

# A MONETARY REFORM FOR THE INFORMATION AGE

by Paul Nollen

on Joseph Huber & James Robertson's *Creating New Money*

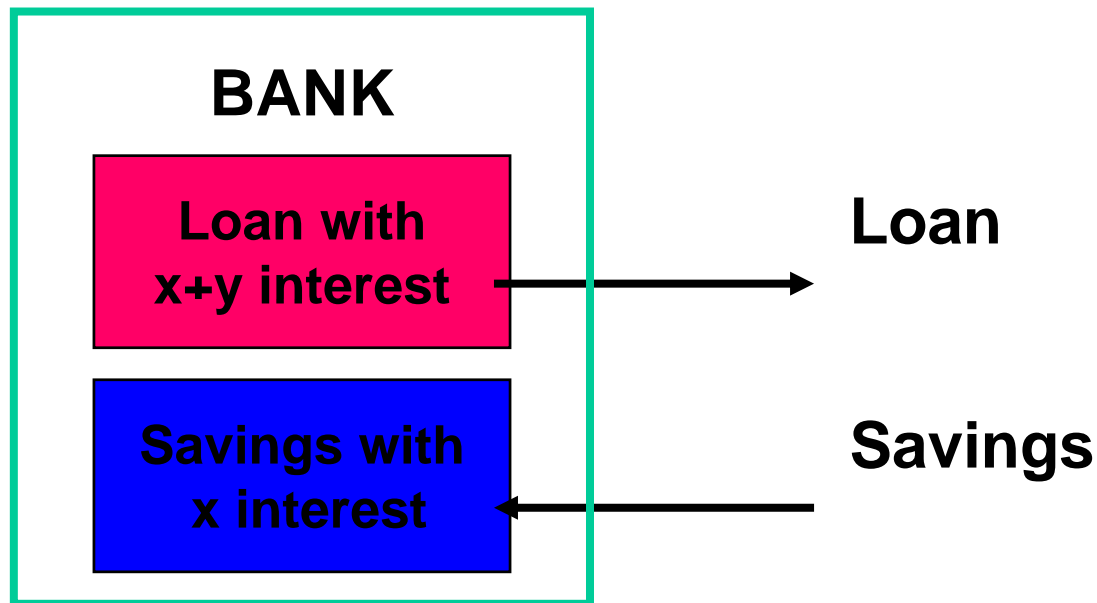
<http://www.jamesrobertson.com/book/creatingnewmoney.pdf>

Today's monetary and banking system is, in essence, still based on the 500 year old fractional reserve system suited to metal money. It still has to catch up with the new payment practices and the accelerating circulation of non-cash money based on modern information and telecommunication technology.

It is now opaque, inherently unsafe and unstable, almost impossible to control, and too expensive.

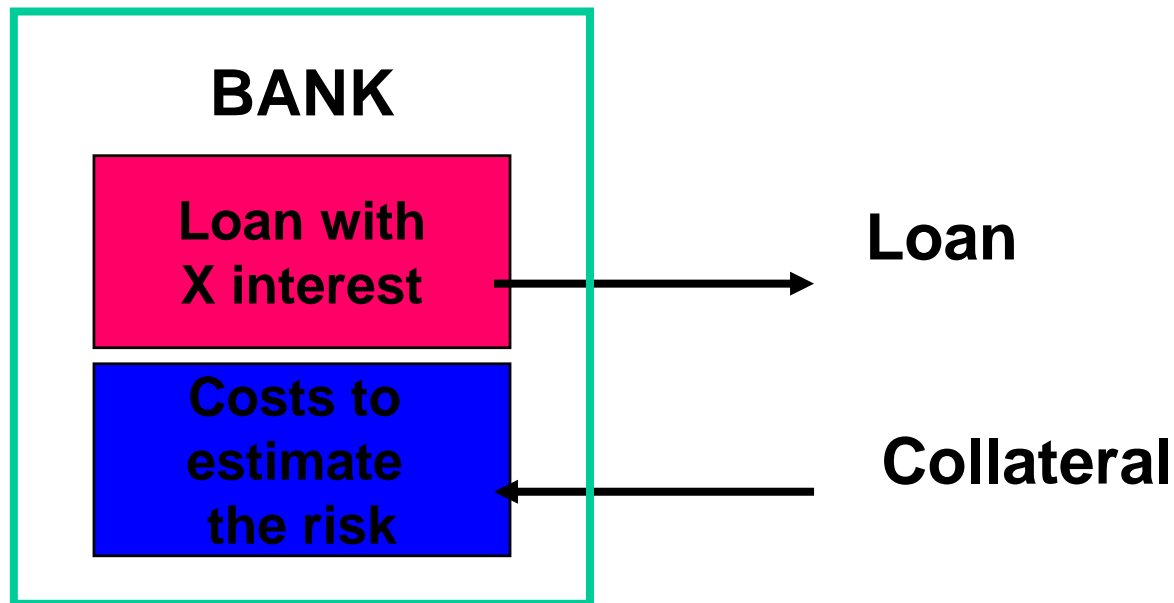
It is increasingly perceived as part of an unaccountable system of money and finance that needs reform at every level – local, national and international.

