THE CHICAGO PLAN REVISITED AND POSITIVE MONEY:

THE MAIN DIFFERENCES

ANDREW JACKSON, HEAD OF RESEARCH, POSITIVE MONEY

ANDREW.JACKSON@POSITIVEMONEY.ORG 0207 253 3235

The Benes-Kumhof Chicago Plan and the Positive Money proposal are both monetary reforms based on a proposal initially put forward by Frederick Soddy in the 1920s, and then subsequently by Irving Fisher and Henry Simons in the aftermath of the Great Depression. The aims of these reforms are the same: namely to prevent banks from creating money in the process of making loans, while returning the power to create money to the state.

However, while the aims are the same, the methods by which the aims are achieved vary considerably. This document outlines the major differences between the Benes-Kumhof Chicago Plan and the Positive Money Proposals. We assume the reader is familiar with at least one of the proposals and has a good understanding of the current monetary system. (This has not been written for the lay reader).

Benes-Kumhof	Positive Money
Reserves are increased to back bank deposits 100%	Sight Deposits on banks balance sheets are moved to the central bank. Time deposits become illiquid, non-transferable liabilities of commercial banks.
Parallel system of central bank reserves (interbank money) and commercial bank money (bank deposits used by the public) to make payments.	All payments by banks and members of the public are made using one integrated quantity of central bank money. Payments between members of the public are made using central bank money rather than commercial bank deposits.

Key Features

Benes-Kumhof	Positive Money
C1. Current (checking) accounts and all other customer deposits remain liabilities of commercial banks	PM1. Current (checking) accounts become customer records administered by, but not liabilities of, commercial banks. They refer to ownership of central bank money held at the central bank. Depending on the accounting regime chosen when the reforms are implemented, central bank money is either: • Electronic tokens, representing state-issued money, held in a database by the Bank of England, or • Liabilities/equity of the central bank, held against central bank holdings of (preferably, irredeemable zero coupon) government securities or against a purely nominal balancing asset such as "the productive capacity of the realm".
C2. Banks carry central bank reserve assets to the value of at least 100% of customer deposit liabilities.	PM2. Customers' money is held in an aggregated account (the "Customer Funds Account") at the central bank. This account is administered by the commercial bank, but the central bank money that it contains is the property of the commercial bank's respective current (checking) or transaction account holders.
C3. Options to prevent the creation of near-monies by the investment trust sector: • Liabilities of investment trust would not be backed by Government guarantee. • Legal requirement that all short term lending be financed exclusively via equity instruments. • Removal of tax advantages (or creation of tax disadvantages) of debt to equity. • Imposition of penalties for institutions issuing near-monies. • Outlaw the creation of near monies. • There will be a statutory prohibition on short-term lending other than through non-bank intermediaries, such as investment trusts, to safeguard against the emergence of near-monies.	PM3. Investment accounts will be illiquid, with fixed maturity dates or notice periods, and will not be back by government guarantee (or the Financial Services Compensation Scheme). These accounts will be non-transferable, preventing them from being used to make payments. In addition, there will be a statutory prohibition on banks' creating sight deposits to make payments to third parties from their own funds on a routine basis on behalf and to the order of their customers and thereby creating demand deposits acting as near monies. Banks will be required to be able to meet the totality of their demand liabilities at all times.

C4. Banks retain the ability to finance longer-term lending by debt (deposit liabilities) for non-monetary liabilities.	PM4. Banks can finance lending by debt, but these liabilities are not money and as such cannot be used in transactions. Banks can lend money they own (i.e. retained earnings) by transfer to the borrowers' funds from their own operational funds.
C7. "management of money growth should ideally be entrusted to a fourth power of government, with a constitutional independence similar to that of the Supreme Court. This would insulate the issuance of money not only from government pressures, but also from pressures that come from private financial interests."	PM7. Management of monetary growth is entrusted to a Monetary Creation Committee independent of government, with authority to instruct the Bank of England. The MCC must be politically independent, neutral, free of conflicts of interest, and sheltered from lobbyists for the banking sector and other industries.
C8. Customer payments are settled between banks by balancing transfers from banks' own holdings of reserve assets.	PM8. Customer payments are settled directly by transfer of customers' own central bank funds from payer to payee accounts. In practice, the banks use the existing payments systems to manage customer transactions through customer records held locally, and make net settlements as appropriate between the aggregated customers' funds held at the central bank.

Operations

Benes-Kumhof	Positive Money
C9. New loans are issued primarily by non-banking investment trusts which are subscribed to using money paid across by investors from their current accounts.	PM9. New loans are issued primarily by banks from funds which are subscribed to using money paid across by investors from their Transaction Accounts, or from the bank's retained earnings (i.e. money held in the bank's own account at the central bank). Banks can also establish investment funds (with any money in them again being held at the central bank).
C10. In addition to C9, fund for loans may be acquired by banks borrowing directly from the Treasury. This credit should only be used to lend to business that contribute to GDP. If funded in this way, bank lending increases the money supply.	PM10. In addition to C9, if the central bank deems that businesses in the real economy are struggling due to a lack of access to credit, the Bank of England can lend to the banks to on lend into the economy, subject to the condition that this money is lent for business that contribute to GDP. If funded in this way, bank lending increases the money supply.

