

What's the big deal?

The policy sticking points for post-election negotiations

April 2015

The prospects for post-election talks between the political parties have often sounded like a logic puzzle during this campaign. Leo has ruled out a coalition with Brad, on the terms insinuated by Johnny. Meanwhile, Brad and Ryan have refused to comment on those same terms, though Ryan has used the opportunity of being asked the question to suggest that Leo will have no option but to strike a deal on a vote by vote basis with Johnny. Leo likes yellow whereas Brad does not dislike green. In 3 years, Johnny will be twice the age that Ryan was 15 years ago. Who has the most apples?

But it doesn't have to be like this. All the parties have published detailed manifestos and we can use these to work out the potential scope of a deal. In the end, the numbers of seats they have won in the new Parliament and other political facts will make a big difference. However, we can use the degree of policy agreement – or disagreement – as a starting point to frame the kind of discussions they will be having.

This briefing note looks in detail at the substance of four discussions: those between Conservatives and Liberal Democrats; Labour and Liberal Democrats; Labour and SNP; and Conservatives and UKIP. In each case the briefing identifies the likely sticking points for a deal – and how these might be resolved. While current polling suggests that any post-election deal may involve more than two parties, this briefing assumes that the core agreement will be based on negotiations between two parties which may then be supported by one or more additional parties.

SUMMARY:

- Contrary to what the parties may have said during the election campaign, we find that the prospects for potential deal-making are good.
- We find the deal that has been most fervently ruled out by one of the likely deal-makers – Labour, commenting on doing a deal with the SNP – looks to be the most achievable, particularly if done on an issue-by-issue basis.
- A new deal between the current partners of the Coalition, the Conservatives and Liberal Democrats, appears more difficult as it will require more negotiation and compromise between the parties than we might assume at first glance. Arguably, the two parties have used up most of the consensus that there is between them during the previous Parliament; and the next one looks more difficult.
- While it is unlikely there will be a comprehensive agreement between the two parties, Labour and the Liberal Democrats would be able to agree on most of the 'big ticket' items, with one notable exception – university tuition fees.
- A Conservative-UKIP deal is easily achievable on issues of domestic policy. The key to any negotiation will be agreeing the date on which a referendum on EU membership is held.

SUMMARY OF PROSPECTS FOR A DEAL AND POLICY STICKING POINTS

	CON - LIB	LAB - LIB	LAB - SNP	CON - UKIP
PROSPECTS	<p>Harder than it looks. Five years of Coalition have used up much of the common ground.</p> <p>Both parties will have to swallow hard and make big compromises.</p>	<p>There will be no comprehensive agreement, e.g. Liberal Democrats will refuse to back Labour on tuition fees.</p> <p>But other big ticket items will be agreed.</p>	<p>The key negotiations will happen after the Queen's Speech, i.e. the disagreements are on detail rather than overall direction.</p>	<p>UKIP likely to be malleable on issues of domestic policy. The key is the referendum on Europe.</p>
STICKING POINTS & WHAT A DEAL MIGHT LOOK LIKE	<p>DEFICIT REDUCTION Conservatives will flex towards the gentler position of Liberal Democrats. In the end future growth and tax revenues are more important factors than what parties have said so far.</p>	<p>DEFICIT REDUCTION Labour will have to deliver on spending cuts rather than rely only on increased tax revenues. But fundamentally both parties have the same objective.</p>	<p>DEFICIT REDUCTION Labour and SNP plans are broadly comparable, including tax changes.</p>	<p>EUROPE Conservatives could agree to referendum in 2016 as opposed to preferred date of 2017. Such an agreement would likely also be aimed at keeping anti-EU Tory backbenchers in check on other votes.</p>
	<p>WELFARE Conservatives will not achieve savings of £12bn. A much more modest figure is likely to become the new target, and that may be a relief to the party itself.</p>	<p>TAX Mansion tax is the common ground. Someone will have to blink first on resolving the other differences: tax for those on low pay; and the top rate.</p>	<p>TRIDENT Labour could play this into 2016 by starting a new review. It will rely on Conservative votes if it presses ahead with renewal.</p>	
	<p>TAX Conservatives will fail to raise higher rate threshold all the way to £50,000. Liberal Democrats will give up on mansion tax.</p>	<p>TUITION FEES Liberal Democrats will refuse to back Labour on the proposed cut in fees. Labour will go it alone and hope to win a vote with SNP support.</p>	<p>FULL FISCAL RESPONSIBILITY Hard to see how Labour stops SNP's campaign for further powers to be devolved.</p>	
		<p>ENERGY PRICE FREEZE Liberal Democrats may agree to the freeze but in exchange for Labour holding back on market reform.</p>		