# How do we think a bank works



The banks are granting loans from savings and charge a higher interest than they are paying. The difference is the brut profit of the bank for granting the loan.

# How a bank really works



The bank “converts” the collateral in money (T. Greco jr). This “credit money”, strictly speaking even not a “loan”, must be paid back with interest. The total amount of Money is increased with the loan.

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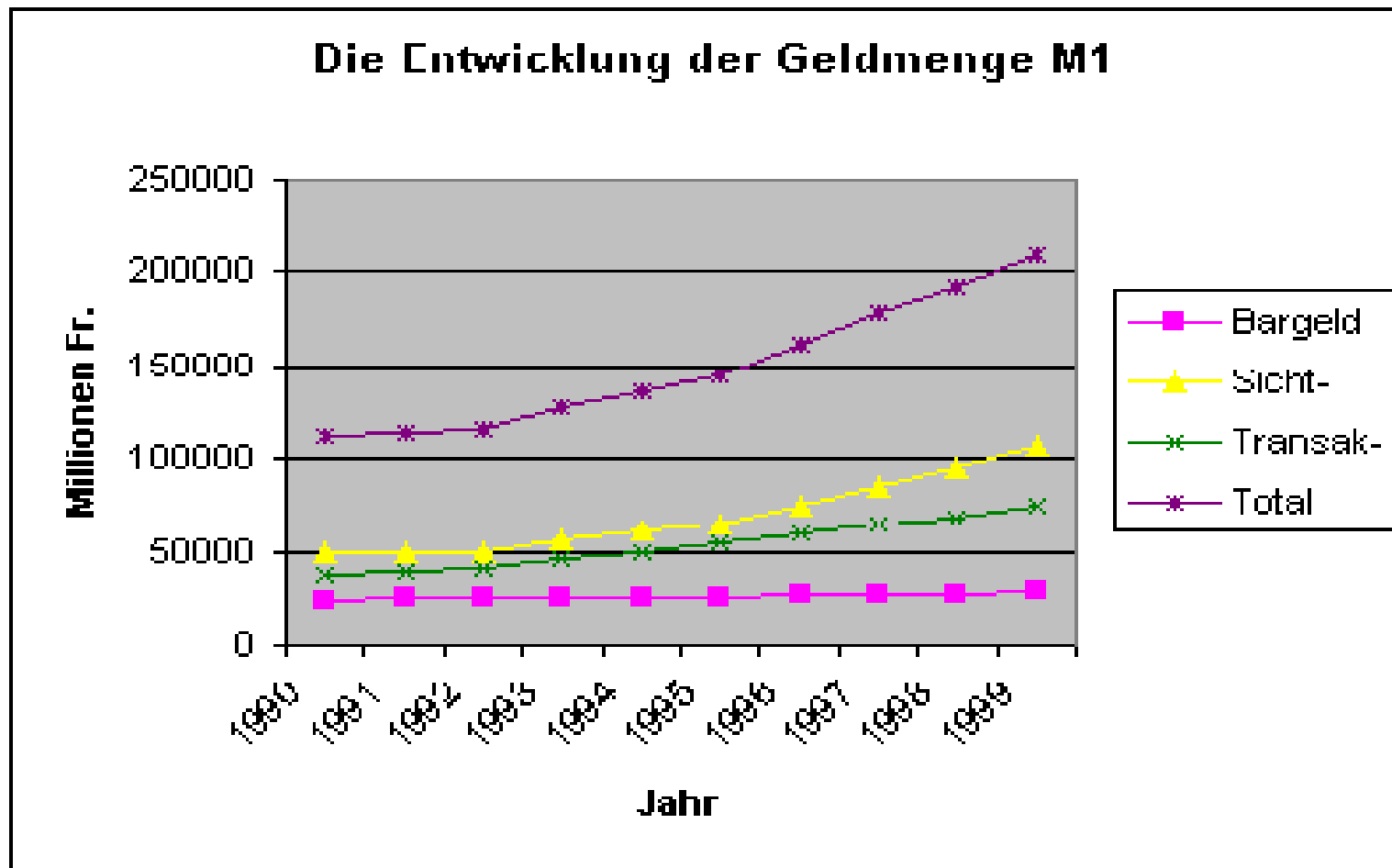
Allowing banks to create new money out of nothing enables them to cream off a special profit. They lend the money to their customers at the full lending rate, without having to pay any deposit rate on it themselves.

So their profit on this part of their business is not, say, 9% credit-interest less 4% deposit-interest = 5% normal profit;

it is 9% credit-interest less 0% deposit-interest = 9% profit = 5% normal profit plus 4% additional special profit.

This additional special profit is hidden from bank customers and the public, partly because most people do not know how the system works, and partly because bank balance sheets do not show that some of their loan funding comes from money the banks have created for the purpose and some from already existing money which they have had to borrow at interest.

