How California Can Create Its Own Credit: OWN A BANK!

Ellen Hodgson Brown, J.D.

December 9, 2010, 6:30-8:00 PM
Marin County Civic Center, Room 329
3501 Civic Center Drive, San Rafael, CA

THE GOLDEN STATE GOES BROKE

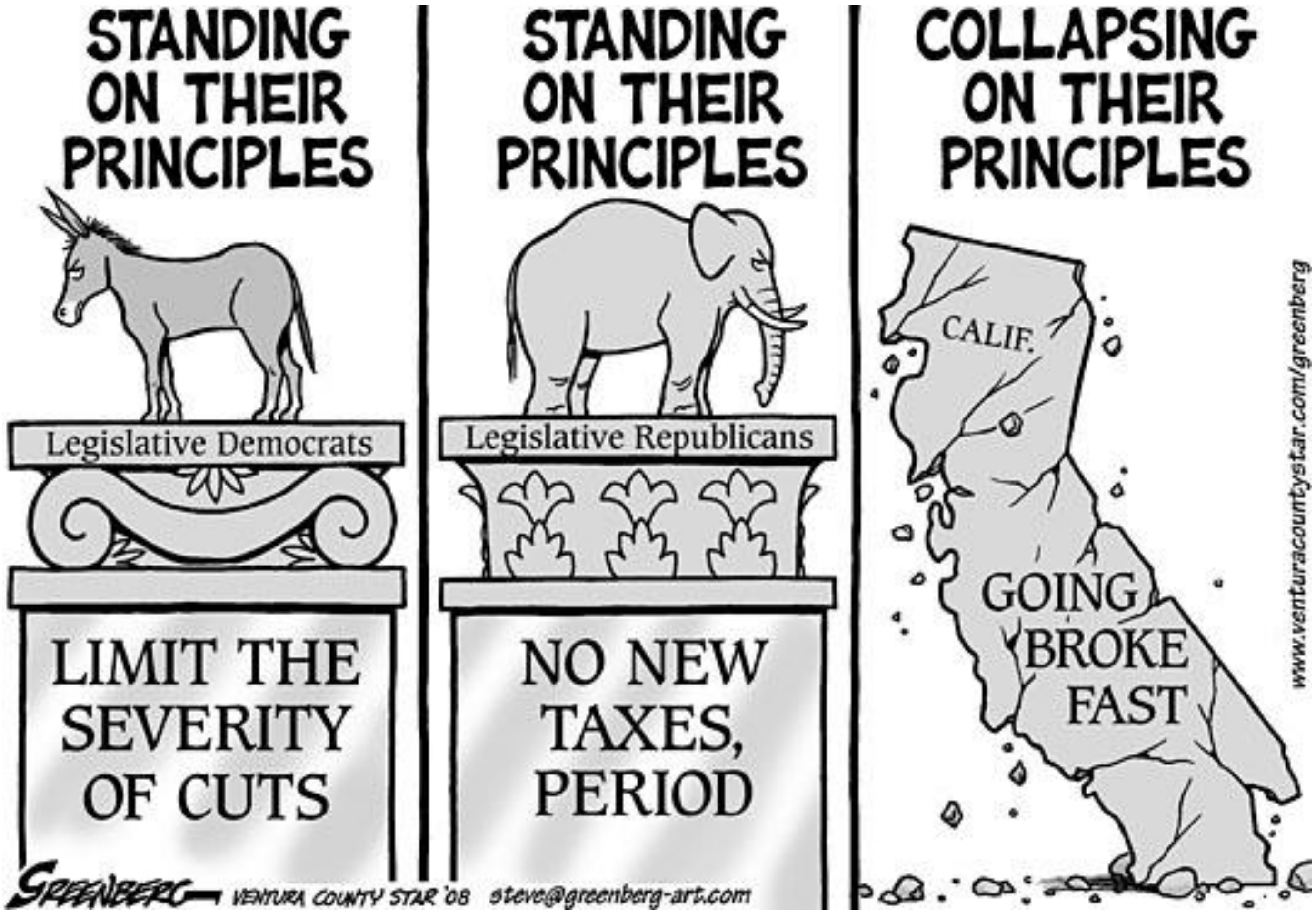
Once the world's 8th largest economy – visionary, progressive – leading producer in agriculture, industry, technology, entertainment . . .

California is now a modern-day Hooverville, vying with Illinois as the most insolvent state.

Cities have joined the panhandlers. Rainy day funds are depleted, with no funds for emergencies.

On Dec 7, Gov-elect Jerry Brown announced that the deficit had ballooned to **$28 billion**.

The choices being debated are all unacceptable.



Everything is up for sale. That could work this year, but what do we do next year?

Tuition hikes are making "public" universities unaffordable.

- UC BERKELEY: Tuition is now $12K/year.
- Total tab: $34K/yr x 4 = $136K + grad school = $200K.
- $200K @ 7% for 30 years = $1330/mo. – the equivalent of a mortgage!
- And it's not dischargeable in bankruptcy.

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MOVE BACK HOME?!... KIDS TODAY ARE SO LAZY AND IRRESPONSIBLE! YOUR MOTHER AND I STARTED OUT WITH NOTHING!...
FIVE-FIGURE STUDENT LOAN DEBT
20 AND 30 SOME-THINGS
TRUST ME, I WOULD'VE LOVED STARTING OUT WITH NOTHING!...

In the 1960s, tuition at Berkeley was FREE.
Or so I remembered it . . .
Prof. Gray Brechin, UC Berkeley Dept of Geography, confirms. His commencement speech, 2009:

"When I tell students that when I came to Berkeley in 1967, there was virtually no tuition, you can hear their jaws hit the floor. I took it for granted then; no one told me that I was the unwitting beneficiary of New Deal idealism . . .

He described what was done in the last Great Depression, something we can do again today . . .

"Many of you probably wonder what I do in my office surrounded with all that Roosevelt stuff. I'm working on an archaeological dig of a lost civilization that our parents and grandparents built in about seven years of far harder times than our own. . .

“[An] alternative universe is all around us, the enormous legacy of public works created by New Deal agencies in only a few brief years. . . By putting millions of Americans to work doing everything from laying sewers and running WPA health clinics to painting murals and planting forests, these public works began to lift the economy out of the last Great Depression.

“[They] built over eleven thousand schools and improved tens of thousands more. . .

“In 1960, aging New Dealers like **Governor Pat Brown . . .** put in place California’s Master Plan for Higher Education that promised free tuition regardless of income.”

Governor-elect Jerry Brown grew up with this vision. We can inspire him with it again.