1. STICKING POINTS: CONSERVATIVES & LIBERAL DEMOCRATS

SUMMARY

Five years of cooperation and compromise creates the bedrock for five more. But the previous Coalition means the two parties have also used up much of the common ground that there is between them. They had already agreed to disagree, for example, on deficit reduction with Danny Alexander presenting an 'alternative Budget' on the day after the Chancellor's 2015 Budget. As well as deficit reduction, the most obvious sticking points for a new deal will be welfare cuts and tax policy.

In a coalition, Conservatives will have to compromise on achieving a full £12bn in welfare cuts. Though they may be glad enough to do that, given they do not seem to have concrete plans for how to achieve reductions on that scale. Equally they are unlikely to be able to raise the higher rate income tax threshold all the way to £50,000. And property revaluation for the purposes of calculating council tax may be the best that Liberal Democrats can hope to achieve as a way of increasing progressive taxation on property.

DEFICIT REDUCTION

Conservatives and Liberal Democrats have both set out two phases to the deficit reduction programme.

The two parties agree on the aim of Phase 1, to balance the structural¹ current budget (that is, excluding investment spending) by 2017-18. However, they disagree on how this should be done.

- Conservative plans involve making £12 billion in welfare cuts; £5 billion from reducing tax evasion and aggressive tax avoidance and planning; and £13 billion from departments.
- Liberal Democrats say they would reject Conservative proposal to finish the deficit reduction programme through spending cuts alone. Instead, they would rely more on tax rises.

The two parties differ on Phase 2 as well – the period after 2017-18.

- Conservatives aim to run an overall surplus (that is on total revenues minus total spending including investment spending) by 2018-19. This would mean no borrowing, so that the Government can start to “pay down our debts”.
- Liberal Democrats would like to allow borrowing for capital investment, and see capital investment rise as a share of GDP. According to the “alternative fiscal scenario” that Danny Alexander presented on the day after the Budget, the Liberal Democrats would not seek to eliminate borrowing – but would want to reduce it to around £17 billion by 2019-20.²

Can a deal be done?

Arguably, differences on Phase 1 of deficit reduction could be reconciled by shifting the balance of cuts versus tax rises. In his budget debate speech, Danny Alexander talked of £6 billion in tax rises and an additional £6 billion from tax evasion and avoidance,³ on top of that planned by Conservatives. Conservatives have ruled out rises in taxes. However, removing some tax reliefs (estimated to be worth around £100 billion⁴) might be an option that is palatable to both parties.

Differences in Phase 2 are easier to reconcile if economic conditions are benign and tax revenues continue to grow over time, as currently forecast by the Office for Budget Responsibility (OBR). Conservatives do not have a specific commitment for 2019-20. So one option could be to allow investment spending to grow in real terms after the 2018-19 target date. This might, however, mean a “rollercoaster” profile for investment spending.

Alternatively, Conservatives could allow spending to grow after 2017-18, as long as debt continues to fall as a percentage of GDP. This would mean potentially abandoning the plan to eliminate borrowing, but it would still mean that debt is on a sustainable path. It would also help meet the Conservative aim to grow investment at least in line with GDP.

Finally, the two parties could postpone the decision: they could agree soon after the election on a spending plan covering Phase 1, the years to 2017-18, with the intention of conducting a spending review to cover the final two years of the Parliament at a later date. This would have the advantage of being able to take into account more up-to-date forecasts of the state of the economy, which will have substantial implications for the health of the public finances.

WELFARE

Conservatives and Liberal Democrats have several areas of agreement, but also several of disagreement, on their welfare policies for the next parliament. Key areas of agreement include the protection of pensioners from almost all cuts and the commitment to the ‘triple lock’ that will see pensioner benefits increasing further as a share of national income during the next parliament. Both parties are committed to the full rollout of Universal Credit. There is agreement, in principle if not in detail, that cuts to working age welfare are required.

The main disagreement stems from the magnitude of these cuts. Conservatives have pledged cuts of £12bn, whilst Liberal Democrats have insisted they will not tolerate cuts on this scale, instead suggesting £3bn should be found. But there is only limited detail in either party’s manifesto on exactly how those cuts will be made.

