service for as long as they are paying into the UK national insurance system.

Q5471 Sir James Paice: I was going to pick up the point about where people retire, but the Minister answered that with his reference to people who retire to France or Spain. Can we clarify that, when we talk about entitlement, that is to a state pension? The level of that state pension, though, is not predetermined. If somebody retired from England to Scotland, they would obviously get the state pension as decided by the Government here at Westminster. Should we not be clear that if they were the Chairman's Scottish pensioners, who had earned their pension in Scotland, although they might be entitled to a state pension, the level of that state pension would be set by the Scottish Government?

Steve Webb: My argument is that, to take the example of a Scottish person who has paid in all their life and then retires to France, they still have an accumulated pension right in respect of the national insurance they paid in when they were part of the United Kingdom. That is the key point.

Q5472 Sir James Paice: But if they have stayed in Scotland, are they entitled to the UK level of state pension, or to the state pension, whatever it would be, as set by the new independent Scottish Government?

Steve Webb: Inevitably, with all these things there is a bit of "Who knows exactly what would happen?" My presumption would be that, because they had paid into the UK national insurance system prior to separation and built up a set of service—my lawyers always tell me not to call them rights—which under our rules converts into a pension under the rules prevailing at the point they draw it, they have banked that bit because of their national insurance contributions to the UK system.

Q5473 Sir James Paice: Yes, but, in the future for Scottish workers who were still working and were not yet entitled, the remaining entitlement that they built up after independence would be at the behest entirely of the Scottish Government.

Steve Webb: Absolutely.

Sir James Paice: That is all I wanted to clarify.

David Mundell: It is also important to understand in this context that the Scottish Government have announced that they would not go ahead with putting back the pension age, so they themselves would be entirely responsible for funding a different age for the start of the state pension. The cost of funding a different, earlier age at which you become entitled to the state pension has been estimated to be around £6 billion.

Q5474 Chair: In this discussion, particularly about pensions, I am trying to distinguish between, on the one hand, these big figures about Governments paying things—at some stage, somebody somewhere will add those up and work out what is affordable and what is not—and, on the other hand, how they impact on individuals. I think you are saying to us that in the event of separation the state pension of any individual in Scotland would not be adversely affected—that they would continue to get the same level of state pension as everyone else in the UK. The question of how that cost is allocated between Scotland and the UK is a matter of haggling, process and all the rest of it, but people themselves can be assured that their pensions are secure. Taking your point, David, if the Scottish Government then decide to increase the pension, they will have to meet the entirety of the costs, since it would be patently unreasonable for them to be able to decide to pay out more and to have somebody else pay in for it. Is that an accurate reflection of the position?

Steve Webb: Yes. They have accumulated rights in the UK system, under the UK system's rules, to a pension, and as David says, at the age at which we would have paid it to them, not at the age the Scottish Government want.

Chair: You are being passed notes correcting that, possibly. In the meantime, Alan will ask you a question.

Q5475 Mr Reid: Under the current rules, how many years does somebody have to work in the UK system in order to be entitled to a full state pension?

Steve Webb: We are introducing a new state pension regime in 2016, which I suspect is the relevant one for the purpose of this conversation. That is 35 years for a full pension.

Q5476 Mr Reid: Let us take the hypothetical case of somebody who left school at 16 and worked for all of their working life. By the age of 51, they would be entitled to a full pension. Let us suppose that they reach 51 at the separation date. They are now entitled to a full United Kingdom pension, but they are living in Scotland, have always lived in Scotland and are a Scottish citizen. Will they get that pension from the UK Government or will the Scottish Government become responsible for paying it?

Steve Webb: Citizenship is irrelevant. It is: what have you put into the UK national insurance system prior to separation? Answer: 35 years. That builds you up a right to a full UK pension under the continuing UK rules, so they are entitled to that money. The question is, who is paying for it and how is that split? But they are entitled to that money.

Q5477 Sir James Paice: But not at 51.

Steve Webb: No, not at 51.

Q5478 Mr Reid: But if they are in Scotland and during the next 15 or 16 years, between their being 51 and their retirement, the Scottish pension rules diverge significantly from the UK pension rules, what happens? Does that person then get their pension at the age that the Scottish Government determine or at the age that the UK Government determine? What about annual increases? Who determines the annual increases?

Steve Webb: That is a good question. It is a different question, but an important one, so let us dwell on that for a moment. Annual increases are a matter of annual discretion, beyond the legal minimum. You do your service in the UK scheme and build up a set of rights in the UK scheme, but the indexation of it post-retirement would be a decision for the continuing UK, if that is the scheme where you built up your rights. Your pre-separation service would be indexed according to whatever principle the continuing UK was using for people who had paid into the scheme. If the Scottish Government wanted to do something, say, more generous, they would have to find the difference.

Q5479 Mr Reid: Or if they did something less generous, there would not be a saving. Would they be able to do something less generous?

Steve Webb: In respect of post-separation service, they could do what they liked.

Q5480 Mr Reid: Obviously this is going to be a very big item in the negotiations. To get a handle on how big it would be compared with other items, do you have a figure for the total liabilities as far as the state pension is concerned?

Steve Webb: We tend not to add up the whole future-ever liabilities for state pensions for Scotland. We tend not to do it very often on a UK basis, if we can help it, because of the numbers. Even I think that trillions are a bit scary. There is a number coming my way. Just to give you a feel for scale, we think that there is probably £100 billion of unfunded Scottish public sector pension liabilities that would have to be paid by someone. We are talking about literally hundreds of billions of pounds and vast numbers of promises that, essentially, are always paid in-year. That is the point.

Q5481 Mr Reid: How big is this figure in comparison with the accumulated national debt, for example?

Steve Webb: Which figure?

Mr Reid: We are still talking about state pensions. I do not know whether that piece of paper gives you a number for the liabilities for state pensions.

Steve Webb: In very round numbers, at the moment at UK level we are spending of the order of £100 billionish on state pensions, give or take—

Q5482 Mr Reid: Did you say £100 billion?

Steve Webb: Yes. It is slightly less than that. The national debt is well over £1 trillion, but these are still very large numbers relative to the national debt.

Q5483 Pamela Nash: What estimate have the Government made of the costs of the promises that the current Scottish Government made in the White Paper for pensions going forward?

Steve Webb: Taking the Chair's injunction to earth this in things that mean something to people, not the trillions and billions stuff, we have said, "What would be the cost per working-age person?" For example, if it were all funded through taxation, what would the extra tax bill be? We estimate that it would be just over £200 a year. Leaving the demographics—ignoring the fact of the ageing population and all the rest of it—if you just take the promises like holding off on 67, keeping the savings credit and having transitional protection in the single tier, and all that kind of stuff, the big-ticket items, the tax hit is of the order of £200 to £210 a year on the average Scottish worker.

Q5484 Pamela Nash: Do you think that the policies that have been announced in the White Paper and otherwise by the Scottish Government will impact on how individual Scottish people save privately for their future?

Steve Webb: Certainly in terms of private pension saving, I have some serious misgivings about what separation would mean. I will run through one or two of those. Something that the UK Government have done very successfully is automatic enrolment into workplace pensions. We started with the biggest firms and we are working our way down to the smallest firms by 2017 or 2018. One of the key elements of that is that every employer has the NEST Corporation to go to. We have given the employer the legal duty to put their workers into a scheme, but we have to make sure that there is a scheme that is willing to take them. As you get to the smaller employers, the big providers are just not interested, so we created NEST with a public service duty to take the business.

If we roll forward, separation happens and the Scottish Government think that auto-enrolment is still a good thing—it seems to me an extraordinarily good thing—they will have to make sure that small Scottish firms have somewhere to enrol their work force. NEST, as a UK body, would have no legal duty to take Scottish employers. The suggestion is that you would create a Scottish NEST, but think about the lead times for all of this. We had the Turner commission over a decade ago. NEST was only set up in 2012. We—the Government—had to lend NEST hundreds of millions of pounds to get started. We had to negotiate it with the EU, because of state-aid issues. Setting up a Scottish NEST would require, first, a lot of money up front, and secondly, negotiation with the EU—if they were in the EU.

I think auto-enrolment would come to a grinding halt. If separation happened soon, I think that auto-enrolment would screech to a halt and that—to answer your question—there would be a set of Scottish workers working for small firms for whom auto-enrolment just could not happen, because there would be nowhere to auto-enrol them. That would be very damaging. Let us say you are a worker in a small Scottish firm and do not have a pension. If you carry on with the UK, auto-enrolment carries on and you get a pension for the first time. If we have separation, who knows what will happen? It could be years before a

Scottish NEST is set up. It would struggle to be as good value for money as the UK-wide one, because it would be a tenth of the size. On the private pensions side, it could be seriously damaging.

Q5485 Pamela Nash: As a layperson on this, I appreciate that we could probably have a full session on the issue. As briefly as you can, could you say exactly why NEST was absolutely necessary for auto-enrolment to be set up? Could a Scottish Government come up with a quicker alternative to create that system?

Steve Webb: The short answer is profit. If I am a Scottish employer with one relatively low-paid employee, the amount of pension contributions going in each year could be a few pounds; it could be tens of pounds—tiny amounts of money. By the time the provider has taken their 0.75%, which is going to be our new cap, it will be a tiny, tiny amount of money. Most providers would run a mile, because you cannot make any money out of it.

Because we have given firms a legal duty to choose a scheme for their workers, we have to make sure that there is one. It is a bit like posting a letter to the Orkneys. It is a public service duty; you have to take it. NEST is legally obliged to do that. The Scottish Government have talked about a SNEST—a Scottish NEST—but it took us years to get the thing going. We had to lend large amounts of money; we had to negotiate and all the rest of it. It is a UK-wide scheme and it will have 3 million or 4 million members by the time it is up and running. If you do that at a tenth of the size, with the same fixed costs, can you even deliver it at the pension charges we are talking about? I would be a concerned employee of a small Scottish firm and would think that my chances of getting into a decent-quality workplace pension would be substantially harmed by separation.

Q5486 Pamela Nash: We may come on to that a bit later. I had not intended to go down the auto-enrolment route, but thank you for that information. I was thinking more in terms of individuals. You said that the extra cost to the Government would be £200 per year per head. Just to be clear, by £200 per head do you mean £200 per working person?