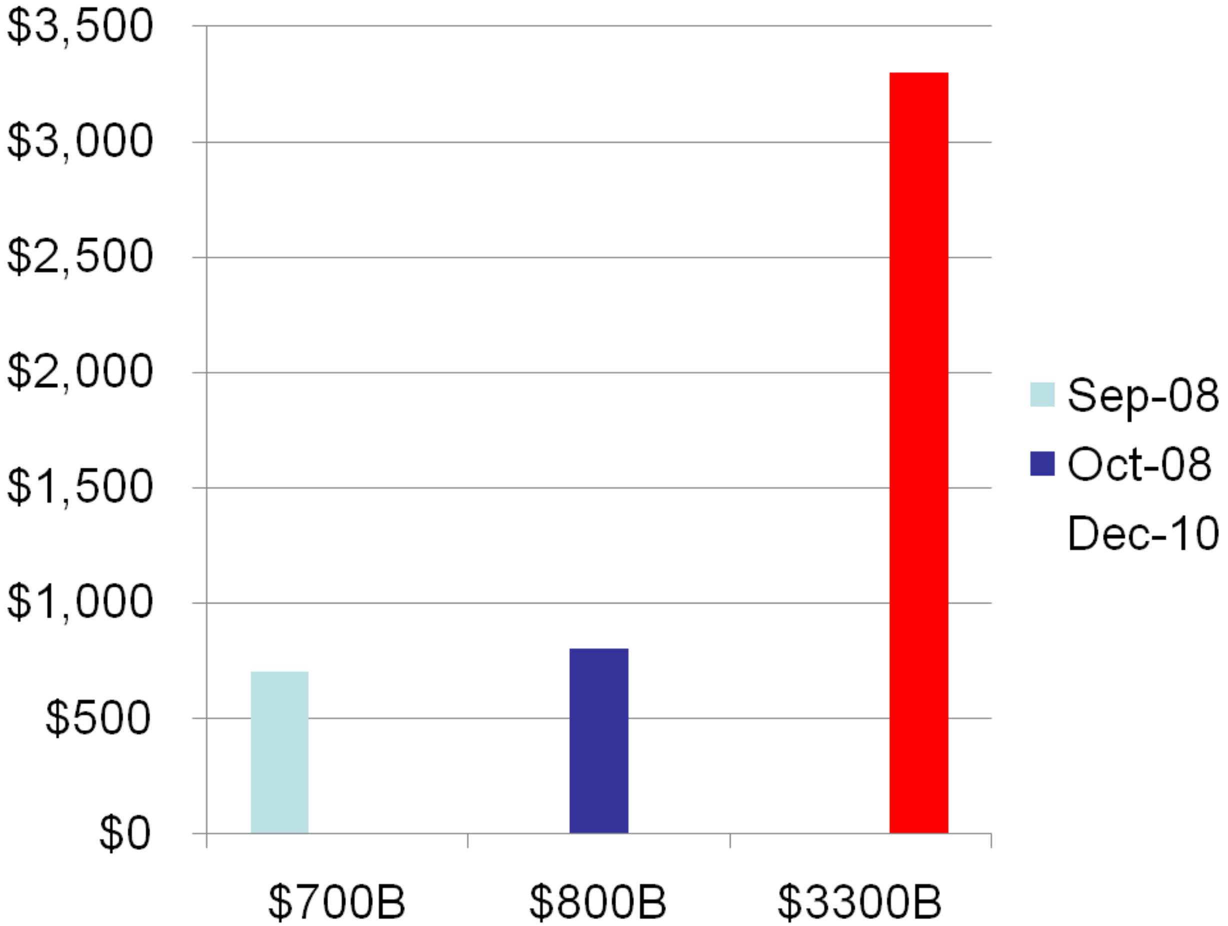
- We've still got the manpower, the resources, the expertise, the imagination.
- All we're lacking is the MONEY. Where will we get it?
- In the same place the Fed got the money to bail out Wall Street . . .

WHERE'S OUR BAILOUT?

While state economies are floundering, Wall Street is flourishing.

The banks that perpetrated the crisis are being lavished with bailout money, but it isn't making it to Main Street.

Somehow, the government and the Fed managed to turn $800 billion into $3.3 trillion (or more).



Where did all this money come from?

Congress too wanted to know . . .

House Speaker Nancy Pelosi, June 2009:

"Many of us were, shall we say, if not surprised, taken aback when the Fed had $80 billion to invest -- to put into AIG just out of the blue. All of a sudden we wake up one morning and AIG has received $80 billion from the Fed. So of course we're saying, Where's this money come from?

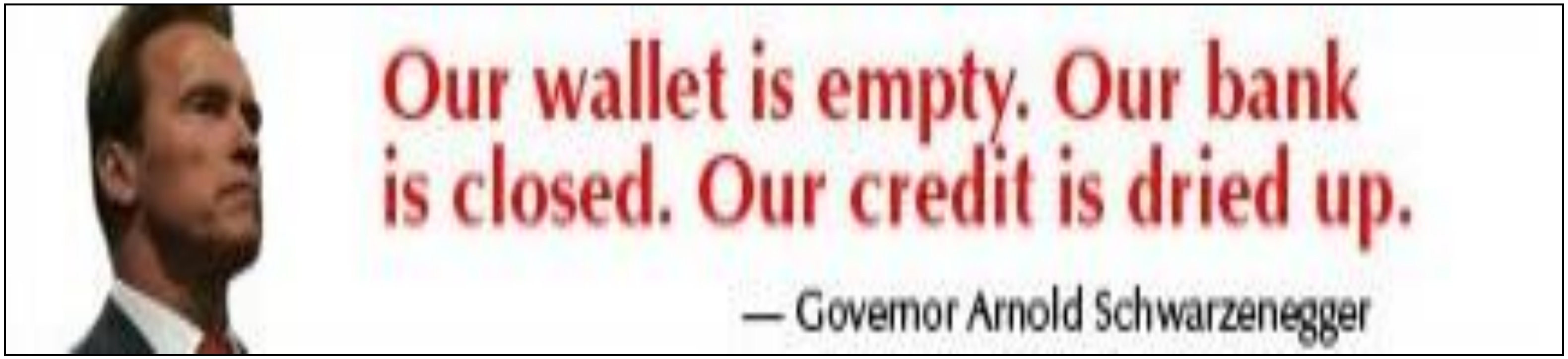
'Oh, we have it. And not only that, we have more.'"

The secret was revealed by Art Rolnick,
former Chief Economist, Minneapolis Fed:

“We make money the old-fashioned way: we print it.”

But what about the states?