Conservatives plan to freeze most working age benefits for two years, excluding disability benefits; whilst Liberal Democrats favour a 1% cap rather than a freeze. Conservatives have also pledged to reduce the cap on household benefits from £26,000 to £23,000; and to prevent 18 to 21 year old JSA claimants from receiving housing benefit. Both policies are not explicitly supported by Liberal Democrats.

Instead, Liberal Democrats have proposed making savings from housing benefit by offering landlords the option of housing benefit being paid directly to them, but in return for a discount to the government. They have suggested withdrawing the Winter Fuel Payment and free TV licence for wealthy pensioners. But they are also committed to being seen as the ‘heart’ of the next government, with proposals to review benefit sanctions, and more emphasis on support for disabled people in work, rather than Conservatives emphasis on Work Capability Assessments.

Can a deal be done?

Despite these differences, there is room here for some deals to be made. It will be crucial for Liberal Democrats to be seen to have softened the Conservatives’ approach, so they could insist on their review of sanctions in return for agreeing to the benefit freeze (or perhaps a reduced cap of 0.5%).

Conservatives could be persuaded to agree to the Liberal Democrat housing benefit discount policy. It would be a concession by them, as it is a departure from their position that forcing

benefit claimants to pay their own rent emphasises personal responsibility. However our estimates suggest the policy could save around £400m, so it would be useful in getting towards the ambitious £12bn target for welfare savings set by Conservatives. The idea is also popular with both tenants and landlords.

The main difficulty in potential coalition discussions over welfare is, however, that neither party has put forward policies that are likely to save very much money. This is particularly problematic for Conservatives. The Institute for Fiscal Studies (IFS) has predicted that their policies will so far contribute just £1.1bn to their £12bn target. The most meaningful parts of the negotiations, therefore, may well be over policies that have not as yet been formally proposed.

What are the possibilities for saving large sums? One measure likely to find consensus between the parties is the leaked Conservative plan to replace the Industrial Injuries Compensation Scheme, with an estimated saving of £1bn. However, other policies would be much more controversial. Conservatives could propose a freeze of working age benefits for the whole parliament, rather than just two years. But this would be a big concession by Liberal Democrats and would damage their image of being the government's 'heart'. An alternative is the abolition of child benefit, replacing it with a means tested element that is incorporated into universal credit. The IFS has estimated this could save around £5bn, but would again be a significant concession by Liberal Democrats. Going forward with either of these policies would surely require Liberal Democrats to be granted their wishes on all other welfare policies, such as an end to sanctions except as a last resort, and retaining the benefit cap at median earnings (rather than cutting to £23,000).

There is one other area in which Conservatives hope their policies will lead to savings in the welfare security budget, but in which the magnitude of the savings is highly uncertain. In their manifesto they pledge to halve the disability employment gap. Getting more disabled people into work has been government policy for several years, with an official document in 2010 recognising explicitly that one of the aims of Work Capability Assessments (WCAs) and migrating people with disabilities onto ESA was to save money – estimated at £500m at the time.⁵ But any such move will probably have to be accompanied by more support for disabled people in work, including programmes such as Access to Work. Equally, Liberal Democrats have promised a review of WCAs, no doubt due to concerns that there is considerable hardship being brought on people that were incorrectly judged to be fit for work.

TAX

Conservatives have wholeheartedly taken up the Liberal Democrat proposal to raise the income tax Personal Allowance threshold, over which there is substantial agreement between the parties (aside from who should take the credit, perhaps). Both parties are committed to raising it further, to £12,500, by the end of the next parliament.

However, there are two taxes over which there is disagreement. Conservatives want to raise the threshold for paying the higher rate of income tax to £50,000. Liberal Democrats have been silent on this, but instead have proposed a mansion tax on homes worth over £2m – a policy that is extremely unlikely to be favoured by Conservatives.

Can a deal be done?

There may be two options for compromise on income tax. The first would be to raise the higher rate threshold only in line with increases in the Personal Allowance. By this logic, it will rise by £1,900 over the parliament to around £44,000. This would allow Liberal Democrats to say they have succeeded in stopping Conservatives raising the threshold all the way to £50,000, but also

allow Conservatives to deliver a part of their policy. It would obviously also have the benefit, to both parties, of raising income tax receipts (compared to an increase to the £50,000 level), helping the government to eliminate the deficit sooner.

