There are several reasons why a 'Credit Creation Charge' should be better than restricting the issue of loans to a state bank:-

- It could be phased in, gradually increasing the rate of tax so giving banks and the economy time to adjust.
- The level of taxation would act as a much stronger regulator than the present 'Base Rate' guidance on interest rates. Bank lending would dry up when the tax rate reached a level that made lending 'temporary loan money' unprofitable.
- Government could if necessary pump money into the economy at very low cost. If, for example the Home Office borrowed at 7% from the banks, the Treasury could recover up to 5% of that cost in taxation. Keynes would have enjoyed spending it on public works!

Which of these methods would be easiest to implement is hard to say. The world is now so 'global' that either might require coordinated international reform. Yet the current system cries out for reform. It is unjust in normal times. It stores up disaster for many individuals and businesses caught in depressions such as the 'credit crunch' of 2008.

The value of sterling seigniorage lost to the banks in 1999 is estimated in Table 4 line H of Reference 1 as £44.1 billion p.a. In 2007 a private estimate was £70 billion p.a., which is of the order of £1,200 per head of the population! This could enable a very substantial reduction in other taxes.

FURTHER READING

1 Huber & Robinson 'Creating New Money', New Economics Foundation
Online at:www.neweconomics.org/gen/uploads/CreatingNewMoney.pdf

2 Ellen Brown in 'Prosperity' newsletter of the Bromsgrove Group 2008.
See also her book: www.webofdebt.com

3 'Money as Debt', an on-line video at www.1909.org.uk and elsewhere

4 Early Day Motion DM 1449 by Austin Mitchell MP
http://edmi.parliament.uk/EDMi/EDMDetails.aspx?EDMID=35711&SESSION=891

5 Tarek El Diwany 'The Problem with Interest Kreatoc Ltd., 2003.
Abstracts at: www.theproblemwithinterest.com

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RESOURCE REVENUE v COMMON WEALTH

LIBERAL DEMOCRAT

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Action for Land Taxation & Economic Reform

Banking and Seigniorage for the Public Interest

A discussion paper by Bill Powell*

Introduction

People know that the government prints and mints money and then spends it. This government revenue is called 'seigniorage'. This money circulates permanently.

Actually there is at least 20 times more money than that in circulation: cheques, credit cards, internet bank transfers, etc. This money comes into being as loans from banks which can lend money they don't even have. The process is called 'fractional reserve banking'. A bank needs only hold enough money to pay those who at any moment might wish to withdraw their deposit. This is only a fraction of its assets, which are mainly its loans.

A bank simply writes a loan into the account of its borrower. It then circulates among us all as 'money' until the borrower pays it back. The loan is then cancelled and stops circulating as money. That money was not permanent but temporary. It has gone out of existence.

At any moment however there are many bank loans, and so long as their total remains constant a constant amount of this numerical loan money circulates. If it is allowed to increase inflation is likely to follow.

Clearly government derives no seigniorage from this numerical money as it does from printed money. Do the banks?

> ***"Each and every time a bank makes a loan,***
> ***new bank credit is created:***
> ***New deposits - Brand new money"***
> ***G F Towers – Governor, Bank of Canada 1934-54***

*The views expressed here are no necessarily endorsed by ALTER

Option 1: A State Bank

Some say that the government would recover seigniorage from this loan money if the Bank of England alone could issue loans. Private banks would merely act as agents. (Ref: 1)

Ellen Brown (Ref: 2) describes a loan and seigniorage process. In colonial times the state of Pennsylvania issued loan notes to its farmers. The notes circulated as money until the state bank was repaid. As old loans were being redeemed new loans were being issued. The circulating loans notes served as 'money' for the colony.

Interest was charged on these Pennsylvania loans. But that created a problem. The notes in circulation equalled the loans issued. Where were the extra notes to pay the interest to come from?

The state bank solved this by giving extra notes to the state to spend into circulation. This was not inflationary because, like the principal, these notes also reverted to the state bank and were taken out of circulation. This state spending was its seigniorage on the circulating loans.

So the Pennsylvania state bank provides a model of how the Bank of England could work if it alone was the source of bank loans. It is as applicable to money circulating as numbers as it to loan notes issued by a bank. A state bank can capture seigniorage by spending into circulation an amount similar to the interest charges on its loans.

Stabilisation of Currency

A state bank can vary the rate of interest it charges to make it more or less attractive to borrow money. In this way it can usually encourage or discourage borrowing and so keep the amount of loan money circulating stable even in unstable times. That is what central bankers try to do indirectly by setting base rates.

This may not work when a boom or bust mentality takes hold. A state bank can then spend more or less money into circulation than needed to balance interest payments. In the great depression Keynes called for governments to build public infrastructure paying for it with money created out of nothing and spent into circulation.

> ***"The process by which banks create money is so simple that the mind is repelled." J K Galbraith - Economist***

Option 2: A 'Credit Creation Charge'

An alternative to nationalising credit creation in a state bank private banks could pay a 'Credit Creation Charge'.

A Building Society might take in deposits at 5% and lend at 7% making 2% to cover defaults and operating expenses. It might borrow additional money to lend from banks. Building societies are not allowed to lend money created simply out of a promise to repay it sometime in the future, but banks are.

Suppose a bank which lends £100,000 at 7% is paying 5% on deposits it holds of £60,000. It makes 2% by lending that out but 7% on the £40,000 it has created out of nothing. That works out at 4% on the whole £100,000 loan.

But where did this £60,000 in its deposit accounts come from? It too will have mostly come from loans further back in the banking system. And so will that money, and so on, and on....

In this way there is a bank 'merry-go-round'. For example six banks, each apparently with loans supported by 60% of deposits, have as a group only 4.6% deposits supporting their loans. The bigger this 'money-go-round' the less support there really is from deposits. They are all making money out of nothing in pyramid of loans.

What right has a bank to this 5% extra made on credit money created out of nothing? It is surely seigniorage. It represents the benefit the circulation of this money confers on the whole economy. It should therefore belong not to the banks but to all of us.

As explained for a state bank this seigniorage must be spent into circulation, otherwise insufficient money will circulate to pay interest on as well as redeem the loans. Borrowers are then forced to take on yet more loans simply to pay the interest on the earlier ones. The economy then sinks into a sea of debt owned by the banks.

There is therefore both a moral and a practical reason to introduce a 'Credit Creation Charge' to recover the seigniorage from the banks and spend it as public revenue. The burden of other taxes could then be correspondingly reduced.

> ***"Permit me to issue and control the money of a nation and I care not who makes its laws" M A Rothschild - Banker***