In 2009, Governor Schwarzenegger declared --

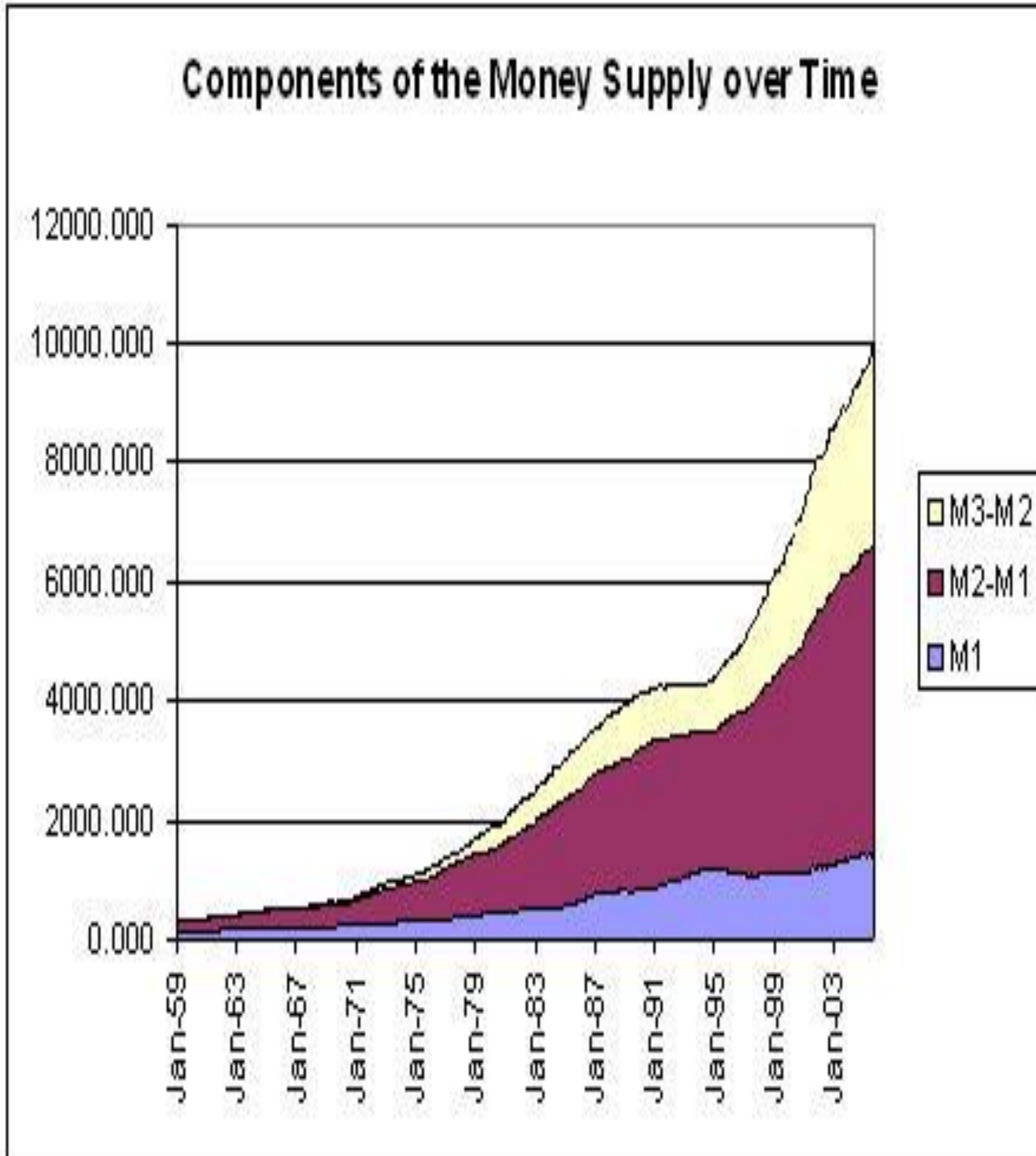


"I understand that these cuts are very painful and they affect real lives. This is the harsh reality and the reality that we face. Sacramento is not Washington – *we cannot print our own money. We can only spend what we have*."

That's true, UNLESS we own a bank . . .

HOW BANKS CREATE MONEY – AND CALIFORNIA COULD TOO, IF IT OWNED A BANK

- States aren't allowed to print money,
- but they're allowed to own banks,
- and banks are allowed to create money on their books.



So said **Wright Patman**, Chairman of the House Banking and Currency Committee in the 1960s:

> “When the Federal Reserve writes a check for a government bond *it does exactly what any bank does, it creates money, it created money purely and simply by writing a check*.”

Treasury Secretary Robert B. Anderson said in 1959:

Photo #: NH 77324-KN Robert B. Anderson, Secretary of the Navy 1953-54

“[W]hen a bank makes a loan, it simply adds to the borrower’s deposit account in the bank by the amount of the loan. *The money is not taken from anyone else’s deposit*; *it was not previously paid in to the bank by anyone. It’s new money, created by the bank for the use of the borrower*.”

As explained by the Chicago Federal Reserve in “Modern Money Mechanics”:

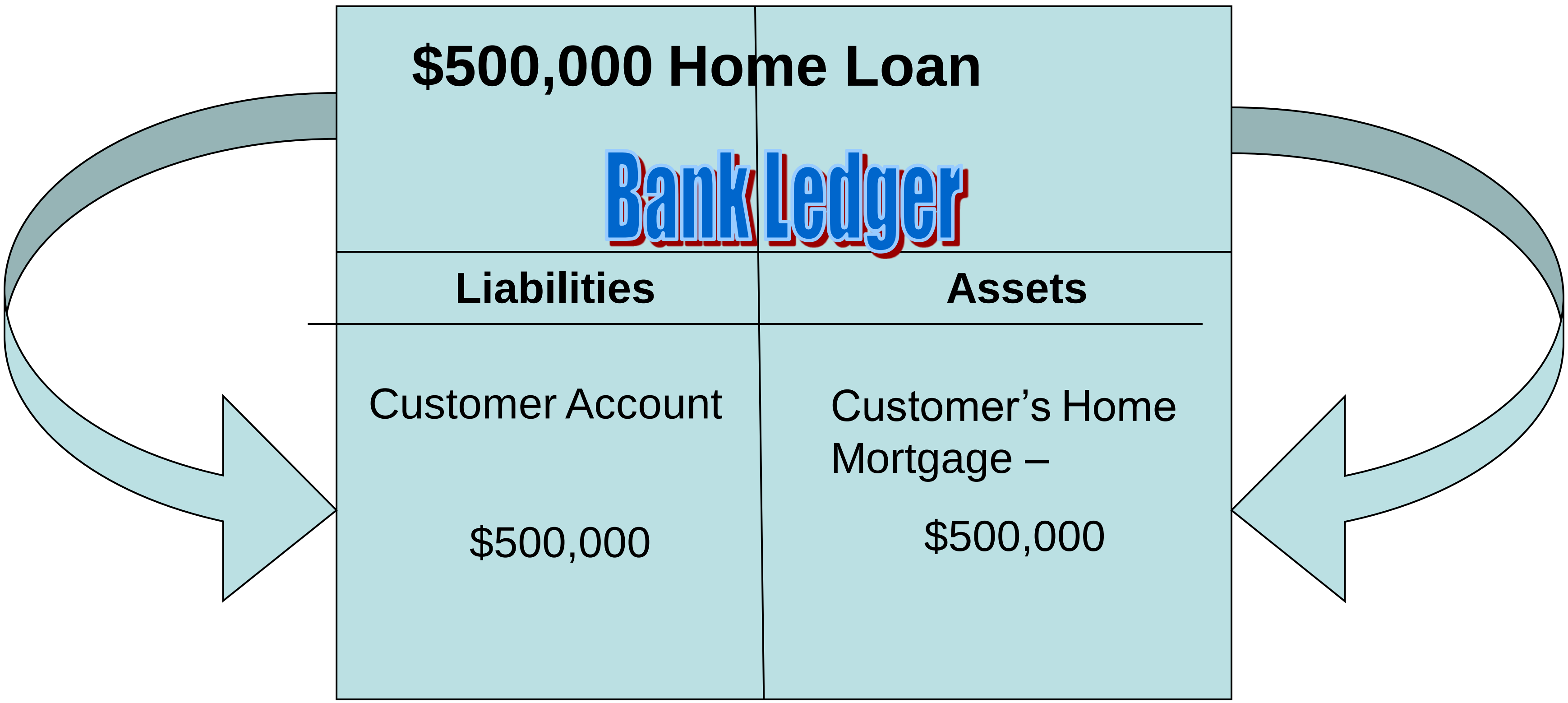
- “The actual process of money creation takes place primarily in banks.” [p3]

- “[Banks] do not really pay out loans from the money they receive as deposits. If they did this, no additional money would be created.

- *What they do when they make loans is to accept promissory notes in exchange for credits to the borrowers’ transaction accounts*.