An alternative compromise that might be more favourable to Conservatives would be to explicitly link the higher rate threshold to some other measure – as Conservatives have proposed already in linking the Personal Allowance with the Minimum Wage. The higher rate threshold currently stands at a very similar level to the 80th earnings percentile for full-time employees. It could be advantageous for Conservatives to guarantee that ‘only the top fifth of earners’ would ever pay the higher rate when they are in government, and so the uprating of the threshold could be linked to the 80th percentile. This would be particularly useful to counter a common media narrative that ‘middle earners’ are increasingly being dragged into the higher rate. Under this system it would take an extremely optimistic prediction of earnings growth for the higher rate to be raised to over £50,000 by the end of the parliament, and so Liberal Democrats could still maintain they had achieved a smaller increase than that proposed by their partners.

The Liberal Democrat proposal for a Mansion Tax would also be a sticking point in coalition discussions. It would be hard for Conservatives to accept this, given their commitment to a ‘property-owning democracy’ and plans to extend exemptions from Inheritance Tax. But a compromise could potentially be reached by Liberal Democrat dropping the mansion tax and focusing instead on a reform of Council Tax – which was Liberal Democrats policy until very recently. This reform – perhaps more acceptable to Conservatives, although still difficult - could take the form of a property revaluation to bring the old 1991 valuations up-to-date.

Such revaluation would be likely to find the difference between low and high value properties had increased markedly, which could be used as justification to make the council tax banding system more progressive. At present council tax liabilities represent a lower proportion of income for people in higher-band properties, and council tax is also a much lower proportion of the property’s value in higher bands.⁶ Liberal Democrats could also push further for additional bands for more expensive properties, to make the reform closer to their proposals for a mansion tax, though their potential partners are unlikely to go that far.

2. STICKING POINTS: LABOUR & LIBERAL DEMOCRATS

SUMMARY

Labour and the Liberal Democrats have a route to a deal but both parties will have to make significant compromises. Labour will have to go some way towards Liberal Democrat plans on deficit reduction rather than rely only on increased tax revenues. But Labour's own planning suggests that cuts in departmental spending are to be made anyway.

On tax for low earners, the parties have opposing plans: a 10p starting rate of tax versus further increases in the Personal Allowance. Something will have to give, or both could change the conversation by increasing the threshold for National Insurance Contributions instead – a solid and arguably better targeted offer to those on low pay.

Liberal Democrats are unlikely to agree to Labour's plan for a cut in tuition fees. Labour may face a Commons defeat on this issue if Liberal Democrats vote alongside Opposition MPs (depending on the size of the SNP bloc, who will likely back Labour's position). The energy price freeze is another contentious issue. Labour may get the freeze but in exchange for pausing on market reform until the regulator has reported.

DEFICIT REDUCTION

Labour does not set out a specific deadline for balancing the books. It says it will "cut the deficit every year". It also says it will "get national debt falling and a surplus on the current budget as soon as possible in the next Parliament". In principle, if "as soon as possible" ends up being "by the end of the Parliament", that is, 2020, Labour would not need to make any spending cuts beyond the first year of the Parliament – 2015-16.⁷

Liberal Democrats have been more specific about their targets. They would want to balance the structural current budget by 2017-18, potentially up to two years earlier than Labour. After 2017-18, they would want to see debt falling as a percentage of GDP, but have capital investment increasing as a share of GDP.

Can a deal be done?

In effect, Labour and Liberal Democrats broadly agree on the objective – balancing the current budget. There is a potential disagreement on timing. The timing is important because of the expected growth of tax revenues. As tax revenues are expected to grow every year, the current budget can be balanced without having to make cuts – if the Government is prepared to wait until 2020. If the aim is to bring the current budget into balance earlier – by 2017-18, cuts do need to be made.

However, there are a number of reasons to think the two positions are reconcilable, with Labour agreeing to target the earlier date of 2017-18 in exchange for Liberal Democrats easing up on the amount of consolidation that is needed.

Labour have already said they would plan to make some spending cuts, saying in their manifesto that there will be cuts in spending outside health, education and international development (which are three areas also prioritised by the Liberal Democrats). This suggests they are not planning on the loosest possible interpretation of their target. Equally, in his Budget debate

speech, Danny Alexander spoke of a £30 billion consolidation by 2017-18. But in practice, this could be reduced to around £20 billion and still allow the current budget to be balanced by 2017-18. This makes the task slightly easier. Finally, there are a range of similar tax measures that both parties promote in their manifestos, which could also contribute to deficit reduction. These include taxes on properties worth over £2 million, reducing tax avoidance and increased levies on banks.