Steve Webb: Yes.

Q5487 Pamela Nash: To me, that does not sound very sustainable. Would you agree?

Steve Webb: I would. It is easy to say, "Maybe we wouldn't put state pension ages up. Maybe we'd keep the savings credit. Maybe we'd do this; maybe we'd do that. Maybe we'd start the new single-tier pension a few pounds a week higher." Those are all nice things, but as we are discovering with pensions, everything has a lot of zeros attached to it. They are very attractive-sounding promises, but essentially what we are doing is promising good things for the retired population at the expense of the working population. Within a couple of decades, they are costing the working-age population hundreds of pounds.

Q5488 Pamela Nash: My view would be that, if these promises are made and cannot be kept, individuals may not save as much for their retirement and may find later on that that is a mistake.

Steve Webb: I see your logic. You think you are going to get a pension earlier than you eventually do and that it is going to be higher than it eventually is, and you plan on that basis. I take the point. You might under-save privately in anticipation of a more generous state pension that never materialises.

Q5489 Pamela Nash: I want to touch on migration. Clearly, migration is essential for Scotland when we are looking at the future of Scotland and of pensions. Is there a figure that the UK Government have been using as an assumption to calculate this?

Steve Webb: Yes. The figures have been calculated on the basis of a set of core migration assumptions, but we have also tested the sensitivity. For instance, you asked what the cost of the pension promises was, and I said £210 per working-age person. If you add the demographic pressures—an ageing population and all of that relative to the working population—that is another £200, so you end up at £410 just on the pensions side. We think there is about another £40 on the working-age side. I will come back to migration in a second, but our headline number is £450 per working-age person to pay for demographics and the Scottish Government's promises. If you thought migration would be bigger—if you took higher migration—that £450 might be £420. Obviously having more working-age people come from outside the country helps a bit at the margins, but it does not change the fundamental story.

Q5490 Pamela Nash: Just to be clear, £210 was just the cost of the promises from the Scottish Government; £450 was including demographics.

Steve Webb: Yes—demographics and a bit of working age as well.

Q5491 Pamela Nash: So you think it would only bring it down by about £30.

Steve Webb: Maybe £30.

Q5492 Pamela Nash: What level of migration would that be?

Steve Webb: As I recall, the migration estimate that has been used is about 15,000 a year. Over a decade, it is migration of something like the size of the population of Dundee.

Q5493 Pamela Nash: How much additional migration would be needed to equalise things?

Steve Webb: I suppose you could argue that if—

Pamela Nash: I am sure I could it work out by extension from these figures, but if you have it to hand that would be preferable.

Steve Webb: I haven't. The short answer is implausible levels. At any plausible level of migration, there is still a significant hit on the working-age population.

Pamela Nash: We would need to more than fill the highlands to sort that out.

Q5494 Chair: The figure that was used by one of our colleagues was that by 2050 it would be just under a million. Does that seem to you to be a reasonable sort of figure? Inward migration would require to be just under a million—930,000, if I remember correctly—by 2050.

Steve Webb: To achieve what?

Q5495 Chair: To have the number of people paying into pensions to be able to fund them at the existing levels.

Steve Webb: The main comparisons that we have used assume net inward migration of just over 11,500 a year for Scotland. That is the sort of scale that we have been assuming. As I said, the kind of scale that you would need to dwarf these underlying pressures is huge. I could not tell you whether it is exactly a million, but it would be huge relative to the numbers we have used.

Q5496 Chair: Can I clarify again this question of £450 per person per year? It has been suggested that there are lots of people in Scotland who would sell their granny for £500 a year, but this is £450 of it relating to pension obligations alone. Is that correct?

Steve Webb: This is principally about pensions. It is a bit about working-age, but overwhelmingly about pensions. There are two things—the demographic pressure and the unfunded promises. Once we get to that point, that is the bill every year.

Chair: That was pensions in general. Can we move on to look a bit more at public sector pensions? Alan wanted to pick up some points, some of which we touched on earlier.

Q5497 Mr Reid: I want to look at public sector pensions. Let us take what are probably the easier ones first—the funded schemes, which I think are largely the local government schemes. Would somebody in a funded scheme see any change if separation happened?

Steve Webb: Again, it would be a very messy thing to disentangle. For example, suppose that you live in the continuing UK post-separation but you worked at some point for a Scottish local authority. Presumably you have a property right on that Scottish scheme. In general, funded pensions are a lot easier because there is the sense of a property right—there is an asset and all the rest of it.

What I want to try to convey is the complexity of disentangling this stuff. Let me give you a simple example. People get divorced. One of the ways they deal with pensions after divorce is that one of the partners gets a claim on the other person's pension. They do not take money out at the time; they just say that this will be paid when they retire. If they live on both sides of the border, this scheme is paying this person because they got divorced.

I do not know the answer to most of your questions. I try not to come to a Select Committee saying this, but many of these things are unknowable until you have that discussion and negotiation. What would be the legal position? What would be the result of a negotiation? One of the things that we are keen to stress on public service pensions is that this is part of a whole. It is not just NHS pensions; it is the NHS and NHS pensions seen as a whole. Who employs everybody will have an effect on the pension side. We cannot segment off just the pension bit of this; it will have to be part of a whole story.

Mr Reid: That was meant to be the easy bit. Turning to the more complicated area—

Q5498 Chair: Before we move off the easy bit, can I be clear? If a public sector pension is fully funded at present, there should be no difficulty, because the liabilities and the funding will simply move together to a separate Scotland. Where there is a deficit, it will become the responsibility of a separate Scottish Government. All of that seems remarkably straightforward to me. I understand that there is a difficulty about partial payments and so on.

Steve Webb: In reality, local government pension schemes in general are chronically underfunded, so we're not going to be talking about fully funded pension schemes. Then there will be an issue—

Q5499 Chair: I understand that. If they are not fully funded, the liabilities transfer. The Strathclyde, the Lothian or some similar pension scheme in Scotland simply transfers to the Scottish Government, and they would inherit the liabilities.

Steve Webb: No. We need to be careful. If it is a genuine pension fund, the fund has to pay the pension, and it has to get the money from somewhere. The fund has taken in contributions and has to pay a pension to members of the scheme, wherever they live. What if it does not have enough money? It will have enough money in-year to pay this year's pensions, because it has billions of pounds, but if its pension fund hole is getting worse, because people are living longer or the stock market is falling, how on earth do you carve up that deficit? There are a thousand different ways of measuring it and a thousand different outcomes, I suspect.

Chair: There are a number of finite and identifiable Scottish public sector pension schemes that are distinct from the ones that are cross-border. Those are the ones that I was identifying.

Q5500 Mr Reid: Ultimately, would the money not come from the local authority?

Steve Webb: At the moment, scheme members pay in, if they are still employed. Potentially, the local authority pays in, if it is still actively employing people. Let me give you the example of what they call in the jargon a deferred member—you used to work for a Scottish local authority. At the moment, there is no money going in from you or from the employer. You have a pension promise that you expect to be kept, and there is not enough money in the scheme to pay those liabilities. Who is going to pay that shortfall?

Mr Reid: We are asking the questions.

Steve Webb: And the answer is, “I don’t know.” If they now live in England, is that a UK problem? If they have retired to Scotland, does it become a Scottish problem? There wasn’t a deficit when they retired; the deficit happened since. Suppose that it is fully funded at the point of separation and then deteriorates. If a new deficit arises, as they do—obviously pension funds go up and down—who is responsible for that? There is no obvious right answer to any of these questions. There is no simple principle that sorts all this stuff out. It will be hugely uncertain, hugely complicated and will take ages to sort out.

Q5501 Mr Reid: If we stay in the UK, who is responsible for making the payments?

Steve Webb: The scheme is responsible for making the payments. Each year employers and employees put money in. In general, the UK Government has overseen the process of making sure that pension funds are properly funded, where there is a fund, but, as you know, in most public service schemes there is not even a fund.

Q5502 Mr Reid: Let us turn to what I think will be a more complicated area—the unfunded schemes. We touched on this earlier. I think I am right in saying that, other than the armed forces and the civil service, the schemes are all clearly identifiable as being separate Scottish schemes—for example, for teachers and the national health service. Is that correct?

Steve Webb: That is right. The NHS and the teachers, in particular, have a separate and identifiable set of Scottish members and so on.

Q5503 Mr Reid: If separation happened, would the Scottish Government be responsible for the Scottish schemes and the UK Government responsible for the English, Welsh and Northern Ireland schemes? Is that a fair comment?

Steve Webb: I am keen to stress that we do not see the public service pension schemes as being a kind of free-floating thing over here, and there’s an answer to that, with what happens to the NHS, in particular, being somehow over there. There is a whole set of costs, assets and liabilities that we think would be negotiated as a whole. You would not carve up the NHS pensions and say, “That’s over there. That’s done and dusted.” I know more about the English NHS, which is employing charities—voluntary and third sector groups—whose pension rights are different. You have to look at the whole thing; you cannot just section off the pension rights.

Q5504 Chair: Yes, but surely things like the NHS—as distinct from, say, defence—are very much geographically based, so it is much easier to make allocations there than for something like defence, which by its very nature covers the country as a whole.

Steve Webb: Again, I would caution against thinking that any of this is straightforward. I do not think that any of it is. For example, Alan talked about Scottish citizens, Scottish residents and Scottish employees. You could make different arguments on all of those bases that would come up with different answers. What if when you were in the scheme the rules were these and subsequently they were changed? Carving all of this up will not be straightforward. I am sure of that.

Q5505 Sir James Paice: Can we have clarity? In your answer just now, you referred to the NHS scheme as part of the NHS more widely, and you implied that in the event of independence the arrangements for different public sector schemes could be different.

Steve Webb: Yes.

Q5506 Sir James Paice: So the arrangements for the NHS pension scheme could be different from those for the teachers or one of the others.

Steve Webb: Yes.

Sir James Paice: I just wanted to have that clarified.

Q5507 Mr Reid: Do you have figures for the liabilities for the purely Scottish public service schemes, as opposed to the equivalents in England and Wales?