- Loans (assets) and deposits (liabilities) both rise [by the same amount].” [p6]

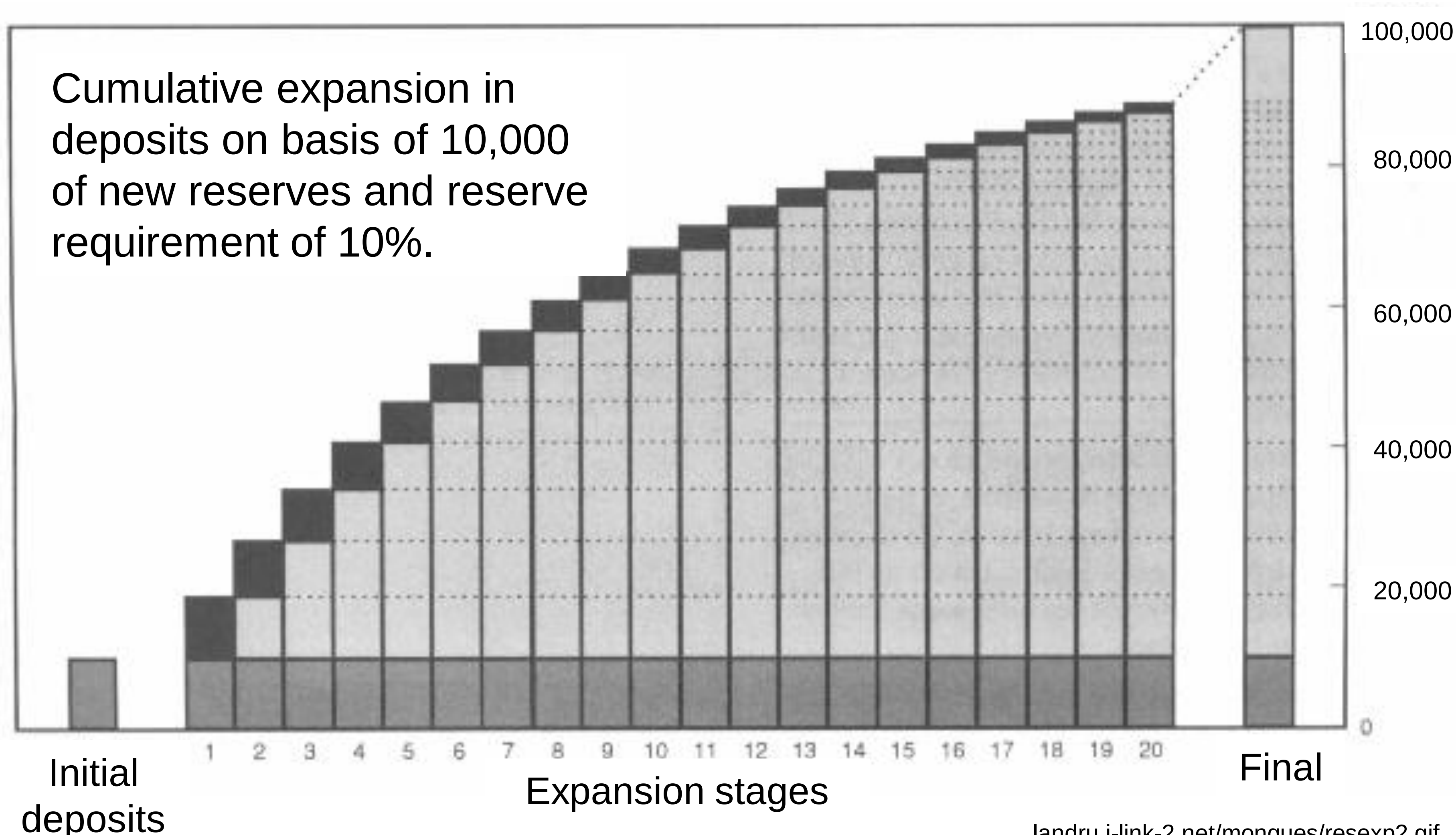
The loan money is created by double-entry bookkeeping.



Net result: 0.

Modern Money Mechanics, p. 49:

"With a uniform 10 percent reserve requirement, a $1 increase in reserves would support $10 of additional transaction accounts."