TAX

Labour and the Liberal Democrats differ on tax policy. The Liberal Democrats' flagship tax policy is to raise the Personal Allowance to £12,500 over the course of the next parliament. Labour have been silent on this issue, instead focusing on their two main tax policies: to implement a 10% tax band, paid for by the abolition of the married couples' transferable personal allowance; and to raise the additional rate from 45p to 50p.

Despite these differences, there are clearly some shared motivations apparent from the two parties' manifestos. In particular, both are committed to helping people on low and middle incomes, and to ensuring the wealthiest pay a larger share.

Increasing the Personal Allowance to £12,500 would represent a tax cut for everyone paying income tax, aside from those earning over around £125,000. The biggest gainers (as a % change in income) are those in the 4th income decile – that is middle, rather than low earners. 69% of the tax cuts go to those in the top half of the income distribution, due in part to the fact that 44% of adults now do not pay income tax at all.⁸

Labour's 10p tax band makes even less sense, given their motivations. It is paid for by the abolition of the transferable personal allowance, meaning they have a limited budget to work with. The IFS have calculated this would mean a new 10p band applicable to just £260 of income – and worth only 50p a week for most income tax payers.⁹ In practice the 10p band would be so small as to be almost indistinguishable from the Personal Allowance threshold, and creates additional and unnecessary complexity in the tax system.

Can a deal be done?

The easiest route to a deal is for Labour to drop their proposal of a 10p tax band and agree to some form of increase to the Personal Allowance – it is a popular policy. But the problem for Labour in particular is that increasing the Personal Allowance is not a policy that is well targeted on helping the low paid.

If helping low income workers is the objective that is most important to both parties, then a better option may be to change the conversation to focus on the National Insurance threshold instead. If this was brought up to the level of the current Personal Allowance threshold this would help a greater number of low income people than raising the Personal Allowance threshold, or creating a 10p tax band. This would also make the tax system simpler.

The other issue is the 50p additional rate proposed by Labour. Practically, Liberal Democrats will have to concede on this, or risk being seen as protecting wealthy taxpayers.

TUITION FEES

Labour's manifesto promises to lower the cap on undergraduate tuition fees from £9,000 per year to £6,000. This is funded by changes in the tax relief available for pensions saving. Both halves of the policy are problematic for a Lab-Lib deal.

Liberal Democrats have been highly critical of the proposal to reduce the fees cap. Vince Cable, who as Business Secretary took through funding reforms in the 2010-15 Parliament, has commented, "Talk about the current system being unsustainable is rubbish . . . A £6,000 [fee cap] would wreck the financial sustainability of universities, reduce the support for disadvantaged students and benefit only the richest."

There is some hyperbole here, perhaps understandably, given the political cost to the Liberal Democrats from the changes made recently, though it's certainly clear that reducing fees will leave a funding gap for universities, unless a new government provides additional public funding; and that low and middle-income graduates will receive no benefit from a cut in fees because payment is already linked to earnings. On changes to pension tax relief as a way of raising the money to provide universities with more funding, the Liberal Democrats prefer a review that looks at the whole set of reliefs rather than tinkering with some parts and they do not assume that there will be savings to devote to other public spending.

Can a deal be done?

Labour cannot compromise on trying to reduce tuition fees, not least because they have attacked the Liberal Democrats for reneging on their pledge on fees in 2010. So the question is what Liberal Democrats can receive in exchange for allowing Labour to do that; and it may be that nothing will do, in which case they will agree to disagree, voting against their coalition partners when the issue comes to Parliament.

There are no obvious trades within higher education policy. The Liberal Democrats' manifesto mentions with pride the support they have begun to introduce while in government for postgraduate students. The consultation on loans for postgraduate study is incomplete with decisions on the detail and guarantees of funding still to be made. Liberal Democrats could press to continue this policy as part of a deal. But a Labour-led government would be under pressure to do that anyway.

Liberal Democrats have promised a new review of higher education funding over the next Parliament with a particular focus on support for living costs. Again, Labour has said that it is already sympathetic to improving support for these costs, so making progress on this would not be a Liberal Democrat 'win'.