Steve Webb: Yes. This was the £100 billion figure that I was quoting. We do not have a very precise number, but from memory the UK-wide liability is £1 trillion or so—what is £1 trillion among friends? The Scottish share of unfunded public service pension liabilities is thought to be of the order of £100 billion. Obviously that is spread over decades and decades; it would not fall due in one go. As the Chair said, that will have to be met in any case. Somebody has to pay for those pensions, but they are huge.

Q5508 Mr Reid: In round figures, the Scottish share of the liabilities is 10% of the UK total.

Steve Webb: Of that order.

Q5509 Mr Reid: That is significantly more than Scotland's share of either the population or the GDP. Is that correct?

Steve Webb: Yes.

Q5510 Mr Reid: Why is that?

Steve Webb: One of the issues is the relative size of the public sector in the continuing UK and in Scotland. Another is relative wage levels. There is a whole raft of different factors, but we come back to the issue of increasing life expectancies and so on. If life expectancy rises at proportionately different rates, that has a bearing as well.

Q5511 Mr Reid: Do the figures for increasing life expectancy that apply to the population as a whole apply to teachers and nurses?

Steve Webb: I did not so much mean public service workers. Obviously that would be the right number to use, but we do not have it. Earlier I said that the average man at 65 will see an improvement in their life expectancy of about the same amount in England and in Scotland, but percentage-wise it is a bigger increase in Scotland because they start from a lower base.

Q5512 Mr Reid: You mentioned that the liabilities per head of population are higher in Scotland. You also said that public spending in Scotland is higher than in the rest of the UK. Is the share of liabilities broadly similar to the share of public spending?

Steve Webb: I do not know. We could have a look at that and come back to you on it.

Q5513 Lindsay Roy: This whole area seems to be a bit of a minefield. How would public sector pension schemes that apply across the UK, such as that for the civil service, be disaggregated? Can you give us an estimate of how long that would take?

Steve Webb: In one sense, disaggregation is simpler if there is not a fund—possibly with a deficit, because that raises different sets of issues—but I anticipate that these things will take years to disentangle. Whenever I have a meeting in the Department about pensions, I always say that, if there are two lawyers in a room, it is bad news. Buy shares in pensions lawyers, because it will take for ever to sort out all this stuff. There are issues about the rights you have built up under the scheme, but the crucial uncertainty is who is actually going to pay the bills. These pension promises have been made and they should be honoured, but there will be arguments about who will pay for them.

Do we even have the data? As I said a moment ago, very often you do not record data that you do not need. If I am a member of the civil service, whether I work for the Pension Service in Dundee or in Burnley does not matter—I am building up the same rights. We may not even know, for example, where somebody was when they did the work, if they are in a UK-wide scheme.

Q5514 Lindsay Roy: Are you saying that new systems would have to come into place?

Steve Webb: Would it even be possible to do? If you felt that the right way to carve things up was to look at where people were working when they contributed, you might not even have gathered the data. Potentially you might be trying to gather data on the working history over decades for millions of people.

Q5515 Chair: Can I be clear? I appreciate that this is enormously complicated and could potentially generate employment for the undeserving. None the less, it would not necessarily impact upon people who were the recipients of pensions. Nodding does not get recorded—we have to have a statement.

Steve Webb: The difficult thing to disentangle would not principally be the level of the pension right you had already built up—we have a figure for that; it would be who pays the bill. That would be the source of endless negotiation and take years to disentangle.

Chair: It could be as long as Trident, couldn't it?

Q5516 Lindsay Roy: I declare an interest, in that I am part of the teachers' superannuation scheme. Would there be a guarantee that those who are already retired or my colleagues who are about to retire would get the balance that is due to them, in terms of the figure that they had been promised for retirement or that they get now in retirement?

Steve Webb: That would clearly be the right outcome. If you are a Scottish teacher, and you have retired and you are drawing your pension under a set of scheme rules, we have to make sure that those pensions go on being paid according to those rules. The pressure would not be so much whether that pension got paid. For example, suppose that a future Scottish Government took on that liability and was then short of cash, because, as I have said, there is a hole in these schemes, what might they do then? Although in principle you would want to see it carry on, they might say, "We are so short of cash that maybe we won't pay the full inflation increase this year," or something like that. That is conceivable. I do not think the UK Government could control that.

Q5517 Lindsay Roy: But you are clear that they would have to take on that liability.

Steve Webb: I don't think anything is clear—I really don't. I do not think you can simply say, "Oh well, it's obvious. You are a Scottish teacher; you've worked in Scotland all your life, so the Scottish Government will pay your pension in future." Even that is not absolutely clear, because you cannot section off the pension stuff from the rest of the public service. The whole thing would have to be considered in the round.

Q5518 Lindsay Roy: You are not scaremongering. In my book, a translation of scaremongering would be asking a question to which people cannot give the answer.

Steve Webb: I want to do right by the citizens of the United Kingdom. I would love to give very clear answers to the questions you are asking.

Q5519 Lindsay Roy: So would we all.

Steve Webb: Yes, and I do not feel able to do that.

Lindsay Roy: Thanks very much. That was very helpful.

Q5520 Mr Reid: As we previously discussed, we are talking about very large amounts of money. Both sides will be extremely anxious to come out of the negotiations paying out as little as possible, so the negotiations are going to be difficult. Let us say that they have not concluded by 24 March 2016, when the Scottish Government plan that Scotland will become an independent state. Is it possible for Scotland to become an independent state without these negotiations having been concluded?

David Mundell: It is important to remember in this context that the date in March 2016 that has been given is an assertion. It is not based on any factual analysis; it is a chosen date. The date on which Scotland became independent would depend on the nature of the negotiations. If the Scottish Government chose to say, "Regardless of where we have reached in negotiations, we will just accept that position so that we can be independent in March 2016," that is an option for them. Our position is that it seems extremely unlikely that these very complicated negotiations—in relation not just to pensions but to all the other areas this Committee has looked at—could be concluded in an 18-month period, so that you had detailed resolution.

Q5521 Mr Reid: If the Scottish Government went through with independence on that date, and declared Scotland to be independent, and these negotiations had not been concluded, what impact would that have on people who were in receipt of pensions?

David Mundell: As is the case in relation to a whole range of issues, if independence was concluded without the resolution of a number of issues, it would manifest and increase the uncertainty for an independent Scotland that Mr Webb has referred to.

Q5522 Mr Reid: If somebody in Scotland was expecting to be in receipt of a pension and we were in this very unclear situation, could they guarantee getting that pension, or could we be in a completely chaotic situation?

David Mundell: It is quite clear that we could be in a completely chaotic situation, although I certainly do not want us to be. As you know, in the Edinburgh agreement the UK Government committed to work with the Scottish Government, in the event of a yes vote, to ensure a smooth transition. Of course, that does not mean—as the Scottish Government sometimes seek to interpret it—us doing exactly what they would wish, because the Government for the rest of the UK will have to act in the interests of the citizens of the rest of the UK, which will include pension issues.

If there is not sufficient time for negotiations and there is not clarity on where the Scottish Government are seeking to take those negotiations, in terms of what resolution they are looking for, you risk a chaotic outcome. Even at this stage, as you know from having looked at the White Paper, there is very little detail on what the direction of travel or objective would be in relation to a range of these matters. On a number of issues in relation to both pensions and welfare, there are just a number of statements that the Scottish Government would not be doing what the UK Government are doing, but no assertion—even by their standards—of actually what they would be doing. That makes it even more complicated to come to a successful resolution within a very short period of time.

Chair: We turn now to occupational and private pensions.

Q5523 Sir James Paice: If I am going to talk about these things, I probably ought to remind the Committee of my entry in the register.

Minister, your analysis paper refers to all the things that apply to private and occupational pensions—regulatory things, compensation schemes and things like that. In the event of independence in Scotland, what would be the effect on occupational and private pensions, in your view?

Steve Webb: The infrastructure for private pensions is one of those things that you do not notice until it goes wrong. There is the fact that we have a Pensions Regulator, based in Brighton, whose job every day is to make sure that company pension schemes are properly funded, or will be. As I mentioned, we have a Pension Protection Fund, so that if your company goes to the wall and the fund is short of money you get a pension paid. We have NEST, which I talked about, to make auto-enrolment work, as well as a pension tracing service and so on; we have a whole infrastructure.

The challenge would be whether an independent Scotland would reinvent all of this stuff, which has taken years and years to evolve and has been designed with a UK context in mind. It would take a very long time to recreate all of these things. Take the Pension Protection Fund, for example. Unless Scottish firms or Scottish pension funds were paying the Pension Protection Fund levy, it is very hard to see how they would have any rights under the Pension Protection Fund; they would not be members of it any more. If I am a Scottish worker, and you have independence and my firm goes to the wall, what happens? The answer is that I do not know, unless a new regime has been put in place. It took us years to legislate for these things.

I would like briefly to make a more general point about the lead time on all of these things. Even if the negotiations we were talking about a moment ago happened, you would then have to write the laws. Generally we take a long time to write pensions laws—we consult and all the rest of it. Even if you have had negotiations that take a while, there is then a lead time to write the legislation, consult on it and put it in. I cannot see how it could possibly work to have independence and have pension protection the day after.

Q5524 Sir James Paice: Can I pursue you on a point you just touched on? You talked about the company paying your pension. Do you mean the company that used to employ you and that has a pension fund—where that company is located? What if it is being run by one of the big Scottish providers such as Standard Life or Scottish Widows? Is there a location issue?

Steve Webb: We are talking about two different sorts of pensions. The first is the defined benefit company pension. Let us say that the sponsoring employer, whose job it is to make sure that the fund eventually has enough money in it, goes to the wall and there is no pension protection fund in place post-independence to pay your pension from the fund, so if the fund is 70% funded, all you get is 70% of your pension. That is one set of issues. The other sort of pension is the defined contribution pension, which involves a pension pot. The concept of a shortfall does not really arise, as it is just a pot of money; it is a set of assets. That is your money, so where you choose to draw it will not make a great deal of difference, on the whole, although there will need to be a regulatory regime.

Q5525 Sir James Paice: I was going to say that. That is only on protection—there is still the rest.

Steve Webb: Yes. If you have a Standard Life pension or something like that, you can draw it wherever you happen to live. There would be an issue about currency. In what currency did you accrue your rights and in what currency do you want to draw them?