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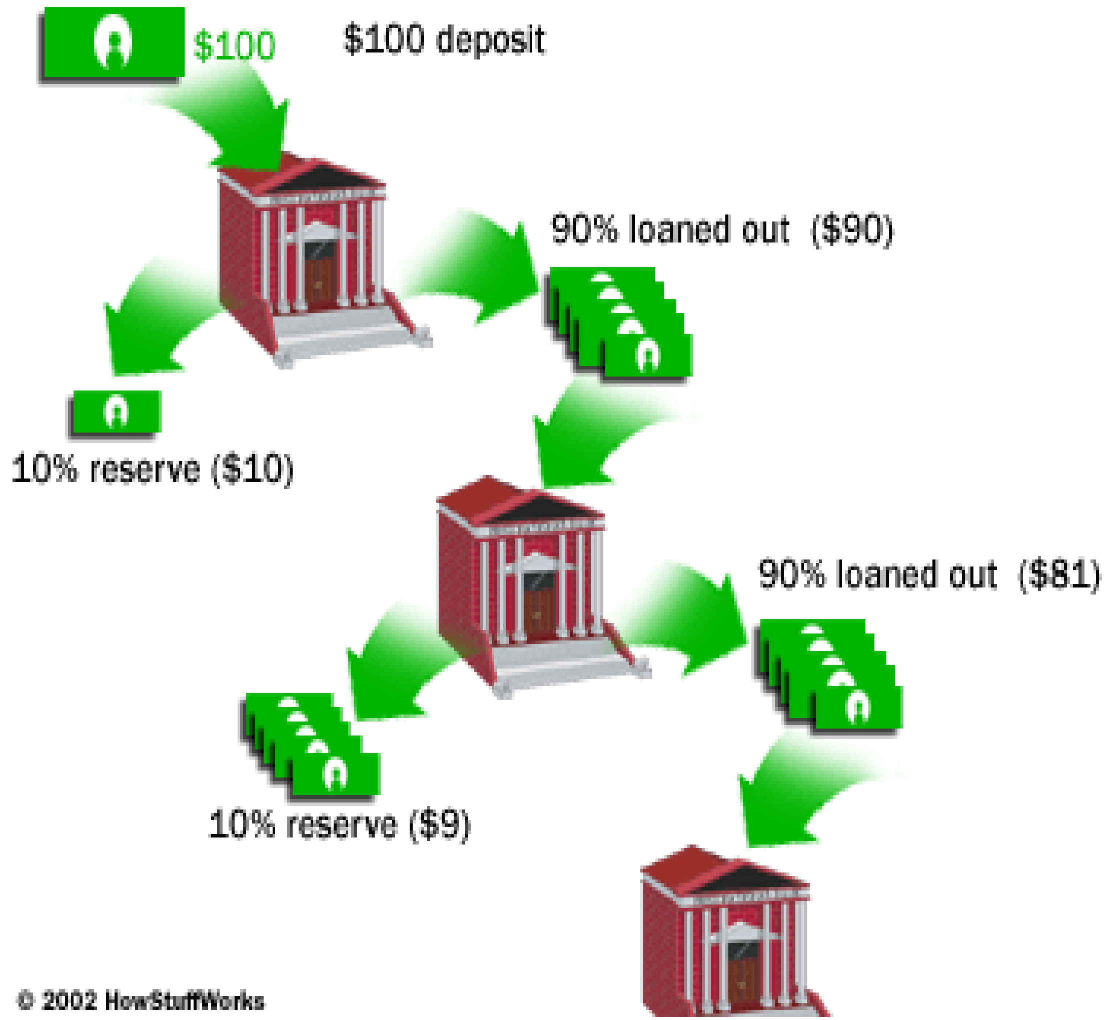
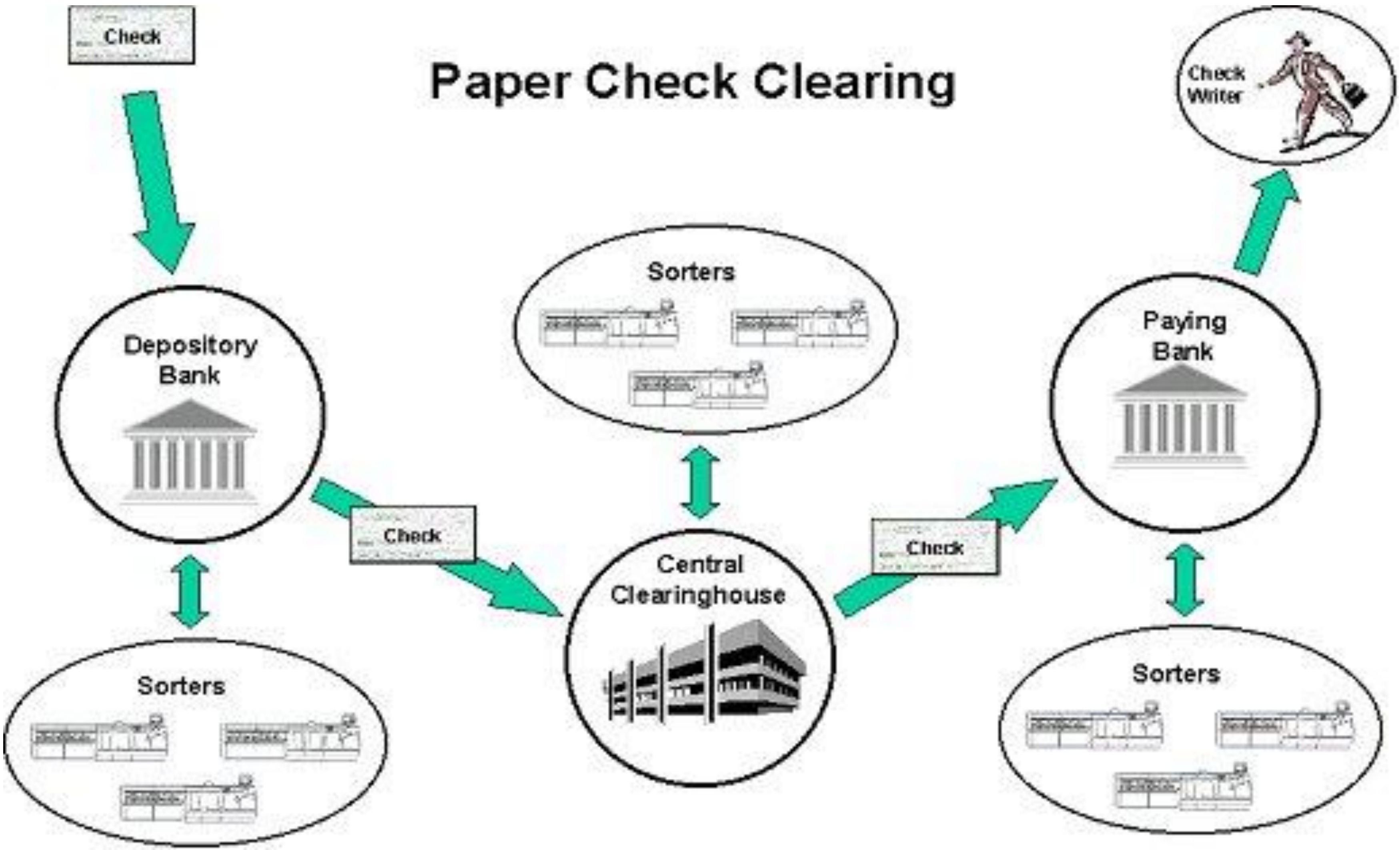
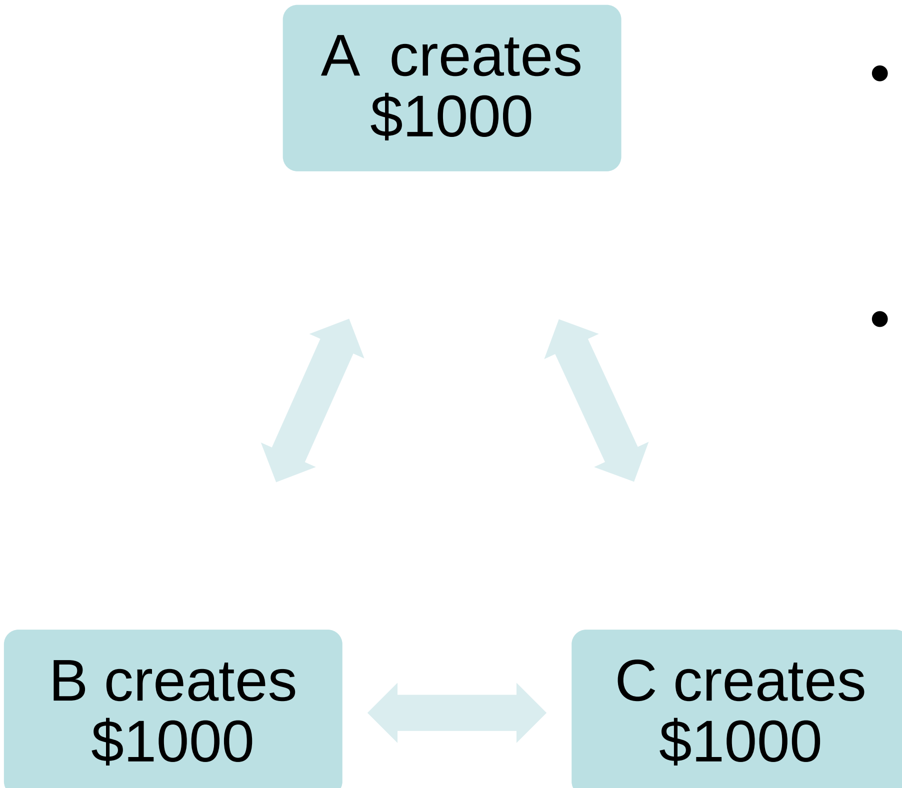
Deposits become loans . . . become deposits . . . become checks . . . become deposits in other banks.

- That's the conventional model, but banks actually create the loans FIRST.
- They find the deposits to meet the reserve requirement later.



Banks can originate all the loans they can find creditworthy borrowers for, but they need incoming deposits to clear the checks . If they don't have the deposits, however, they can borrow them.





- So banks create money as loans, which become checks, which go into other banks.
- Then, if needed to clear the checks, they borrow back the money they just created.