Our assessment is that, unless Labour is willing to give way to the Liberal Democrats' priorities on some other area of policy, then no deal will be reached on the issue of cutting tuition fees. Liberal Democrat MPs may be able to combine with Opposition MPs to defeat Labour when it comes to a Parliamentary vote.

ENERGY PRICES

The promise to cap energy prices for households recurs in Labour's manifesto. Despite the fall in both wholesale prices and household energy bills since the policy was first announced in late 2013, Labour remain determined to address what they see as critical failings in the way the market runs and is regulated. They see the freeze as vital to "protect consumers" while they "reform the energy market so that it delivers fairer prices".

Liberal Democrats have indicated that they do not support a price freeze, expressing concern that it would kill off nascent competition in the market by hitting small new suppliers harder than the 'Big 6'. Instead, the party's manifesto makes a promise to "back new entrants to the energy

market ... aiming for at least 30% of the household market to be supplied by competitors to the 'Big 6' by 2020."

Can a deal be done?

Delivering the price freeze will be important for a Labour-led government; it helps to characterise their position as an activist on behalf of consumers. And, if the biggest concern of Liberal Democrats at a practical level is that a price freeze hits competition, then it's arguable that falling wholesale prices mean that there is now less of a threat for smaller firms. There is unlikely to be significant upward pressure on wholesale prices in the next 18 months or so – essentially, over the duration of the proposed freeze. This may go some way to reducing Liberal Democrat anxieties about the impact of a freeze on smaller energy suppliers.

In return, Liberal Democrats are likely to demand that, before making any other reforms to the market, Labour holds on until the outcome of the ongoing Competition and Markets Authority (CMA) investigation, which is due to report in December. So long as the price freeze is implemented quickly, Liberal Democrats may persuade Labour to wait.

But this does store up disagreement. The CMA has already suggested that neither vertical integration nor a lack of liquidity is a substantial problem in the market, whereas Labour have committed to end vertical integration of firms involved in both generation and supply and to force firms to trade all energy on an open exchange with the aim of improving liquidity. Waiting for the CMA – and then adapting future reform to its findings – may create the impression that Liberal Democrats have prevailed over Labour in this area.

3. STICKING POINTS: LABOUR & SNP

SUMMARY

Both parties appear to be ruling out a formal coalition; and Nicola Sturgeon has suggested that the SNP will vote for a Queen's Speech put forward by a Labour Government, then work on policy detail afterwards.

While practically deals can be reached on detail within the framework of a stable government, Labour will face significant threats to its authority, for example, on Trident, potentially having to rely on Conservative votes if it wants renewal, or going back to the drawing board for alternatives; and to its electoral position in Scotland, as the SNP continues its campaign for full fiscal responsibility.

DEFICIT REDUCTION

The SNP has said that its objective is to end austerity. It wants spending by Government departments to increase by 0.5% above inflation every year after 2015-16. It expects that this will still allow the deficit to fall in every year and achieve a balanced current budget (although it sets no deadline for the latter).

Can a deal be done?

The SNP's position is just about consistent with Labour's plan. Labour also want to see the deficit fall in every year and achieve a balanced current budget "as soon as possible", if "as soon as possible" is stretched to mean 2020. If tax revenues do grow as forecast by the OBR – by around £20 billion a year, it will be possible to both increase spending and reduce the deficit over time. Under SNP plans to increase departmental spending, the current budget target would be achieved at the end of the Parliament – by 2019-20, when a surplus of £1 billion could be run.

If Labour wanted to move more quickly on reducing the deficit, it could do this through tax measures. The SNP has already said it will vote for a number of potential tax-raising policies set out in Labour's manifesto, including introducing a 50p rate of tax for those earning over £150,000, a tax on bankers' bonuses, a tax on properties worth over £2 million, measures to reduce tax avoidance, abolishing non-dom status and ending tax allowances for married couples.

TRIDENT

Despite some of the rhetoric, there is scope for a deal on renewing Trident. On launching the SNP manifesto, Nicola Sturgeon said, "We will seek to build an alliance in the House of Commons against the renewal of Trident". Labour, by comparison, and according to its manifesto, "remains committed to a minimum, credible, independent nuclear capability, delivered through a Continuous At-Sea Deterrent".

However, that statement can be read in the context of two others. First, Labour's manifesto goes on to say, "We will actively work to increase momentum on global multilateral disarmament efforts and negotiations, and look at further reductions in global stockpiles and the numbers of weapons." This is a statement that might often be repeated, if for no other reason than to provide pleasant mood music, during any discussions with the SNP.

