Funding the Future

Only a new currency could set Scotland free

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The Scottish Growth Commission of the SNP is, I am told, reporting this coming Friday.

One of the key issues for the Commission will be the central one of which currency Scotland should use if it were to be independent. I hear rumour that it will not be the euro. Equally, I hear rumour that it will be the pound, before transitioning to a Scottish currency. But, I stress, rumours can be wrong.

My own position on this is clear, and is reflected in my White Paper on Scottish Taxation after independence written for Common Weal last year. In the summary of that paper I said:

If Scotland is to have a sound tax system then it must be based on economic reality. It is widely believed that tax is necessary to pay for government provided services. It has, however, recently been realised that this is not the case. This is because all government services can in principle be paid for either by a central bank creating new money or by quantitative easing ('QE') operations (which amount to much the same thing).

This understanding is critical to the design of a Scottish tax system. What it demands is that Scotland must have its own currency from the day it becomes independent. This is because of another critical consequence of the understanding of tax and money, which is that a country with its own central bank and currency cannot go bankrupt.

What should also be clear is that a Scottish currency is also essential for the creation of an effective tax policy for an independent Scotland. This is because if a country has its own currency then there is technically no limit to what a government can achieve. There are, however, two practical constraints. The first is that the government does not try to create more economic activity than the economy can deliver. And the second is that they must tax sufficiently to cancel enough of the money that the government has created through its spending to ensure that its inflation targets are met.

The implications of this understanding are profound. First, a policy based on this understanding does not require that the Scottish Government balance its budgets.

Secondly, this understanding means that the Scottish Government does not need to think itself beholden to bond markets or their interest rate whims. Third, in this scenario tax entirely ceases to be a mechanism that raises money to pay for government spending. Tax is, instead, a means of reclaiming the money that the government has spent into the economy as a result of that spending.

I am pleased to say that leading independence campaigner Robin McAlpine adopts a similar position in his recent book, ‘How to make a country’.

Scotland could be half-hearted and go for a gradual transition, but if it does three things follow on.

First, it will not be economically independent.

Second, it will have to balance its books, which will be desperate for a new nation needing to invest for its future.

Third, the new social settlement that a Scottish tax system should deliver will not be capable of delivery.

And perhaps as bad, who knows how long the transition will last?

The Commission has to go for an independent currency. Anything less sells the people of Scotland short and would reveal a lack of understanding of tax and money that would be deeply worrying in a party that will seek power as the government of a new country.

Courage is required. It will pay handsome rewards. Scotland would be free.