LIMITATIONS ON CREDIT CREATION

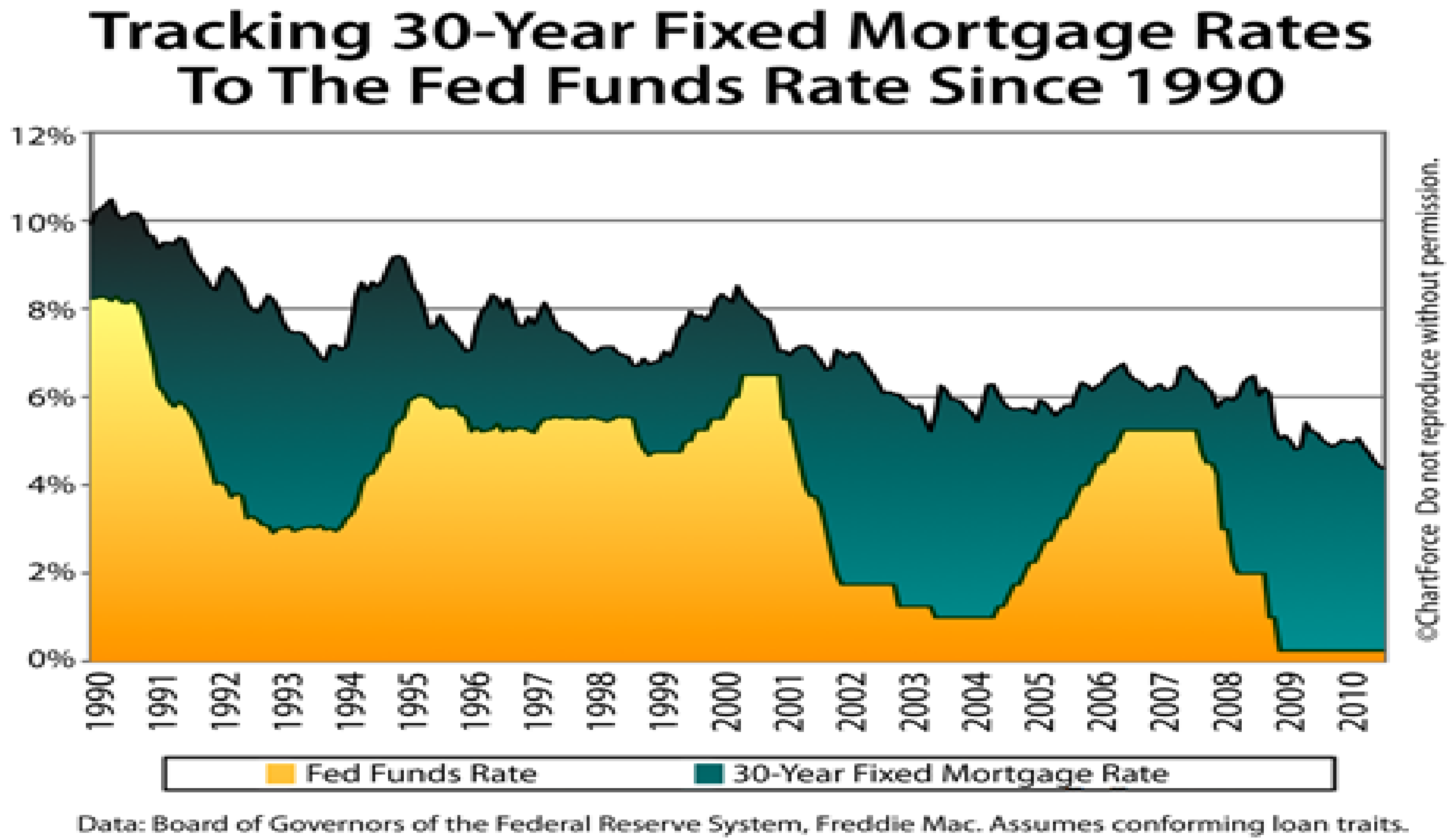
- Available reserves or, if reserves are borrowed, the cost of funds
- Creditworthy borrowers
- The capital requirement

The capital requirement

- Established in 1988 by the BIS in Switzerland for international lenders (Basel I – followed by Basel II and Basel III)
- $8 of capital required per $100 of loans
- “Capital” means the bank’s own equity, not the money of depositors.

The cost of funds --

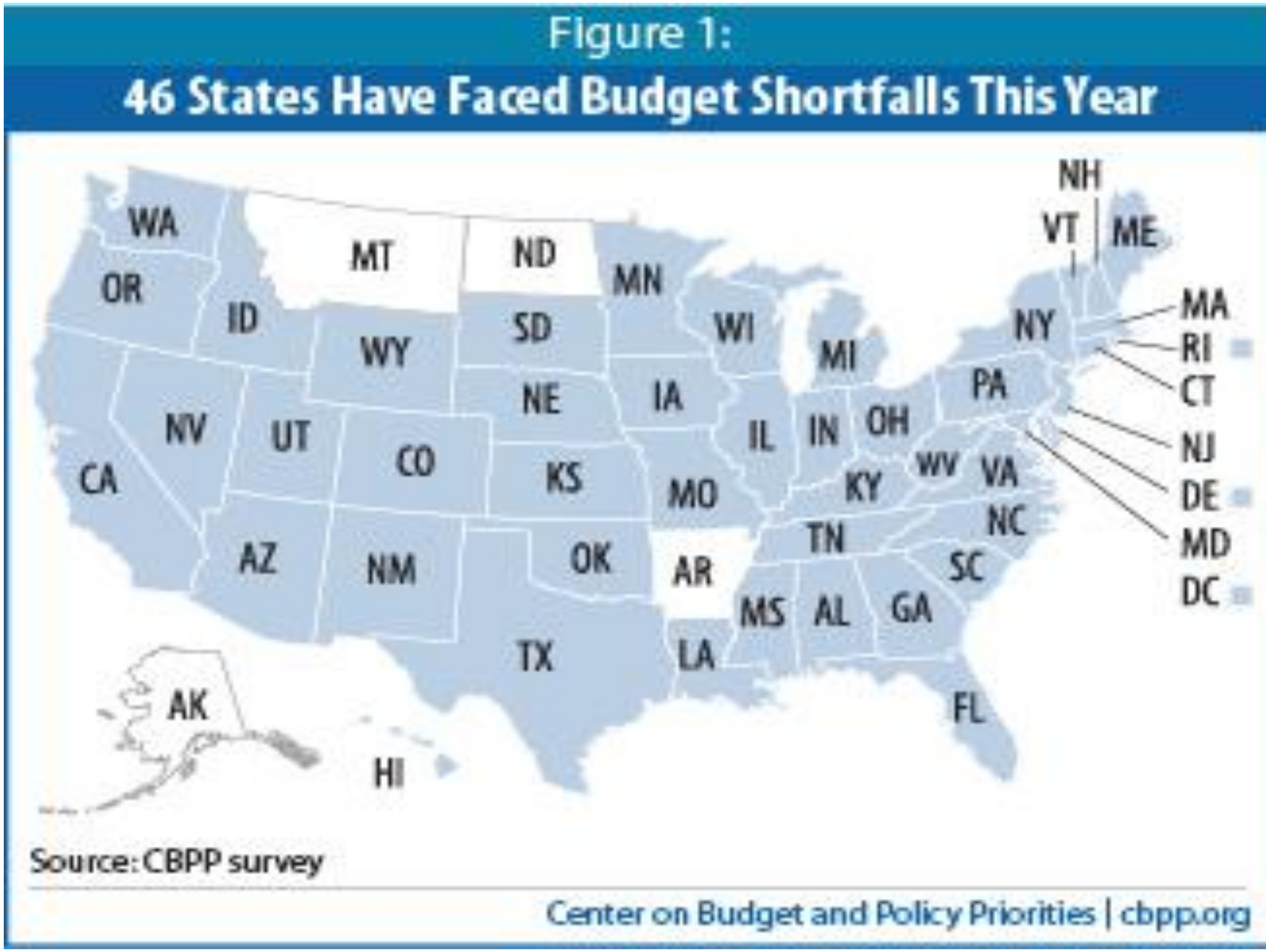
The Fed funds rate has been dropped to 0.2%, but this windfall isn't passed on to us. States are borrowing at 4-5% and the rest of us at higher than that.



HOW CALIFORNIA COULD SOLVE ITS BUDGET CRISIS – THE NORTH DAKOTA MODEL

- With its own bank, a state too could multiply its money by turning its deposits into loans.
- A state too could borrow from other banks at 0.2%, or from the Fed's discount window at 0.75%.
- Only one state currently has its own bank . . .

As a result of the credit crisis, most states are facing serious budget shortfalls – most but not all . . .



Center on Budget and Policy Priorities, Oct 2010

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One billion big ones

State budget outlook predicts huge surplus, $70 oil

By DALE WETZEL
Associated Press Writer

A new forecast of North Dakota's tax collections predicts a $1 billion budget surplus in July, continuing a robust financial trend that has defied a national recession and budget deficits in most states.