Secondly, all of the specific material on defence is premised by the commitment to “conduct a Strategic Defence and Security Review in the first year of government, with an inclusive national debate”. This is an important piece of process.

Can a deal be done?

Neither party has to shift its position on Trident immediately. The review promised in Labour’s manifesto allows discussions on the formation of a Labour-led government to be decoupled from the decision to renew Trident. Indeed, the one year timeframe for the review means that a decision can even be pushed to the other side of the elections for the Scottish Parliament on 5 May 2016.

Whatever the timing, the review could return options for discussion. At this point, a Labour-led government could press ahead with Trident renewal without SNP support and aim to get enough votes or abstentions among Opposition MPs to pass the Commons. Despite what they are saying currently, most Conservatives can be expected to vote with a Labour Government on this issue.

A cheaper alternative to Trident may be to implement an airborne rather than continuous at-sea deterrent.¹⁰ This would release savings to be deployed either elsewhere in the defence budget or on other public services; and have the added potential advantage of removing nuclear weapons from Scottish soil. This may be enough to secure the cooperation of the SNP in a parliamentary vote.

Another option for a Labour-led government may be to declare in advance that it will allow a free vote on the options for Trident renewal. This will obviate the need to make an agreement with the SNP, though it is risky – governments are normally expected to provide a stronger lead on issues of national security. However, it may minimise the impact on the government of any dissent within Labour, as well as make it easier for Opposition MPs to vote with their conscience.

FULL FISCAL RESPONSIBILITY

The SNP’s manifesto contends that the measures arising from the Smith Commission, which in itself followed the pledge of further devolution made by the unionist parties during the campaign for the independence referendum, are insufficient. The next steps wanted by the SNP are devolution of corporation tax, National Insurance Contributions and welfare.

By contrast, Labour’s manifesto focuses on the effect of implementing the Smith Commission proposals through a Home Rule Bill. It is worth remembering that the new Parliament in Westminster will be debating and voting on this Bill early on. By its terms, Scotland’s Parliament will gain control over income tax rates and bands, air passenger duty, half of VAT receipts and some benefits. To put it another way, “fiscal responsibility” will rise from around 7% of the Scottish Government’s budget to around one half.

Can a deal be done?

The passage of the Home Rule Bill will provide an early test of a new Labour-led government. The SNP should be expected to propose amendments that continue the journey towards full fiscal responsibility. Labour could refuse to make a deal on any of these, relying on votes or abstentions among Opposition MPs to win. But this will make it all the harder for Labour to recover ground from the SNP at elections for the Scottish Parliament in May 2016. Tactically, Conservatives or Liberal Democrats may decide in any case to vote with the SNP, e.g. on the devolution of corporation tax rates – a power that has already been passed to the Assembly in Northern Ireland – either on the principle or to defeat the Labour-led government or both.

To manage these risks, Labour could offer a package of further devolution to the SNP. The SNP may take that in order to bank progress towards full fiscal responsibility, especially as such a deal may reinforce its narrative on winning new powers for Scotland and do precious little for Labour's own cause in May 2016.

The one option available to Labour in changing the terms of debate on devolution may be in reform of the House of Lords. Labour has said that its ambition is to create an elected Senate of the Nations and Regions following a wide-ranging Constitutional Convention that involves citizens and civil society organisations. Creating a fresh, cross-national, UK-wide representative body might usher in a new era for unionism and check SNP momentum. Even if that is wishful thinking, the SNP may have to engage positively with what Labour proposes in any attempt to make the UK's institutional architecture more devolution-friendly, especially if Labour moves forward on this issue before the SNP raises the prospect of a new referendum on independence.

4. STICKING POINTS: CONSERVATIVES & UKIP

SUMMARY

Any relationship between Conservatives and UKIP is likely to be informal (confidence and supply) rather than formal (coalition).

Domestic policy is unlikely to matter that much. In their manifestos, the two parties agree on a surprising amount: more money for the NHS, lower taxes for the low paid, lower taxes for middle earners and the scrapping of the Human Rights Act. This shouldn't mask the differences: UKIP proposes to abolish the £5bn Barnett formula, the Conservatives to retain it; UKIP wants to bin HS2, the Conservatives see it as part of the route to the 'Northern Powerhouse'; UKIP are strongly against privatisation in the NHS, the Conservatives have introduced more since 2010; and UKIP wish to reduce foreign aid to 0.2% of GDP, the Conservatives retain it at 0.7%.

