



HM TREASURY

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www.hm-treasury.gov.uk
FOI.responses@hm-treasury.gsi.gov.uk

Ref: 9/769

Re: Freedom of Information Act 2000: Money

Thank you for your enquiries that we received on 20 October and 9 November, headed 'Fractional Reserve Lending'. These were following our FOI response of 5 October.

2. You ask us to revisit the answers we gave. We have not treated this as an internal review, however, if you remain dissatisfied in the wake of this letter, you can ask us to do so in line with the note at the end of the letter.

3. Your most recent email challenges us to recognise that you have asked valid questions. I am sorry if we have given the impression that we did not think they were valid. What we meant to indicate was that, although you cite the Freedom of Information Act, these are not valid requests for information under that Act; that is a different point. Your original request was in the form – '*my assumption is .. is this correct?*' Our problem with such an enquiry is that it requires us to interpret your description and make a judgement about whether or not it tallies with the information we have; that goes beyond the requirements of the Freedom of Information Act. Your new request is in a similar form.

4. However, it may be helpful if I explain outside the Act, that UK banking supervision follows the international model developed by the Basel Committee on Banking Supervision¹. Under the Basel system, banks have to hold capital equal to 8% of their risk-weighted assets. Some assets carry a risk weighting of less than 100% (e.g. government bonds) and therefore the overall capital requirement can be less than 8% of total assets.

5. This 'creation' of money has social utility as it enables investment. For example, if a farmer who grows one tonne of grain a year and saves £1 a year wants to buy a tractor for £20, he would need to save for 20 years. But if the tractor would enable him to grow 10 tonnes of grain a year and save £10 a year, with fractional reserve banking, he can borrow £20 to buy a tractor and repay the money over 2 years. After 20 years he has grown 180 tonnes more grain and has saved £180 more (all this excludes debt and savings interest).

6. So it can be seen that fractional reserve banking has great benefit. But it does create risk and these risks need to be carefully managed.

7. The Government's policy is to abide by the internationally agreed Basel agreements, and these have also been adopted as Directives by the European Union. However, the Financial Services

¹ <http://www.bis.org/bcbs/index.htm>



Authority retains the authority to impose greater capital requirements on banks it deems to carry more risks.

8. Both domestically and internationally (within the EU and in the Basel group of countries), the system described above is being re-examined, in terms of the amount and type of capital banks have to hold, and the risk weightings of the assets they hold. The G20 group of countries, under the UK Presidency for 2009, has also agreed to implement a leverage ratio. This will place an overall cap on the amount of money a bank can create on the base of its assets. In addition to this, the FSA has introduced new rules on the amount of liquid assets a bank must hold to meet depositor and investor demand and new rules on liquidity are being discussed internationally.

9. You also complained that we did not provide the information where we did recognise a valid FOI request - about the percentage of taxes that go to service public debt. Our letter referred you to Budget documentation, which does indeed provide such information. Section 21 of the Freedom of Information Act explicitly lays down that information already published is exempt, because it is otherwise accessible to you.

10. I hope the above is 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.