Oil prices, a key contributor to the state's wealth, are expected to average $70 a barrel for the next two years, the forecast finds.

Revenues are expected to rise almost 10 percent during the same period. An even higher spike is expected in sales tax collections, which provide the biggest share of the budget for North Dakota government.

"I think it's good news, but it's not unexpected," Lt. Gov. Jack Dalrymple said Tuesday. "It shows the economy in North Dakota is still in good shape."

North Dakota's current two-year budget is $8.84 billion, a figure that includes federal aid to the state.

The forecast was compiled by the state Office of Management and Budget and Moody's Economy.com, a West Chester, Pa.-based consultancy, to prepare Gov. John Hoeven's budget recommendations. Its numbers will be updated in November, a month before the governor's spending plan is presented to the Legislature, said Pam Sharp, the state budget director.

The forecast includes estimates of state tax collections for the rest of the current 2009-11 budget period, which ends June 30, and a forecast of revenues for the *Continued on 9A*

- In 2009, while other states floundered, North Dakota had its largest budget surplus ever.
- North Dakota is the only state to own its own bank.
  In 2008, the Bank of North Dakota (BND) returned a 26% dividend to the state.
- ND has the lowest unemployment rate in the country and the lowest default rate on loans.
- It also has the most local banks per capita.

North Dakota has had its own bank since 1919, when farmers were losing their farms to the Wall Street bankers. They organized, won an election, and passed legislation.

The BND has a captive deposit and capital base. It's a dba of the state, and all state revenues are deposited in it by law.

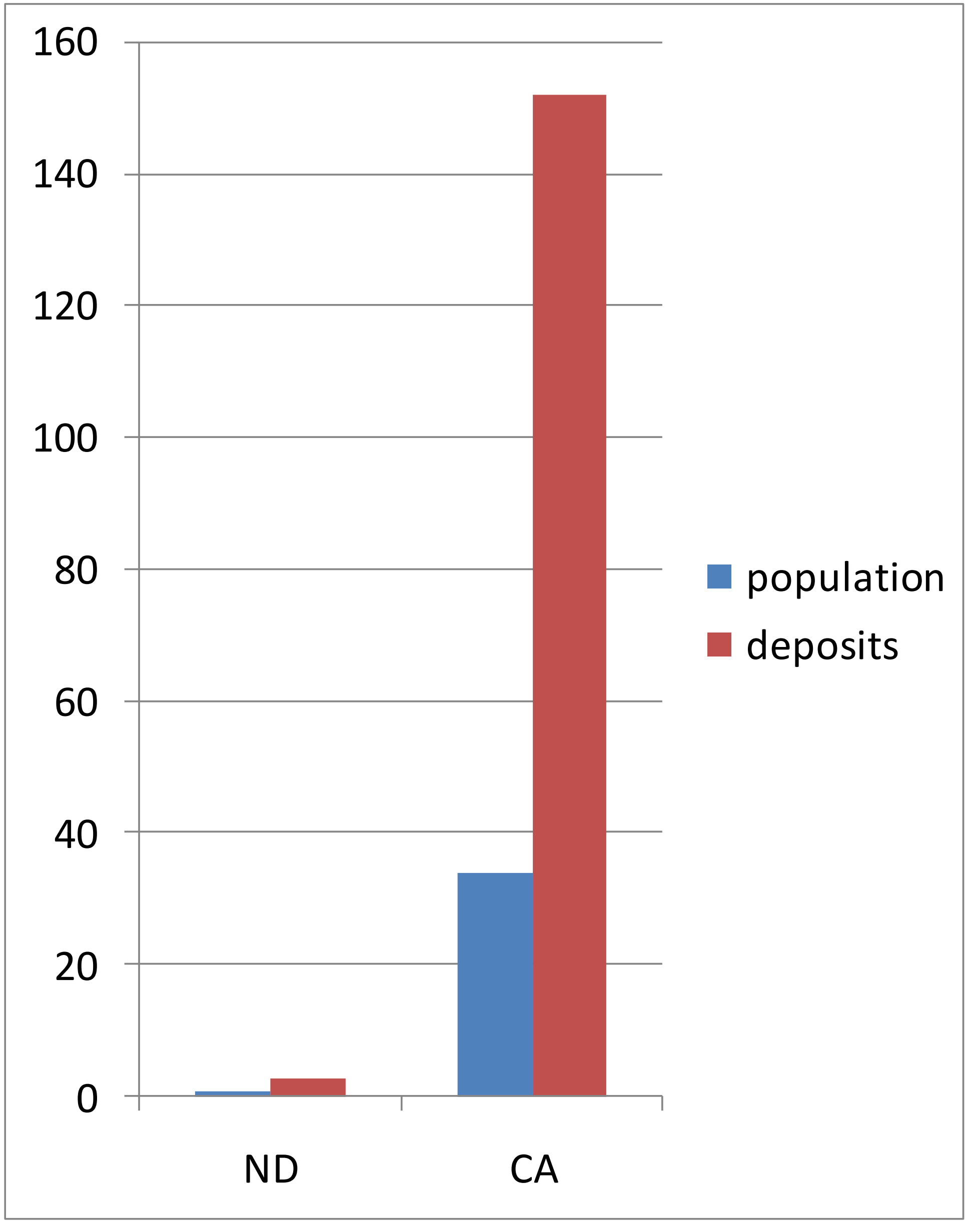
Consider the potential for California --

North Dakota:

- Population 647,000
- Deposits $2.7B
- Deposits per capita – approx. $4000
- Loans $2.6B

California:

- Population 37,000,000
- At $4000/person, deposits = $148 B
- Potential loans = $142 B



For the capital requirement --

- CA has funds stashed in an investment pool managed by the Treasurer of *$71 billion*, earning *2.24%* interest as of Aug 2009.
- CA has pension and other trust funds of *$306 billion*.
- At an 8% capital requirement, only *$12 billion* of this fund money invested in equity in a state bank could back a potential loan portfolio of *$150 billion.*
- The BND is rated A+ by Standard & Poor's and returned a *26%* dividend to the state in 2008, substantially better than the CA fund's 2.24%.

What could CA do with $142 billion?

- Fund the deficit at 0% interest = $28 billion.
- Fund infrastructure and other public projects interest-free.
- Rehire 20,000 laid-off teachers = $3.4 billion/year.
- Partner with local banks, guaranteeing and sharing in low-interest loans to local businesses and homeowners.
- Reduce state tuition or give interest-free student loans.

Investments in education and infrastructure can pay for themselves.

- Example: the G.I. Bill, which paid for itself many times over with increased productivity and taxes.
- Cutting out interest reduces project costs by 30-50%.

Borrowing from their own banks would be a much better deal for the states.

- States rated AA now pay an average of 4.45% on 20 year fixed bonds.
- CA and IL are rated A-, along with Estonia and Libya, and just above Greece.
- CA pays 4.7% on its $53 billion debt.
- IL pays 12% on late payments.

- With their own banks, states could acquire the funds to back their loans for --
- As low as 0% on their own deposits
- 0.2% on interbank loans at the fed funds rate
- 1.27% on 6-month CDs

Advantages to local banks:

- In North Dakota, the BND serves as a “banker’s bank,” partnering with local banks and helping them with capital requirements.
- Risky loans to students and startup businesses can be underwritten by the state.