Q5526 Sir James Paice: But Standard Life—assuming that it remains in its current location—would need to be regulated under whatever regime the new Scottish Government developed.

Steve Webb: Yes.

Q5527 Sir James Paice: So an English person in the rest of the UK currently saving with, or a pensioner with, Standard Life, for example, would no longer be protected by the regulatory systems that currently protect them.

Steve Webb: Broadly, yes. Effectively, they would have chosen to save with a pension provider in another country. They would have to hope that the Government of that country had a good regulatory regime in place.

Q5528 Sir James Paice: Except that they did not choose.

Steve Webb: By remaining in the scheme, they are choosing.

Q5529 Sir James Paice: It has been suggested by the Institute of Chartered Accountants for Scotland that the EU could have a locus in all of this, and that the rules would require cross-border pension schemes to be fully funded in the event of separation. Do you have a view on that?

Steve Webb: Yes. I had a very good meeting with the ICAS in Edinburgh a little while ago. They have made a really valuable contribution to this debate. The issue is that the EU has rules—what is called the IORP directive, which says that where you have a cross-border pension scheme, you have to make sure within a two-year time frame that it is funded up to the requisite level. There was some suggestion that the EU might row back on that in revising the directive, but in fact they didn't. I think there was some hope among the nationalists that the EU would relax those rules, and they have not done so. They might at some point in the future, but at the moment they are in place.

If independence—separation—happened on a certain date, those rules would bite, as far as one can tell. If you worked in Scotland for a big supermarket with headquarters in England, potentially you would immediately become a member of a cross-border scheme. If that supermarket scheme had a shortfall in it, within the next couple of years your employer would suddenly have to fill that gap or do complicated restructuring of the pension scheme. That is bad news for your employer. There are going to be costs associated with all of that. The current rules would allow the employer to fill the deficit over a reasonable length of time. If firms suddenly have to find that money in the short run, potentially that is bad news for the business.

Q5530 Sir James Paice: Can we be clear? What money would they need to find to balance the Scottish fund?

Steve Webb: The deficit for the whole scheme—the entire UK scheme.

Q5531 Sir James Paice: The whole scheme?

Steve Webb: Yes, because it is a cross-border scheme.

Q5532 Sir James Paice: By virtue of its becoming a cross-border scheme.

Steve Webb: Yes. They would have to fill the whole deficit.

Q5533 Sir James Paice: That would be a major impost on a vast number of businesses that currently trade and employ in both England—the UK—and Scotland.

Steve Webb: Yes. If they had defined benefit pension schemes—traditional salary-related pension schemes that are capable of having a deficit—that deficit would have to be filled over a two-year period, in principle. We, the UK Government, have been fighting EU attempts to impose strict funding requirements on UK pension funds, precisely because it brings up front these long-term liabilities. That is exactly what would be at risk of happening.

Q5534 Chair: Can I seek clarification on whether it would be possible for a firm simply to break its unified scheme in half and say, "Yesterday we had one scheme. Today we have two schemes, and each has the assets and liabilities of the staff in particular locations"?

Steve Webb: It is certainly possible that restructurings of that sort might be one thing our friends the lawyers would look at, but then you have the issue of whether they are genuinely separate schemes. Would you literally have to carve them up and make them completely separate schemes? You probably would. Then, of course, you have the issue of scale. If you have one sub-scheme that is now a fraction of the size of another, you will have additional costs and so on, so it is not a free lunch. It might be a way around that particular problem, but it would create new problems and, certainly, new costs.

Q5535 Chair: I understand that, but in circumstances where there are cross-border firms we cannot always assume that the proportions of employees are the same as the proportions in the populations of the UK and Scotland.

Steve Webb: No, it could be the other way round.

Q5536 Chair: The Scottish end could very well be the bigger end.

Steve Webb: Yes.

Q5537 Chair: Leaving aside the question of the running costs, simply splitting them would leave them no worse off than they were before, because presumably if there was a deficit, the deficit would be apportioned, as would the assets. You would then have a dislocation, but that would be a tenable position, would it not?

Steve Webb: It might well be the way that some schemes chose to respond. You say “running costs,” but I would not want to dismiss them. Let me quote one sentence from the National Association of Pension Funds. In March, when this directive was published, they said, “The knock-on effect of this”—the directive—“is that schemes with members both north and south of the border would become much more expensive to run if Scotland were to vote for independence.” I always say that I want every pound that goes into a pension fund to turn into as much pension as possible. The risk of all of this is that it is all cost that is coming out of people’s pensions.

Q5538 Chair: Could I go back to the point that Jim made earlier about the structures for regulation of occupational and private pensions, the protection fund and all the rest of it? Is there any reason why, in the event of a decision for separation, the UK Government should not simply say, “We will allow this to continue on a cross-border basis”? That would overcome the short-term difficulty. In the long term, could they not keep it as a joint function, subject to negotiations or, in the longer term, allow the Scottish Government to develop its own? That would overcome the short-term difficulty, would it not? Obviously it would be subject to negotiation, but it is a possibility.

Steve Webb: There will be a differential hit on the Pension Protection Fund, for example, between Scotland and England, just because the risks are different. I do not know which way it would necessarily go; I am not saying that it would be worse for one or the other, but they would just be different. If you are the continuing UK Government and have your own Pension Protection Fund for your continuing employees in your country, do you want insolvency risk, for example, from another country potentially destabilising your protection fund? I do not know, but because you cannot control that insolvency risk in the same way—you cannot control these things altogether anyway—it would not necessarily be attractive. I would not say that it could not happen, but there might be reasons why it would be unattractive. Likewise with NEST, if the independent Scotland had more low-paid employees than the remaining UK, you would be getting more poor-value members, in economic terms, which you were essentially subsidising. I am not saying that any of this is impossible, but it might be quite unattractive.

Q5539 Chair: I understand that. The question of the basis of the division of assets and liabilities—as with so many things—potentially involves big sums that are complicated to work through, but the decision to do it would essentially be a political one and, therefore, entirely possible. All the arithmetic would be consequential upon a whole set of complex negotiations that would be balancing the health service against pension responsibilities, or against defence. On the basis that nothing is agreed until everything is agreed, it would not, in fact, be impossible for a solution to be found that was agreeable and that involved Scotland keeping the UK Pensions Regulator and the UK protection fund.

Steve Webb: It would not be impossible, but bear in mind that on this one I am talking about the future as well as the past. It is not just an argument about how you carve up the past. If I were a member of the continuing UK Government, I really would not want my Pension Protection Fund to be exposed to risks—and revenues—from another country. Why don't we allow another country into our Pension Protection Fund? We know our domestic situation, know our risks and can control them to some extent, so why would you want to expose yourself? It is not impossible, but I think it would be unattractive.

Q5540 Chair: Are you ruling it out?

Steve Webb: I am not ruling it out, no.

Q5541 Chair: It is something that is subject to negotiation—it is entirely possible.

Steve Webb: But I think unlikely.

Q5542 Chair: But that is what negotiation is all about, isn't it?

Steve Webb: Yes.

Q5543 Sir James Paice: On a point of order, Chairman. I want to clarify my comment about my interest. I was referring to the entry that says I am chairman of First Milk, which, as you know, is a Scottish company and has employees in England, Wales and Scotland, rather than anything to do with occupational pensions.

David Mundell: I want to say something in relation to a point Sir Jim touched on in passing. I know that you will have the Chief Secretary to the Treasury here for the separate inquiry that you are conducting in relation to the currency union, but it is worth recording that, complex as these issues are, they will be even more complex if Scotland is not operating with the pound sterling in relation to cross-border pension payments. A separate currency or other currency arrangement would have a very significant impact on the issues that we are discussing today.

Q5544 Chair: Can I ask why? Presumably, if the UK Government were paying pensions to somebody in Scotland in sterling, it is just changed into the merk, or whatever the Scottish currency is, at the prevailing rate of exchange. Surely, that is fairly straightforward.

David Mundell: I do not think it is, because you run into exchange rates being required to determine payment levels and the point at which the future assessment of the payment is being made. It also makes it much more difficult—I think you are going to come on to discuss the operation of systems—for those systems to operate on a dual currency basis at all.

Q5545 Chair: When the UK Government pay pensions to pensioners in Australia, Spain or anywhere else, presumably we pay the money in sterling and they then translate it, do they?

Steve Webb: We sometimes do bulk currency conversion for people. If we pay British people in Australia, we can pay into Australian-denominated accounts but at whatever deal we have been able to strike on currency, and so on.

Q5546 Chair: All of that is doable.

Steve Webb: Yes. As David rightly says, none of these things is impossible but a lot of them add cost and complexity.

Chair: I understand that it adds cost, but it is doable.

Q5547 Graeme Morrice: I want to touch on the labour market. In the "Scotland analysis" paper we are discussing today the DWP goes on about the advantages to all with regard to the current UK labour market. Can you confirm that it is correct to say that we have a single UK labour market in the country? Can you explain what that is and what the advantages are, particularly for Scotland?

Steve Webb: Wherever you are working in the UK, there is a common set of legal employment rights; a common minimum wage, although sometimes there are different rules for London, but that is a separate issue; and a common set of employment rights. For example, if you work for a big firm and you move from their office one side of the border to the other, that is not changing your terms and conditions of employment. I think that both sides of that mix give flexibility to individuals and employers. On the social security side, you are paying national insurance into one system. Therefore, if your job in that common labour market fails you have a set of rights wherever you paid in. There is no disentangling of different periods of service and splicing it together, so for the individual it is seamless and the employer is able to treat everyone the same. When you are deciding where to work you are not thinking, "I'm in a different benefits system, or have a different set of legal rights." All of that is standardised, so it adds to the individual's and the employer's flexibility.

Q5548 Graeme Morrice: Turning to the second part of my question, in particular how is this advantageous to Scotland?

Steve Webb: If you are working for a UK-wide company that wants you to work in Scotland, there is no issue about being paid in a different currency, your future state pension rights being built upon on a different basis or, if you lose your job, your benefit position being different. As an employee you are happy to work, other things being equal, wherever in the UK you need to. It means from a Scottish point of view that, if your firm wants you to work in Scotland, there is nothing in the back of your mind saying, "Ah, but there are all these things I need to think about." You just do not need to think about them.