# Growth of M1 in Switzerland



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1. Central banks should create the amount of new non-cash money (aswell as cash) they decide is needed to increase the money supply, by crediting it to their governments as public revenue. Governments should then put it into circulation by spending it.
2. It should become infeasible and be made illegal for anyone else to create new money denominated in an official currency. Commercial banks will thus be excluded from creating new credit as they do now, and be limited to credit-broking as financial intermediaries.

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It will be for central banks to decide at regular intervals how much new money to issue. They will make their decisions in accordance with monetary policy objectives that have previously been laid down and published, and they will be accountable for their performance.

But they will have a high degree of independence from government, giving governments no power to intervene in decisions about how much new money to create.

Scaremongers will raise the spectre of inflation.

But we show that, among other benefits, seigniorage reform can be expected to provide more effective safeguards against the risk of inflation than exist today, when commercial banks print almost all the new money.

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**Four comparatively straightforward changes will be needed, as follows.**

1. Sight deposits denominated in the official currency will be recognised as legal tender, along with cash.
2. The total amount of non-cash money existing in all current accounts (including those of bank customers, banks, and government), together with the total amount of cash in everyone's possession, will be recognised as constituting the total stock of official money or legal tender immediately available for spending.

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3. Customers' current accounts will be taken off the banks' balance sheets, and the banks' will manage them separately from their own money (which is not what they do today). As a result, a clear distinction will be introduced between means-of-payment money ("plain money") in current accounts, and store-of-value money ("capital") in savings accounts. In practice this will mean that, except when a central bank is creating new money as public revenue, payments into current accounts will always have to be matched by payments out of other current accounts, or paid in as cash.
4. Finally, if any person or organisation other than a central bank fails to observe that distinction and prints new non-cash legal tender into a current account, they will be guilty of counterfeiting or forgery – just as they would be if they manufactured unauthorised banknotes or coins.

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Proposals for monetary reform have often advocated 100% banking (in place of fractional reserve banking) as a way to prevent banks creating new money.

Failure to get those proposals adopted has been at least partly due to the difficulty of implementing them, reflecting as they did an out-of-date understanding of the changed nature of money and the process of creating it.

The plain money proposal will achieve the same aim as 100% banking would have done, but in a simpler way – easier to understand and implement, and more fully reflecting the nature of money in the Information Age.

## Among possible advantages are:

- greater equity and social justice
- eliminating inflationary tendencies in the economy
- creating greater financial and economic stability by pre-emptively avoiding 'irrational exuberance' during the peaks as well as withdrawal of credit and money during the troughs of business cycles
- improving the safety and stability of domestic banking institutions
- removing distortions caused by channelling 95% of new money into the investment and spending priorities of banks and their customers
- reducing monetary pressures and constraints arising from the creation of new money by commercial banks as interest-bearing debt, that encourage environmentally unsustainable development, and
- a monetary and banking system that is transparent and open to public and political understanding of how it works.

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So let central banks directly control the quantity of the entire stock of money, let the public purse enjoy full seigniorage, and let the banks continue to develop profit-efficient businesses providing loans on the basis of saved income.

The monetary system will be transparent and easy to understand.

Money supply will be under effective control.

Money will be safe. The purchasing power and foreign exchange value of money will be more stable than today.

Last but not least, money will be cheaper to obtain for private households, businesses and governments alike.

# TANSTAAFL – TISATAAFL WIGI en WOTGI

In a talk in London in 1999 on land value taxation Professor Mason Gaffney of the University of California referred to the reaction of some right-wing libertarian economists to calls for economic justice.

Their response is **TANSTAAFL** (there ain't no such thing as a free lunch). As he pointed out, they are wrong.

The truth is **TISATAAFL** (there is such a thing as a free lunch); and the important questions are **WIGI** (who is getting it?) and **WOTGI** (who ought to get it?). Where the issuing of new money is concerned, the answers are: the commercial banks are now getting the free lunch; in future all citizens ought to get their share of it – as public revenue.

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The EU budget was € 116 bn in 2009, including the euro-opt-out countries. The increase in the stock of money within the Euro area, not including the opt-out countries, was of late between € 134–531 bn (ECB Monthly Bulletins, Table 2.4).

So the EU budget could be more than fully financed by EU seigniorage. On the basis of those figures, national governments of the Eurozone states would be able to stop paying contributions to the EU budget altogether, and – on top of that – actually receive from Brussels more than the amounts they were previously having to pay.

## **The democratic state is being eroded in the face of global markets.**

Issuing new money in the form of public expenditure enables the public purse to go further – whether for public transport, environment or regeneration.

Restoring democratic control over how new money is issued is an important step towards a global economy in which unpayable debts are reduced and resources can be freed up for sustainable development.

## How, then, should governments spend the new money into circulation?

- One suggestion is that the money should be used to reduce and eventually pay off the National Debt altogether, thus reducing and eventually eliminating the need for taxes or further borrowing to pay interest on it
- others have suggested that the new money should be put into circulation as a national dividend or citizen's income
- A third suggestion is that government should put the new money into circulation in the form of interest-free loans, e.g. to local government for infrastructure development.

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