C11. New money is created by Treasury lending of reserves to commercial banks or by the government spending money into circulation.	PM11. New money is created by the central bank, under instruction from the Monetary Creation Committee, incrementing the Treasury account at the central bank under the same accounting principles as P1. above. This money enters circulation through government spending.

Transition

Benes-Kumhof	Positive Money
C12. At the outset of transition, Treasury lends reserve assets to banks to at least match the value of banks' customer deposit liabilities. These reserves are accounted for as part of the equity of government, balanced by the government's "Treasury credit" at commercial banks.	PM12. At the outset of transition, commercial banks' demand liabilities to their customers are converted into a long-term liability to the central bank. The central bank then creates new central bank money to replace the demand liabilities that customers held. Current account customers now have ownership of central bank money, instead of holding a liability of a commercial bank.
C13. In the course of the transition period, Treasury pays out to householders and manufacturers a citizens' dividend, which are required to be used by recipients to pay down their bank loans. (A consequence of the dividend payment, not explored in the Plan, will be the reduction or elimination of government equity, leaving some or all of the banks' reserve asset holdings unmatched by any corresponding liability - a status accorded only to reserve holdings of gold bullion under international accounting standards for the System of National Accounts.)	PM13. Banks' customer loan portfolios remain at all times assets of the banks themselves. In the course of the transition period, repayment by borrowers of outstanding principal on the loans which predate the transition, is by transfer of money from the borrowers' Transaction Accounts held at the central bank to the banks' operational funds held at the central bank. A portion of these repayments will finance the repayment by the banks of their transitional debt liabilities to government. Interest revenue from these loans remains the property of the banks. Repayment of loans incurred post implementation would be from the borrowers' funds to the banks' investment funds from which the loans were drawn, as in P9.

Benes-Kumhof	Positive Money
C14. In view of their reduced risk-weighted asset holdings following early redemption of banks' customer loans portfolios financed by the citizens' credit, banks are required to reduce their equity via a dividend payout to shareholders which is then taxed back in full, with the tax revenue being deposited back in the banks, so increasing Treasury credit. (The Plan does not consider where the banks would get the reserves needed to back the increased deposits following the dividend payment and before the tax clawback.)	PM14. There is no change to banks' assets so no adjustment to their equity is necessary.

Implications

Benes-Kumhof	Positive Money
C15. Since all customer deposits are 100% backed with liquid reserves, bank runs are impossible so deposit guarantee schemes are unnecessary.	PM15. Since all current account balances are actually liquid central bank money, bank runs are impossible so deposit guarantee schemes are unnecessary. Investment accounts (the old savings accounts) remain bank liabilities and so are exposed to liquidity risk, as are accounts in the investment vehicles of other institutions, but bank liquidity risk poses no greater systemic risk than other institutions' liquidity risk.
C16. "Large scale loan defaults have no implications whatsoever for the money supply and the safety of the payments system, which remains fully insulated from the credit system"	PM16. As for the Chicago Plan

Other issues

Benes-Kumhof	Positive Money
C17. Reserves have to exceed deposits in order that banks are able to meet their own payments to staff etc. Therefore the quantity of reserves may be higher than the quantity of deposits.	PM17. All payments between banks and nonbanks proceed through transfers of pre-existing funds at the central bank with no implications for money supply as a whole.
C18. The treatment of overdrafts is not covered. With short-term lending by banks prohibited, payments which would overdraw accounts must be refused.	PM18. Banks are permitted to lend from their own accounts and from the unlent residue of their investment funds and so may make provision for short-term loans to cover customer overdrafts with no implications for the money supply.

DIFFERENCES BETWEEN **NEED** ACT AND THE POSITIVE MONEY PROPOSALS.

The NEED Act has the following differences from the PM proposals:

- The NEED Act implements an interest rate cap of 8% per annum, and limiting total interest charged over the lifetime of a loan to the amount originally lent. The PM proposals do not cap interest in any way.
- Under the NEED Act, all deposits (demand and time) are converted into sovereign money ("US money"). Under PM proposals, only demand deposits are converted into sovereign money (state-issued currency) and time deposits remain as liabilities of the banks to their Investment Account holder customers.
- The NEED Act prohibits government borrowing (unless specifically permitted under another Act of Congress) and requires government bonds to be retired as they mature. The PM proposals do not prohibit government borrowing, do not change the current mechanisms for government borrowing, and expressly recommend that government debt should only be reduced once personal and household debt has been significantly reduced (because household debt is higher than government debt and is subject to higher average rates of interest).
- The NEED Act suggests a number of spending programmes through which newly created money can be distributed. The PM proposals only states that newly created money will be added to government accounts. How it is distributed depends on the choice of the government of the day, but may be a mix of spending increases, tax cuts, or direct payments to citizens.
- The PM proposals allow for the Bank of England to create money which will be lent to banks specifically for on-lending to the real economy. This is to ensure that the supply of credit to the real economy is not affected during the transition or if banks are reluctant to lend to the real economy. The NEED Act is not explicit about the possibility of the central bank creating money to on-lend to the real economy, but does not seem to rule it out.

Positive Money

205 Davina House
137-149 Goswell Road
London
EC1V 7ET

Tel: +44 (0)207 253 3235

info@positivemoney.org

www.positivemoney.org

Positive Money is a not-for-profit company limited by guarantee, registered in England and Wales.

Company number 07253015