Q5549 Graeme Morrice: What risks do you perceive if Scotland was indeed to become independent?

Steve Webb: In terms of the labour market, I could give one anecdotal example. I have a constituent who worked in Scotland and in England, in the public sector as it happened, and she built up pension rights in both. She said, "I want all my pension in the English scheme because I want all of my money in one currency." She was worried about currency fluctuations. If you imagine a world where you have two separate countries and you work in both of them, you are going to build up pension rights going forward in different state pension schemes. You will get pensions potentially paid in different currencies. If you lose your job, it might depend which benefit system you are going to be under, so there is all that kind of uncertainty and complexity that you do not have now, and for no obvious benefit, in terms of your job.

Q5550 Graeme Morrice: You talk about the healthy state of the single UK labour market as it is. Despite Scotland perhaps becoming independent, would there still not be advantages in terms of people crossing the border either way, seeking jobs, and businesses moving to and fro? We have a single market when it comes to the EU, so why in particular do you think Scotland may be disadvantaged in relation to this if Scotland did indeed become independent?

Steve Webb: If you are an employee of a UK-wide company and the company says, "We would like you to work in Scotland," at the moment, subject to your wanting to work in Scotland, that is absolutely fine, whereas in the new situation, just as if they said, "We want you to work in France," say, you would be thinking, "Hang on. If I'm working in France, what tax am I paying? What pension rights am I building up? What if I fall sick?" There is a whole set of things that are common now that you do not have to think about and suddenly you have to think about. It seems to me that the Scottish economy wants to have the biggest available pool of labour that it can; it wants the brightest and best from around the United Kingdom willing and happy to work there without having a second thought about all those things.

David Mundell: Referring back to our borders paper, which the Committee looked at before, as part of the general evidence, although there is interaction between the North and the Republic of Ireland, between Canada and the United States and between Austria and Germany—three examples—it is less than people would anticipate for very similar coterminous countries. The evidence presented there was that, if you create a border, that border has an effect not just in terms of movement of goods but of people as well.

Q5551 Graeme Morrice: Mr Mundell, I suppose your point in relation to the likelihood of there not being a currency union if Scotland was to become independent is that it would probably put up a very sizeable barrier to the free flow of labour, business and trade between Scotland and the rest of the United Kingdom.

David Mundell: I think you are correct. I have many constituents in my border constituency who operate small businesses and are very concerned that people on the other side of the border simply would not employ them because they would be put off by the thought, factual or otherwise, that there would be a great deal of complexity in using trades people or a business on a different side of a border.

Q5552 Graeme Morrice: That is an interesting point because of the geographic location of your constituency, which borders England. Have these concerns been expressed to you personally by individual constituents?

David Mundell: They have been expressed by a large number of constituents. That was why I was quite surprised that Mr Alex Salmond, First Minister of Scotland, visited Carlisle to tell people that all these things would be all right, but did not feel that he needed to come to the Scottish side of the border to reassure people there. My constituents were quite surprised that he chose to go to Carlisle to announce that their concerns were unfounded rather than come and meet them.

Graeme Morrice: Don't worry, Minister; we are going to Dumfries and Galashiels shortly.

Chair: I think Peebles is in your constituency.

David Mundell: Indeed.

Q5553 Pamela Nash: Are you surprised that it was kept from us? I meant the visit to Peebles. It's not my question.

David Mundell: You will very much enjoy the visit to Peebles. Peebles high street has the largest number of independent shops of any high street in Scotland, so it is a thriving small business centre.

Q5554 Pamela Nash: I didn't know that, but it doesn't surprise me, having been shopping there. My favourite piece of jewellery is from there.

Back to the matters in hand, away from Scotland tourism. In terms of welfare and benefits, can I clarify that Scotland has higher expenditure on benefits compared with the rest of the UK? Can we look at the UK Government's analysis of why this is the case, particularly in relation to disability benefit, but I would be interested to hear your views on other benefits too?

Steve Webb: You are right. Scotland currently has a slightly higher expenditure per head on social security. That number has fluctuated a lot. There have been times when it has been a lot higher; it is now slightly higher. One of the reasons the differential has come down is that within the United Kingdom the Scottish economy has been doing relatively well. Employment growth has been relatively rapid, which has changed the differential. There is a slightly higher proportion of pensioners and children in the population in Scotland relative to working age, which puts an upward pressure on spending. There are slightly fewer children relative to the rest of the population, which puts downward pressure, so there is a range of different factors. Rent levels tend to be slightly lower in Scotland than the rest of the UK, particularly London. There are lots of different factors going on, but taking it overall, particularly because of pensioners, it is slightly above. As you say, incapacity benefits are slightly above. I am guessing, but I am reasonably confident, that a lot of people now on incapacity-type benefits worked previously in heavy industry, manufacturing and so on, and that is part of the reason they now have bad backs and all the rest of it. It tends to be a hidden form of long-term unemployment in those sectors of the economy, which I would speculate have been historically quite well represented in Scotland, but I would not swear to that.

Q5555 Pamela Nash: That is not the first time I have heard, either in this Committee or beyond, that that is the reason why we have higher levels of disability benefits in Scotland. Are you aware of any analysis that has been done of it?

Steve Webb: We could certainly give you the figures for Scotland and the rest of the UK and some historical trends. I am very happy to supply you with that.

Q5556 Pamela Nash: In terms of the health problems.

Steve Webb: We would have that information, yes.

Q5557 Pamela Nash: In that case, if Scotland was to leave the UK, is the gap between the current UK level of disability benefit and other benefits and Scottish benefits significant enough that a Scottish Government would need to increase taxes to fill it?

Steve Webb: At the moment the difference is relatively slight. To take the whole of social security together first of all, if I may, it is a couple of per cent higher. Converting it into my pounds per working-age person, it is perhaps an extra £10 now, which does not sound very much, but when you roll forward the demographics and so on that £10 turns into £120.

Q5558 Pamela Nash: To be clear, the additional cost for social security in Scotland is £10 per head per year.

Steve Webb: Per head per working-age population. If you simply required the current working-age Scottish population to pay for what the Scottish benefit-receiving population got, there would be a slight increase in taxation, or borrowing or whatever. As I say, it is about £10 a head of working-age population, but there are long-term trends; for example, because the Scottish working-age population is older, there are more 50 to 65-year-olds. The incidence of disability and incapacity benefit is higher in that age group, and that is one of the reasons why the Scottish figures are higher. We know that, although there has been a growth in young people getting these sickness-related benefits, it is still quite heavily concentrated among older working-age people, so those trends would get worse over time.

Q5559 Pamela Nash: What benefits are you including in the £10?

Steve Webb: That is everything.

Q5560 Pamela Nash: Not pensions.

Steve Webb: It does include pensions, so it is plus £80 on pensions and minus £70 on working age. If the Scottish working-age population had to fund the bill of the Scottish benefit-receiving population, it would be paying £80 extra per working-age person on pensions and £70 less on working age. The reason it is less on working age is primarily because there are fewer children. If you think about the working-age population—families with children, tax credits and all the rest of it—that is where we pay out a lot of money.

Q5561 Chair: This £10 is in addition to the £400-odd we discussed earlier, which gets us ever closer to the magic £500 at which people will sell their souls or their grandmothers.

Steve Webb: That is the baseline now, and these other figures are additional.

Q5562 Pamela Nash: To be clear, is it correct that the £450 refers to Scottish Government policies, whereas this figure is referring to current UK Government policies?

Steve Webb: Yes. The £450 is a split of unfunded Scottish Government promises and demographics, so half of it is the £10 that will become worse, as it were.

Q5563 Pamela Nash: You said there was only a slight difference in terms of benefits. We discussed disability benefit. What is the difference in the case of disability benefit?

Steve Webb: I have not got the sub-breakdown, but I am very happy to give you that.

Q5564 Mr Reid: I want to turn to universal credit. As you know, the Scottish Government, in the event of separation, propose to stop the implementation of universal credit in Scotland. Is that a practical thing to do?

Steve Webb: I think it gets to the nub of the inconsistency of the Scottish Government's position. On the one hand, even they recognise that you cannot invent a new social security infrastructure overnight; it takes years to do all the computers and all the rest of it. They anticipate paying the UK Government, presumably, to go on administering these things post-independence, but the UK Government will only be administering UK social security benefits according to UK rules, so there will be a computer system delivering universal credit, personal independence payment and all these things. The UK Government will not want to jeopardise what it delivers to its own citizens by changing its computer systems to do versions of its own benefits system that work for a different country. Either the Scottish Government sets up its own systems or it pays the continuing UK Government to run UK benefits, but what it cannot do is immediately deliver its own version of those benefits.

Q5565 Mr Reid: There is a computer system that operates the present pre-universal credit system. Why could the Scottish Government not simply continue to operate that existing computer system?

Steve Webb: Those systems are being progressively dismantled essentially; they are being run down.

Q5566 Mr Reid: But the software exists.

Steve Webb: It exists.

Q5567 Mr Reid: Why can't it just carry on running that software?

Steve Webb: I think it is very unlikely that the UK Government will want to be running what we call in the jargon legacy systems; a lot of them, not all, are very old, and some we are eking out until the day when we can switch them off. To keep them going into the medium term would probably cost a lot of money. I cannot see the UK Government wanting to spend that money, or to be diverted from doing the day job. That is the important point. The UK Government will still be trying to pay hundreds of billions of pounds in benefits and pensions to its own citizens; it will not want to be diverted to running legacy systems for a small number of people.

Q5568 Mr Reid: Have you any estimates of how long it would take for the Scottish Government to design and implement a computer system of its own for the benefit system that it wanted?

Steve Webb: It is clearly multiple systems. For example, it says it would not have universal credit. Bear in mind that universal credit replaces three separate streams of benefit: local authority housing benefit, or rent rebates; DWP jobseeker's and ESA; and tax credits. The Scottish Government would have to keep, presumably, three separate computer systems going for those three things. It would not have the personal independence payment; it would have disability living allowance, so it would need a system for that. It would keep the savings credit bit of the pension credit, which we are getting rid of for new cases, so it would have to add a bit. You start to see multiple systems over many years. Trying to merge all of those into one has proven demanding to the DWP over a period of many years. These things take several years to do, even when you have had plenty of time to think them through, plan and get the legislation through. Before you do the systems you write the laws, so the lead times on these things are huge.

