



HM TREASURY

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Information Rights Unit

Simon: of the Elder family

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Ref: 9/

23 April 2009

Dear Simon

Freedom of Information Act 2000: Money Creation

Thank you for your enquiry dated 18 April requesting information under the Freedom of Information Act 2000. I am treating this as a fresh request.

2. You asked for information covering –

- *what is the mechanism by which electronic money comes into being*
- *how is electronic money released into circulation*
- *what precisely constitutes the demand for the amount of money (including electronic and bank money) that is created*
- *who authorises the release of electronic money into circulation.*

3. You say that I restricted the scope of your previous request against your intent. By the same token, I have assumed it would not be helpful to interpret your new request in a narrow sense as referring to e-money under the EU e-money Directive that was implemented in the UK in 2002; but please tell me if this assumption is wrong-headed.

4. My previous letter explained the reason I treated your request as I did: the only relevant information we hold is in connection with issue of currency and with monetary policy; we do not hold information about the theoretical basis of money. Turning to your new request, the same difficulty applies: following a search of our records, I confirm that we do not hold relevant information.

5. In general, the Bank of England is better placed to address enquiries about the mechanics of the monetary system, because of their executive responsibility for monetary policy and financial stability. There is a wealth of relevant material on their website.

6. To be helpful – and on the assumption that what you are seeking from us is an acknowledgement that money supply is increased by new borrowing - the closest I can offer in terms of information we hold, is in a speech made by Paul Tucker from



the Bank of England and included in the Bank's Quarterly bulletin for 2008 Q1. Below is a link to the speech and the crucial excerpt -

<http://www.bankofengland.co.uk/publications/quarterlybulletin/qb080110.pdf>

Subject only but crucially to confidence in their soundness, banks extend credit by simply increasing the borrowing customer's current account, which can be paid away to wherever the borrower wants by the bank 'writing a cheque on itself'. That is, banks extend credit by creating money. This 'money creation' process is constrained: by their need to manage the liquidity risk — from the withdrawal of deposits and the draw-down of back-up lines — to which it exposes them.

7. Against that background, government monetary policy is aimed at ensuring that money remains sound. It seeks to achieve this, partly by regulation of banking activity, but mainly by using interest rates to indirectly control inflation. Inflation arises when too much money is chasing too few goods and services – which is a useful reminder that the value of money reflects the confidence that it can be exchanged, at relatively stable values, for goods and services. Changes in the money supply do not generally take place in the abstract, but are a reflection of the vigour of the economy in terms of the production of valuable goods and services: people take out loans in order to purchase goods and services; they are granted loans on the basis of their ability to repay, frequently from hiring out their valuable labour.

8. I hope this commentary and these links are helpful. If you have any queries about this letter, please contact me. It will be helpful to us if you remember to quote the reference number above in any future communications.



Paul Morran
Information Rights Unit

Your right to complain under the Freedom of Information Act 2000

If you are not happy with this reply, you may request a review by writing to HM Treasury, Information Rights Unit, 2/S2, 1 Horse Guards Road, London SW1A 2HQ. Email foi.responses@hm-treasury.gov.uk

Any review request must be made within 2 months of the date of this letter. It would assist our review if you set out which aspects of the reply concern you and why you are dissatisfied.

If you are not content with the outcome your complaint, you may apply directly to the Information Commissioner for a decision. Generally, the ICO cannot make a decision unless you have exhausted the complaints procedure provided by the Treasury. The Information Commissioner can be contacted at: The Information Commissioner's Office, Wycliffe House, Water Lane, Wilmslow, Cheshire SK9 5AF.