However, UKIP should be considered malleable on many aspects of domestic policy. This is not merely because of their genesis as a single-issue party; many of their manifesto policies have changed dramatically between 2010 and 2015, implying that they may not put a very high price on achieving them. Anti-market policies for the NHS in 2015 were countered with very pro-market policies in 2010, including tendering out key services to profit-making companies and opt-outs for patients. In 2010, UKIP argued for three new high-speed lines including a north-south route; the policy is now to scrap 'the HS2 vanity project, which will benefit the few at the expense of many'; even cutting foreign aid is a new preoccupation for UKIP. On these matters, we would expect UKIP to give ground. The only major policy where UKIP has consistently differed from the Conservatives is over proportional representation – UKIP supports it. This is a debate that Conservatives could cut off at the pass with reference to the 2011 referendum on AV.

EU REFERENDUM

For these reasons, the viability of a Conservative Government supported by UKIP is likely to be determined solely by the founding purpose of UKIP – Europe. Despite the fact that both parties are standing on a platform of an in/out referendum on Europe, there are significant sticking points.

The ideal scenario for UKIP would be an immediate referendum on Europe. At the most basic level, this would ensure that the referendum takes place before a change of government. At a more strategic level, a prompt referendum would deny pro-Europeans the opportunity to build a more compelling case for European membership by renegotiating terms of membership. For their part, the Conservative Party (a significant part of which is pro-European) under Cameron has relied heavily on 'renegotiation' both as a route to postpone (or even make redundant) a referendum on Europe and as a means of going to the population with a stronger reason to remain 'in'. As a means to achieving the latter, the Conservative Party gives itself until the end of 2017 to hold the referendum.¹¹ A 2015 referendum would give the sitting government little time to open conversations with European leaders let alone agree actual terms.

Can a deal be done?

UKIP has argued publicly for a more rapid referendum than any other party would facilitate. Prior to the campaign, Farage cited timing as the price of UKIP support.¹² This was summed up in his quote: 'I want a full and fair referendum to be held in 2015 to allow Britons to vote on being in or

out of the European Union. There would be no wiggle room for “renegotiation” somewhere down the line.’

Despite this (and somewhat surprisingly), the UKIP manifesto does not pledge a deadline for achieving a referendum, instead calling for ‘a referendum on our membership of the EU as soon as possible’.¹³ This may be tactical. Or it may be a mistake. If Conservatives wanted to be tough, they could refuse to give ground on the referendum date. However, Conservatives might offer a European referendum in 2016 (rather than 2017) for the sake of managing elements in the party itself; and the flexibility in UKIP’s manifesto would allow them to accept that as a reasonable *quid pro quo* for their support to a Conservative government.

Without giving ground on the date, Conservatives could potentially cement a deal with UKIP in any case by legislating for a referendum – including a fixed date for it – in the first Queen’s Speech.

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REFERENCES

- ¹ This is a measure of the budget that takes into account the effect of the economic cycle. On the OBR's forecast, the economy will be neither over-heating nor under-performing in 2017-18, so in this year there is no difference between the current budget and structural current budget.
- ² https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/414486/Fiscal_Scenarios_FINAL4.pdf
- ³ <https://www.gov.uk/government/speeches/chief-secretary-budget-debate-speech>
- ⁴ <http://www.nao.org.uk/wp-content/uploads/2014/03/Tax-reliefs.pdf>
- ⁵ http://www.legislation.gov.uk/uksi/2010/875/pdfs/uksiem_20100875_en.pdf
- ⁶ <http://www.ifs.org.uk/comms/comm123.pdf>
- ⁷ The 2015-16 cuts have already been allocated in the 2013 Spending Review and Labour has previously said it would abide by the budget for that year.
- ⁸ http://www.ifs.org.uk/uploads/publications/bns/BN172_executive_summary.pdf
- ⁹ http://www.ifs.org.uk/uploads/publications/bns/BN172_executive_summary.pdf
- ¹⁰ <http://www.centreforum.org/index.php/mainpublications/719-retiring-trident>
- ¹¹ Conservative Party Manifesto 2015
- ¹² <http://www.theguardian.com/politics/2015/mar/15/ukip-nigel-farage-support-conservatives-eu-referendum-before-christmas>
- ¹³ UKIP Manifesto 2015