Q5569 Mr Reid: To take an example, in terms of universal credit how long will it take from thinking about it to it being fully implemented?

Steve Webb: A Scottish version of it?

Mr Reid: How long did universal credit take from the initial concept to implementation, just to get a handle on how long it takes to do these things?

Steve Webb: The Welfare Reform Act that provided for universal credit to come in was in 2011, or early 2012, so the lead time is about six or seven years from getting the law through to having the payments on the ground to everybody, certainly when you are bringing together complex systems.

Q5570 Mr Reid: Do you have a figure for the cost of implementing universal credit?

Steve Webb: We think a significant IT programme for a major benefit is of the order of £300 million to £400 million, and a lot of that cost is fixed, whether you are doing it for 5 million or 50 million. A lot of it is just fixed cost.

David Mundell: The point I made earlier is that it is not clear what benefits system and welfare proposals the Scottish Government intend to bring forward. They established a commission, which you may be aware of, but, as far as I am aware, it has not reported within the time scale that was initially set out, so the framework in which they would wish to legislate to create their new system, if they were to do so, is not clear.

Q5571 Mr Reid: I am sure you are aware of the NAO report which found that the DWP had no detailed view of how universal credit is meant to work and has not achieved value for money with the programme. First of all, what is your response to the NAO report, and would an independent Scotland, therefore, not have a point in designing a different system?

Steve Webb: I think it is worth reminding ourselves what universal credit is trying to achieve. All of us will have constituents who have had tax credit nightmares. You have a tax credit system based on annual assessment, end-year reconciliations, clawbacks, overpayments and underpayments; you have a local authority-based rent rebate system; and a DWP-based JSA and ESA system. For the constituent, universal credit is saying, "Let's have all of this in one place and make sure we do not have overlapping rules that are to the detriment of the individual." Scottish citizens, presumably, would have to carry on with some continuing tax credits thing, going to the council for housing benefit and whatever the DWP's successor is for JSA and ESA, or whatever that is, with overlapping tapers and all of those things. If I were a Scottish citizen, I absolutely would want to be part of universal credit. I think there is a compelling case that it would be a better experience for the consumer. It takes a while to get in, but once it is in I think it will be very good.

Q5572 Mr Reid: In the "Scotland analysis" paper you suggest that stopping universal credit would create poor incentives to work and so make unemployment higher in an independent Scotland. What evidence do you have that incentives such as a universal credit system do raise the employment rate?

Steve Webb: Let me give two examples. One is smaller jobs. At the moment the benefits system is very much that you're in work/you're out of work. It is either/or; it is black or white. There are 16-hour rules and all sorts of artificial rules. What universal credit enables people to do—for example, those with disabilities who may not be able to do a full week's work—are smaller jobs, part-time jobs, or jobs where hours might vary from week to week. It is much more accommodating, rather than saying, "Are you in work? Were you out of work that week?" A lot of the newer jobs being created are full-time, but there are also jobs being created that are perhaps part-time, or variable hours. The new labour market is a much more flexible one, and you need a benefits system that meshes with that, so for the sorts of jobs employers want to create, to some extent anyway—many of them are traditional full-time jobs—at the margins a benefit system that fits that is going to help.

The second thing is the whole issue of tapers. If you earn another pound, is it worth it, because things are clawed back? At the moment you have tax credits here, housing benefit there and ESA/JSA here. All of that together can mean you are only a few pennies better off in extremis. Because universal credit is all in one system, it can align all those withdrawal rates so many people do not face the very extreme withdrawal rates that put them off working altogether. Surveys and all the rest of it have been done, but there are good structural reasons to think that universal credit will be good for the labour market and good both for employers and for employees, and a country which misses out on UC will miss out on employment opportunities.

Q5573 Mr Reid: Do you have evidence to suggest that under the old system people are being deterred from taking a job because the financial incentive is a very small amount of money?

Steve Webb: Yes. The classic one is the 16-hours rule. I talk to employers who say they have people who will work for them for 15 hours but not 16 hours because a whole different set of benefit rules applies. Also, when universal credit comes in, typically it is more generous. Those who would get less get transitional protection. We estimate that about 300,000 people in Scotland will be an average of £166 a month better off under universal credit, which potentially they will miss out on if they are not part of it.

Q5574 Chair: When you say a certain number of people are going to be better off, is there a net increase in expenditure as a result of the introduction of universal credit? If not, presumably the number would be balanced by the number who would lose.

Steve Webb: Universal credit does involve an injection of money into the system.

Q5575 Pamela Nash: I have a brief follow-up on Mr Reid's questions. It might be a little out of the remit of this session. You were talking about issues arising if universal credit did not go ahead in Scotland. If Scotland votes no, there is talk, certainly in the Labour party but beyond as well, about devolving at least some elements of housing benefit to Scotland. Can you see how that would work within the universal credit system?

Steve Webb: Part of the point of universal credit is integrating the different bits of the benefits system both so that the individual does not have to go to different places and so that all the rules are aligned. For example, there is a set of rules on how savings are treated. They are different for housing benefit, as for other benefits. Instinctively, part of the point of universal credit is that it is an integrated single payment system, so fracturing a bit off would, I think, potentially undermine some of those advantages.

Q5576 Graeme Morrice: If we had a separate Scotland, there would be a separate benefit scheme presumably, and also a separate benefit administration system. Have you done an estimate of the cost of that, including any transitional costs, or are you aware whether the Scottish Government have estimated the cost of this as well?

Steve Webb: We think that at the moment it is costing about £720 million a year to deliver social security benefits and pensions to the people of Scotland. That is the scale of what we are talking about. Inevitably, there is an infrastructure for all of this. In having to set all of that up from scratch clearly there are fixed costs, and there are also ongoing running costs. For example, one of the things we try to do is pool call centre capacity. You phone up and the call centre is at capacity, so you can divert to another one. There is a big rush on phone calls about JSA this month, and next month it is about ESA. We have this phrase in the Department, "one DWP," where we pool all these things and then you can flex the system. Clearly, if you are doing all of these things on a much smaller scale the potential for flexibility is smaller. You will probably have surplus capacity. Of course it is doable—small countries run social security systems—but clearly the cost per head is bound to be higher, and there would be substantial set-up costs as well.

Q5577 Graeme Morrice: If you were disaggregating the DWP within Scotland, presumably there would be a knock-on cost effect on the rest of the UK because it would have to fine-tune its system and its scheme as well.

Steve Webb: Yes.

Q5578 Graeme Morrice: Has any assessment been undertaken of the financial implications of that?

Steve Webb: Not specifically, as you rightly say. Just to give you a feel for it, in Scotland we have 94 jobcentres, three contact centres, seven benefit-processing centres, two pension centres and three child maintenance centres. We do a lot throughout the United Kingdom, so clearly there would be a knock-on cost to the continuing United Kingdom of disentangling all of that, which would be a deadweight cost to the rest of the UK as well.

Q5579 Graeme Morrice: On your earlier point about sharing DWP resources, call centres in particular, presumably there would be a disadvantage to Scotland and the rest of the UK in terms of losing the advantages of economies of scale.

Steve Webb: Yes. In a sense, the UK is losing a tenth, or whatever, of its capacity; Scotland is operating at 10% of the UK scale, give or take, so the cost hit on Scotland is clearly significant.

I just mentioned child maintenance, which does get a mention in the Scotland paper. I think it is a neglected area. We have a child maintenance system undergoing reform. Wherever you are in the UK, if you are a separated parent, there is a mechanism to try to make sure separated parents sort things out between themselves; if not, there is a statutory scheme to try to recover money. What does all of that look like in a post-independence situation? Does the Scottish Government have to set up a Scottish CSA—that will be a joy, I imagine—with a whole set of rules? The Scottish legal system is different anyway, which might complicate things, but if you have an ex-partner on the other side of the border, suddenly you are chasing someone for money in another country, and we know from our own experience just how difficult and complicated that is. You are getting court orders in other countries. In terms of simple things like the infrastructure of child maintenance, it is one of those things where we take it for granted and it is not an issue; if your ex is living on the other side of the border, it is not an issue. Is that something else that will have to be reinvented?

Q5580 Graeme Morrice: What assessment have you undertaken in relation to the number of DWP staff working and living in Scotland? Is there a disproportionately larger number of those staff in Scotland compared with the rest of the UK? Have you looked at it on the basis of share of population and per capita?

Steve Webb: In general, because of Scotland's geography there are probably slightly more jobcentres per head, because you have to cover a rural area. Clearly, coverage is limited—I understand that—but there are probably slightly more per head. On the other hand, out of 32 contact centres, there are three in Scotland. It is different for different services. There has not been a deliberate drive to over or under-represent Scotland, but different services would be differentially affected.

David Mundell: An important point is that the services provided are not geographic. I recently visited Northgate in Glasgow where 1,300 DWP staff work. They are providing support to people right across the United Kingdom; they are not providing a geographic service solely for Scotland.

Q5581 Graeme Morrice: That is a helpful intervention, and that was the point I was driving at. That being the case, would we ultimately see fewer people employed in Scotland compared with what we have currently within the DWP providing that service?

Steve Webb: To give you some sense of scale, about 11% of DWP staff are in Scotland, as against about 9% of claimants. You could argue that it is slightly more, although I would not make a huge issue of it. Clearly, there would be huge disruption. I visited the Dundee pension centre, for example, and as David said, those folk are providing UK-wide services. That would all have to be sorted out.

David Mundell: It is part of a wider issue, which is one of the little-known facts that perhaps we have not in the past made clear enough. There are twice as many UK Government civil servants in Scotland as Scottish Government civil servants. We recently visited HMRC offices in Aberdeen, for example, where people are providing specialist and UK-wide support. There is a clear sense of uncertainty among those people as to what their role would be in an independent Scotland, given that the Scottish Government have not indicated that they would wish to have a Scottish civil service of 30,000 people.

Q5582 Chair: Can you help us by coming back with some information about that? When I was in Stornoway recently it was drawn to my attention that there is a service in Stornoway providing a UK-wide service, or certainly beyond the western isles. Can you give us a note of how many DWP people there are in Scotland, and where they are based, who are providing a UK-wide service, or a service furth of Scotland if it is not for the whole of the UK? I think that would be quite helpful for us.

Steve Webb: We are happy to do that.

Q5583 Pamela Nash: And beyond DWP, for all the UK Government.

Chair: Given the victims that we have today, I was being specific.

David Mundell: I think we could look to provide that information. I accept that perhaps the UK Government has not in the past made it as clear as possible. We are a major employer in Scotland, regardless of all our other interests.

Chair: If Steve can do the stuff for the DWP and David can arrange for it to be done for the other Departments, it would be very helpful.

Q5584 Graeme Morrice: The DWP have stated that, if Scotland does not use sterling, Scotland and the UK cannot share a benefits system, even for a transitional period. Can you explain why?

Steve Webb: Clearly, our systems are geared up to make payments in sterling. It is astonishing how difficult it is to change these systems. It would not be wilful hostility. To give one example, currently we have a cold weather payments system. There are just under 100 separate cold weather stations across the United Kingdom. We had a report that recommended we should go from just under to just over 100. I was told that this would be incredibly expensive because the computer was hard-coded to have a two-digit number for the cold weather stations, and to have a three-digit number would require vast amounts of consultant and expert time just to make a tiny change. What seems to a lay person to be a trivial change, because a lot of these systems are very old and rigid, is very difficult.

Q5585 Chair: You believed that, did you?

Steve Webb: I absolutely believe that, yes. We would be geared up to make payments in sterling.

An interesting question is that you are in Scotland under some sort of Scottish system with a legal right to payment of a set amount in a Scottish currency. We deliver a payment in sterling, so is the Scottish Government then taking on an exchange rate risk? We would not be changing our systems; we would be paying sterling benefits if we had that deal.

Q5586 Chair: There is one other major area we want to cover relating to the bedroom tax, but I want to pursue some elements of the timing of the introduction of universal credit and the various changes. As far as I am aware, it is not running quite to time, is it? It has been suggested that it might not be entirely implemented by the date either of the referendum or of separation in the event of Scotland voting to leave. To what extent does that make a substantial difference? If you are still transitioning, presumably it would be possible to have a situation where you are operating both anyway; you simply change the geographical areas that are operating the existing system, and don’t transition it, and do the transition into the new system elsewhere.

Steve Webb: To be clear, there are two sorts of transition going on. One is geographic. From memory, universal credit started to be rolled out in Inverness, for example. Then there is transition by family type. I understand that that is starting with what is regarded as the simplest cases: the young single unemployed person, and then moving to couples and families and so on. Over the coming months and years there is a set of phases. Clearly, that process will not have finished by the referendum, or by the date that the Scottish Government have indicated they want this process to be completed.

In terms of DWP investment and so on, there will be no interest whatsoever in maintaining computer systems and capacity to deliver what we call legacy benefits. The crucial point is that we, the continuing UK, will want to deliver the best we can for our citizens through universal credit and so on. We will not want to take our computer people off, our policy people off and our lawyers off to set up, maintain and modify legacy systems to keep them going in Scotland.

Q5587 Chair: Will you refuse to do it?

Steve Webb: We will refuse to do anything which is to the detriment of the citizens of the continuing United Kingdom. We will not prejudice the wellbeing of the citizens of the continuing United Kingdom to deliver services to the people of Scotland.

Q5588 Chair: This is obviously a crucial question. We have had discussion with a number of Ministers about what they might prefer to do and what they would not prefer to do, but we have not been entirely clear, except for David Willetts and maybe some Minsters talking about currency, whether or not they would actually decline or refuse to do certain things. I think you are saying to us—we want to be absolutely clear about this—that the DWP would refuse to operate two parallel systems simply because of the question of complexity, and would also refuse to maintain a legacy system for a separate Scotland. The implication of that, unless I am mistaken, is that a Scotland that voted for separation would end up, at least for a period, being bound into the UK benefits system, and, if they wanted to make changes and transition to a new system, they would have to develop their own system over quite a substantial period, and to suggest that they can either have a change or retain the existing system at the time of separation, or have a transition to their own system, operated by the UK, is neither feasible or practical.

Steve Webb: Let me put it in my own words. I entirely agree with the point that, if a future independent Scotland wanted the UK Government to administer benefits, we would be administering UK benefits under UK rules. That is what we want to be doing. As to the idea that Scotland can design its own benefits system and ask us to tweak our computer systems and so on, I do not see that happening. We are running our own systems under our own rules. As David said, we have the Edinburgh agreement to work constructively, but not to the detriment of UK citizens, so diverting our policy people, our computer people, our lawyers and so on to do any of that work, I cannot see that happening.

If I may, I will pick up on the currency point, to make sure I am absolutely clear—to get this absolutely right. Obviously, our systems assess in sterling; that is what they are set up to do, and that is something we could not change. Clearly, as I said earlier, in principle we can press a button and pay out in another currency. As in the case of Australia, we can pay out in another currency, but our systems are set up to assess in sterling, and that is the thing we would not be able to change. The rules and rights would be in sterling, whatever the currency. I wanted to put that on the record to clarify it.

To go back to your earlier point, our guiding principle, without being hostile or unhelpful, is that we have an ambitious programme of welfare reform going on, with big computer systems, big evolution and all the rest of it, which we as the UK Government would not want to be to the detriment of our own citizens by tweaking legacy systems, for example.

Q5589 Chair: In the event of a change of Government in the UK, leaving aside the question of separation, with maybe a different coalition—you might still be there, but who knows—you are not telling us that there could be no change made to the system being proposed at the moment, are you?

Steve Webb: It is obviously at the disposal of the UK Government of the day to form a judgment as to whether its reform programme needs to be changed. Clearly, the UK Government, thinking that is in the best interests of UK citizens, are able to do that. What I am saying is that, from where we stand now, we, the future UK Government, would not want to do anything to the detriment of UK citizens.

Q5590 Chair: I understand that. I just wanted to be clear that you are not telling us that the scheme you have at the moment in both strategy and detail is so set in stone that it is unamendable.

Steve Webb: Things can always change.

Q5591 Chair: Fine. I just wanted to be clear about that. The point you were making was that you did not see operating two parallel systems; you cannot see operating two parallel systems. You phrased it in different ways. Am I clear you are saying that you won't? You will refuse to do so.

Steve Webb: I am saying we will form a judgment. We are in multi-hypotheticals here. If there is a yes vote and if the question is asked, "Do you, the UK Government, mind running another system for us over here, say, with different rules?" the first thing we would ask ourselves is, "Can we do that without detriment to our own citizens?" I think it implausible, to be honest, that we could, given the stress on resources and all the technical skills we have in running the system. It is hard to see how that would be possible.

Q5592 Chair: I labour this because one of the most important and significant drivers of the move towards separation is to break away from what they see as basically Tory anti-welfare policy. People who are campaigning for separation would be horrified at the idea that they were going to end up with it anyway—even if they voted for separation. That is why I am trying to be absolutely clear about this. I think you are saying to us that the 18-month period would not be sufficient for a Scottish Government to develop its own system. In the event of a vote for separation you would not be willing to operate two systems in parallel. Therefore, in the event of a vote for separation and even a declaration of independence, the only system that could actually be operated is the existing—or with variations—UK system.

Steve Webb: It is very hard to see a scenario in which independence has been declared, or whatever, and there is immediately in place either a system the Scottish Government can run for itself, or a continuing UK Government that would be willing to run a bespoke Scottish system according to Scottish specifications. It is very hard to see that scenario happening.

Q5593 Chair: The best that those who were voting for separation could envisage would be reducing the period between an inherited UK system and the introduction of a separate Scottish system, which might take six or seven years. I am not quite clear how long these things might take.

Steve Webb: That would be an illustrative lead time. Bear in mind that when in its first year or so this Government introduced universal credit, it was based on years of policymaking, thinking and all the rest of it, so it is many years down the track.

Q5594 Chair: How long did it take to introduce the CSA, for example, from the time the decision was made to its paying out, leaving aside that the CSA was not a raging success immediately, or indeed ever?

Steve Webb: If you think about the reforms we are doing to the child maintenance system now—what we call the 2012 system, which started on a small scale in 2012—we have another three years of moving people, closing places and bringing people on until 2017-ish, so that is five operational years preceded by legislation and all the rest of it. Again, we are in five to 10-year lead-time territory.

Chair: Maybe you could reflect on this. If you feel that a five to 10-year period is unrealistic, one way or the other, it would be helpful if you could come back to us. This is of considerable significance for people in Scotland, and it is one of the areas where we are trying to provide clarification for people who will be voting in the next six months or so.

Q5595 Lindsay Roy: Gentlemen, you will be aware that the bedroom tax is as welcome in Scotland as a stink bomb in a spacesuit. You will be aware that it is a hated tax. At the last meeting, David, you said quite clearly that the Scottish Government already had the power to mitigate and nullify the tax within the powers they had. Can you tell us what they are?

David Mundell: At the last meeting I think we agreed that we may have different views in relation to the spare room subsidy, but that we would focus on the practical operation. In my previous evidence I set out that I believed the Scottish Government did have powers by which they could use their own funds to mitigate what they said was the impact of these measures.

Q5596 Lindsay Roy: For the record, could you tell us what they were?

David Mundell: Essentially, they control the funding of local government and registered social landlords. Therefore, they were able to direct funding to those bodies, rather than to individuals, in ways that would mean that there was funding support available for some of the measures which councils were already coming up with proactively to take steps to mitigate what they said was the impact of the change, particularly in relation to the spare room subsidy. What became clear to me was that the Scottish Government either were unwilling or did not have the capacity to develop those mechanisms.

In discussions that I had subsequently with, I think, all local authorities, other than Argyll and Bute that I had met previously—I met your own local authority, the city of Glasgow, and West Lothian and North Lanarkshire—it was clear to me that those local authorities were potentially being put in a position where we, the UK Government, were saying that the Scottish Government had power to spend money that it was forced to allocate to this matter by the Scottish Parliament, and the Scottish Government were saying, "We can allocate this money only through discretionary housing payments."

I formed the view that I did not want local authorities in Scotland to be caught in a to and fro between the UK Government and the Scottish Government, particularly in this highly political period, and that therefore it would be better to find a way by which they could receive additional discretionary housing payments. I remain firmly of the view that the Scottish Government could have developed their own approach but they have not done so.

Q5597 Lindsay Roy: Do you have evidence that the facility was available but they did not have the determination to see it through?

David Mundell: I set out in detail at our previous meeting a range of things that could be done. Anecdotal evidence is that clearly a large number of Scottish Government officials are very heavily focused on the issue of independence. Therefore, they might not have the capacity to determine a scheme they could operate in Scotland to put forward their own measures mitigating the spare room subsidy. As we saw with the way they allocated the £20 million that they spent, they did not really spend a lot of time determining which local authorities should receive the money and which would not, and how that interacted with payments that the Department for Work and Pensions had already made. Some local authorities were in a very positive position where they received money from both the UK Government and the Scottish Government, which indicated to me that a lot of thought had not been given to how to allocate that funding.

I hope you would agree that the principle we adopted was to put the needs of the local authorities first and to come forward with a way in which they could achieve their objectives. What I respect about local authorities in Scotland is that, although many of them do not agree with the Government's policy position, and I accept that, they take a very pragmatic and professional approach in taking forward what is Government policy. They do not politic about it; they get on with what they have to do on the ground. I did not feel that they should be drawn into a perceived political battle between Westminster and Holyrood.

Q5598 Lindsay Roy: Your experience was that local government had used their initiative and enterprise and been pragmatic, but your feeling was that the Scottish Government had put Scotland on pause in relation to their determination to see this through.

David Mundell: Whether or not there was agreement on this policy, it was announced in June 2010. Nothing happened in relation to the Scottish Government until September 2013 when they announced some additional funding. No proactive steps were taken. In January this year, the day before I was due to appear before this Committee, Nicola Sturgeon was on the radio announcing the approach they wanted to follow. Since then we have restated our view that discretionary housing payment was not the only way forward. I think Margaret Burgess came before this Committee and reasserted that it was. I came to the view that it was not appropriate simply to be engaged in a situation where Scottish local government and housing associations were caught between us saying, “You have the power to do this,” and the Scottish Government saying that they did not.

Q5599 Lindsay Roy: Why do you think it took so long for the Scottish Government to act?

David Mundell: My personal view would be that the Scottish Government concluded this was a highly political issue and wished to derive the maximum benefit from politicising it. That is in marked contrast to local authorities in Scotland who have sought to achieve the best outcome they could for their tenants and wider citizens.

Q5600 Lindsay Roy: Like me, you think this is about getting political capital from the situation.

David Mundell: That is the conclusion I came to, but the reason we have gone forward to offer the discretionary housing payment cap, to be determined by the Scottish Government, is to allow the additional money that, as you know, the Scottish Parliament pressed the Scottish Government to spend—it was not entirely voluntary—to be spent in a way that meant local authorities and housing associations in Scotland were able to receive the funds, and were not caught in a “he said/she said” situation between the Scottish Government and the UK Government.

Q5601 Lindsay Roy: I think there is a welcome for an increase in the cap, but it is all the same money from the Scottish Government; there is no additional funding from the UK Government. Is that right?

David Mundell: There is no additional funding from the UK Government. We put forward approximately £15 million. The Scottish Government had intended to put forward £20 million, and after discussions in the Scottish Parliament that sum was increased to £35 million.

Q5602 Lindsay Roy: To what extent will increasing the cap nullify the problem, bearing in mind the evidence we have taken about people with learning difficulties and mental health issues?

David Mundell: On the basis of the funding that has been put forward, I think there is no excuse for the Scottish Government in relation to any specific group that there are not measures in place in individual local authorities to mitigate any perceived adverse impact.

Q5603 Lindsay Roy: It would still be the case that citizens have to apply for DHP.

David Mundell: Clearly, it will be for individual local authorities as to the basis on which they administer DHP, under certain guidelines, which clearly come both from the DWP and from the Scottish Government. Across Scotland, one of the things I have said in discussions with the Scottish Government, COSLA and others is that some local authorities have been much more proactive in terms of what they have done. There has been some very good work in North Lanarkshire, Fife, West Lothian and the city of Glasgow. Having visited all 32 local authorities, there is some very good and proactive work being done. What we want to look at is best practice in relation to how these steps have been taken. Within that there is a degree of discretion in relation to the length of the payment and just how much information and so on has to be provided.

Q5604 Lindsay Roy: I think our evidence indicated that 25% of those eligible but who had not taken it up were people who had learning difficulties and mental health issues. Is there flexibility for a local authority to deal with that in a different way?

David Mundell: A number of local authorities have been very proactive in identifying individuals who have specific issues, and have sought to do that effectively by going out and visiting them. I think that has been done in Fife, as I recall.

Lindsay Roy: Yes, it has.

David Mundell: A wider issue that was identified is that there is a group of people in society that it is very difficult to make contact with, but the local authorities and housing associations that have been most proactive have been the most successful in terms of signing up people. What I want, and there is great scope to do, is to encourage best practice in terms of how these issues have been approached.

Q5605 Lindsay Roy: You can look no further than David Ross and his Fife council team. Thanks for the plug. In terms of equity and fairness, do you think that those who scrimp and save and have paid part or all of the DHP should be reimbursed by the Scottish Government?

David Mundell: In terms of issues within the responsibility of the Scottish Government, these are for them and the Scottish Parliament to determine.

Lindsay Roy: I understand that.

David Mundell: What I can set out is a factual background. This policy having been announced in 2010, the Scottish Government did not take any proactive steps until September 2013. I think people in the Scottish Parliament and Scotland will form their own conclusions on that basis.

Q5606 Lindsay Roy: I understand where you are coming from, but I ask you whether, in terms of social justice and fairness, you think the Scottish Government should reimburse those who scrimped and saved—maybe had gone without—and paid their bedroom tax?

David Mundell: I genuinely do not think that it is for me or for Ministers within Westminster to tell the Scottish Government what to do. I think the situation is clear. The Scottish Parliament was able, in relation to a wish to see additional funding in this area, to demonstrate the effectiveness of the Scottish Parliament in forcing the Scottish Government to put in additional funding. If the view of the Scottish Parliament is that there should be some recompense, that would be the way to take it forward.

Q5607 Lindsay Roy: But you personally have no opinion on this.

David Mundell: I do not think that it would be helpful for me to be seen to be telling the Scottish Government or the Scottish Parliament what to do.

Q5608 Chair: Can I seek clarification on a couple of points arising from what Lindsay said? I think you have given it but I want to be absolutely clear. I think you were saying to us that the lifting of the cap effectively allows the Scottish Government to cancel the impact of the bedroom tax for everyone in Scotland this year. Is that your understanding?

David Mundell: I would not phrase it like that, but that could be—that is my understanding.

Q5609 Chair: That is for this year. For last year, my understanding from previous discussions we have had is that the power that the Scottish Government already had would allow them, if they wished, to write off any debts that had been accumulated. Is that still your understanding?

David Mundell: That, in general terms, would be my understanding.

Q5610 Chair: Without asking you to say whether or not you are in favour of it, my understanding is that the Scottish Government had before, but certainly have now, the power, if they wish, to refund any bedroom tax payments that were made by anybody last year.

David Mundell: What they cannot do is make payments directly to individuals that could be construed as the operation of a welfare system. As we have discussed before, welfare vis-à-vis payments to individuals is a reserved matter. It would seem to me that, if thought was applied, some form of process could be drawn up to achieve the objective you set out, but I am not able to set out what that is.

Q5611 Chair: After you said to us in our hearings that you thought the Scottish Government had powers to deal with various things, we asked Margaret Burgess whether or not she had pursued this with you to seek clarification. Can you let us know whether or not the Scottish Government ever came to you when you indicated you thought they had powers to go beyond those they already had, and pursued that with you?

David Mundell: There was no direct dialogue with me.

Q5612 Lindsay Roy: Do you think that housing benefit under the welfare system should be devolved?

David Mundell: We always need to look at the balance between reserved and devolved responsibilities and between local decision making and getting decisions which are specific and relevant to the people of Scotland, and the benefits of having UK-based systems. As Pamela set out, at the moment each of the political parties is coming forward with proposals for additional devolution. The Conservative proposal will be tabled, or made public, at the end of May. I know that the commission under Lord Strathclyde has looked at this issue. I am looking forward to seeing what their conclusion is. It is an important part of the debate in judging the benefits of the wider UK pensions and benefits system set against more local needs. We have to debate and discuss where that balance lies.

Q5613 Lindsay Roy: It has been on the table, and the answer at the moment is "Maybe."

David Mundell: I think it is an issue worthy of significant debate.

Q5614 Chair: To be fair, it is not simply a question of it being devolved or retained; it is a question of whether housing benefit is to do with housing or to do benefit, isn't it?

David Mundell: It is where the balance lies. I think that is what we should be discussing, not that if we do not like a particular way the benefit system or housing is administered we tear up our country. In my view that is not what we do. We have a debate; people vote, and that is how policy is determined.

Q5615 Chair: I think that covers all the points that we had. As I indicated to you privately before we started, we always like to end these things by asking whether or not there are any answers you had prepared to questions that we have not asked, or any issues that you feel we should have touched on that we haven't. Is there anything you want to leave us with that we have not gone over?

Steve Webb: If I may make a concluding observation, for me the biggest message is one of uncertainty about people's future pensions, how they will be paid, what they will be and how they will be organised. We are spending all our time on UK pension policy trying to give people greater certainty and firm foundations and enabling them to plan. Part of the colour of the replies that I have given is that in many of these areas it is very difficult to know what might happen. Clearly, we will act in good faith—of course we will—but the prospect of independence—separation—creates huge uncertainties and real cost, setting up new systems and all the rest of it, and periods of great uncertainty. We want people to plan ahead for their retirement with confidence and certainty, and so many of these issues would be thrown into uncertainty in the event of a yes vote.

David Mundell: I think that is correct. I launched this analysis paper with the Secretary of State, along with the Institute of Actuaries. You can imagine that that was a non-stop fun event. As in the course of so many of these publications, it has not been met with any counterfactual statement; it has been met, as you alluded to earlier, by the usual scaremongering general statement, but the basic underlying information in the publication has not been challenged.

Chair: With an apology to any actuaries who might have been offended by that last statement—they have full and complete social and family lives—thank you for coming along.