Advantages to local governments:

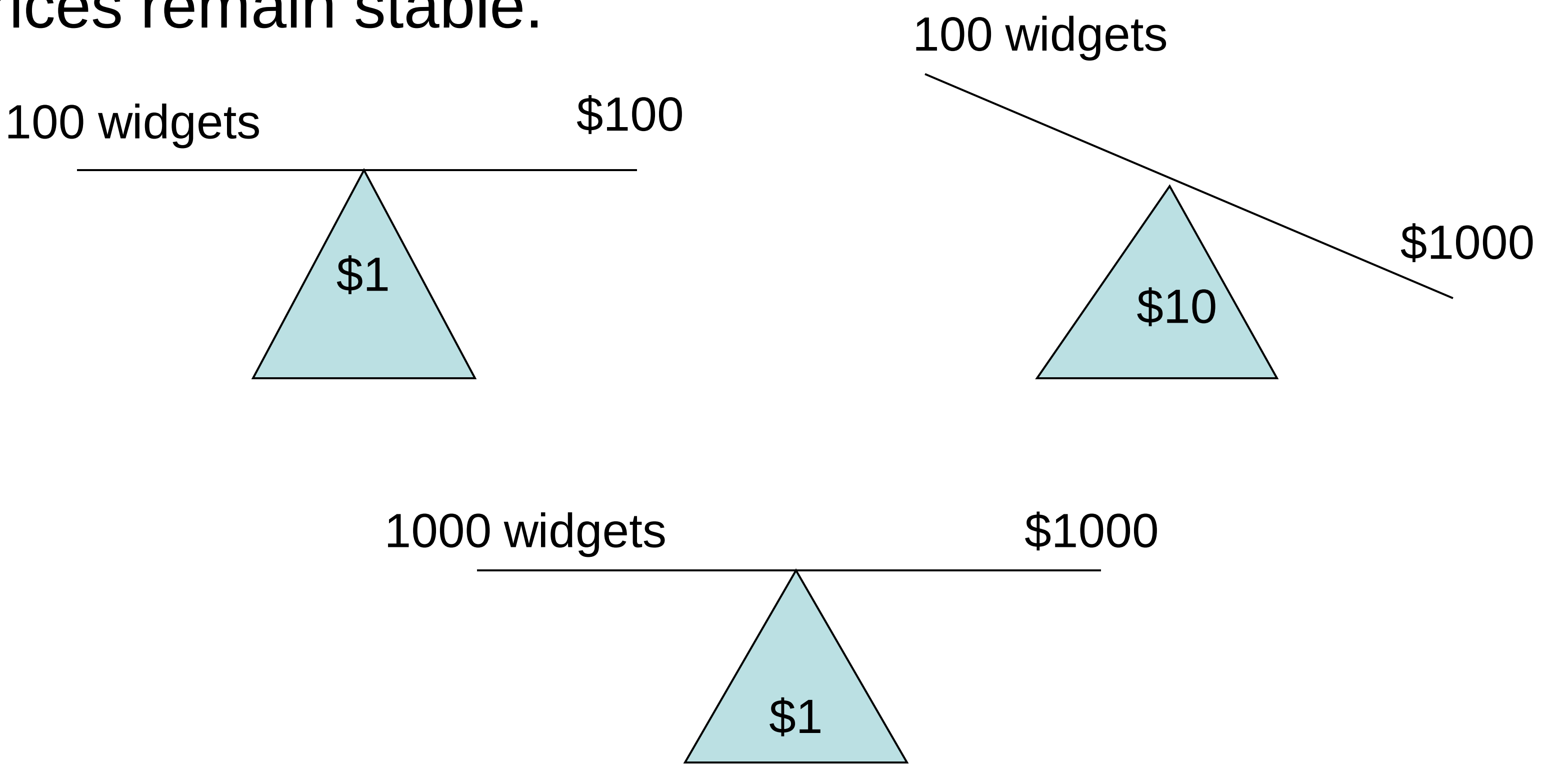
- Honest lender with a mandate to serve the community replaces “city slicker” bankers selling derivative scams to unwary local politicians.
- Low-cost credit line replaces costly “rainy day” funds.
- Infrastructure projects can be funded interest-free with the state’s own credit.

Advantages to the state

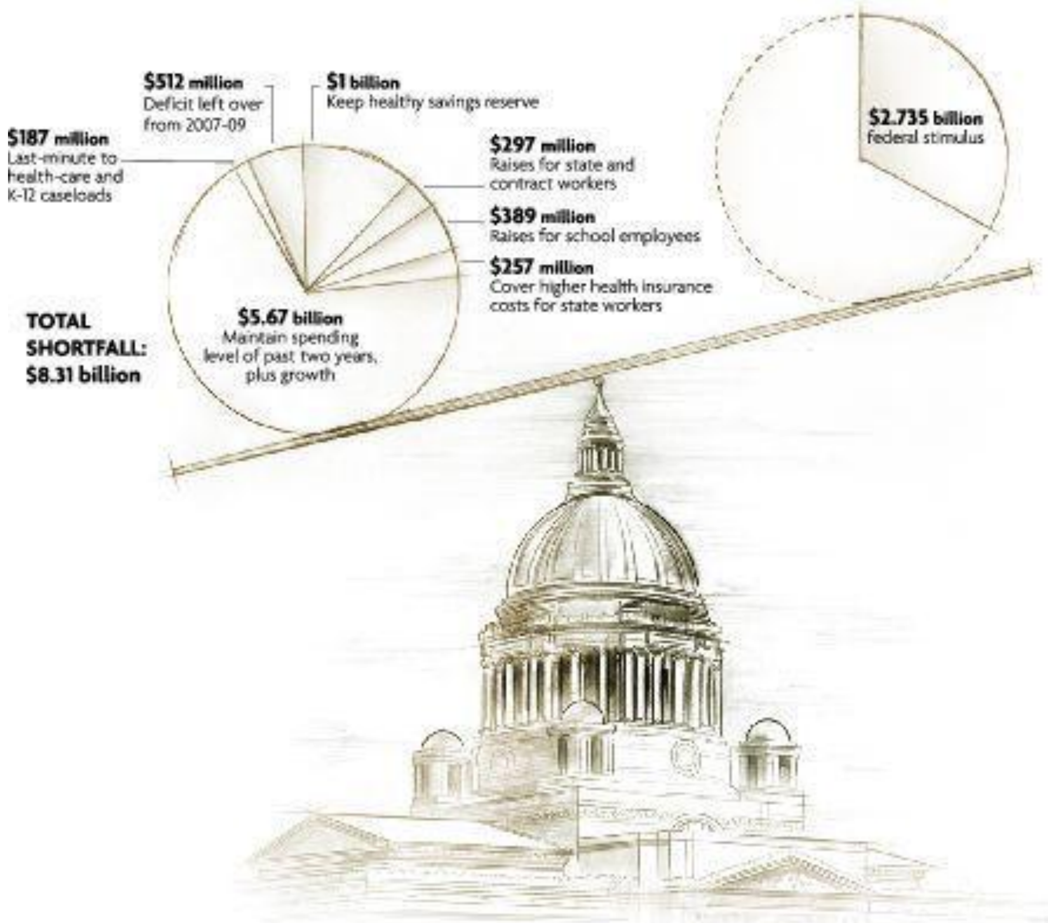
- State revenues remain in the state.
- Profits and interest return to the state government, defraying taxes.
- No high-paid CEOs; no bonuses, commissions or fees; no toxic collateral.
- Can take the long view: no shareholders demanding short-term profits.
- No late fees or fears of lost credit ratings.
- Huge savings in interest costs.

HOW SERVICES AND INFRASTRUCTURE CAN BE EXPANDED WITHOUT ADDING TO THE TAX BURDEN OR CREATING INFLATION

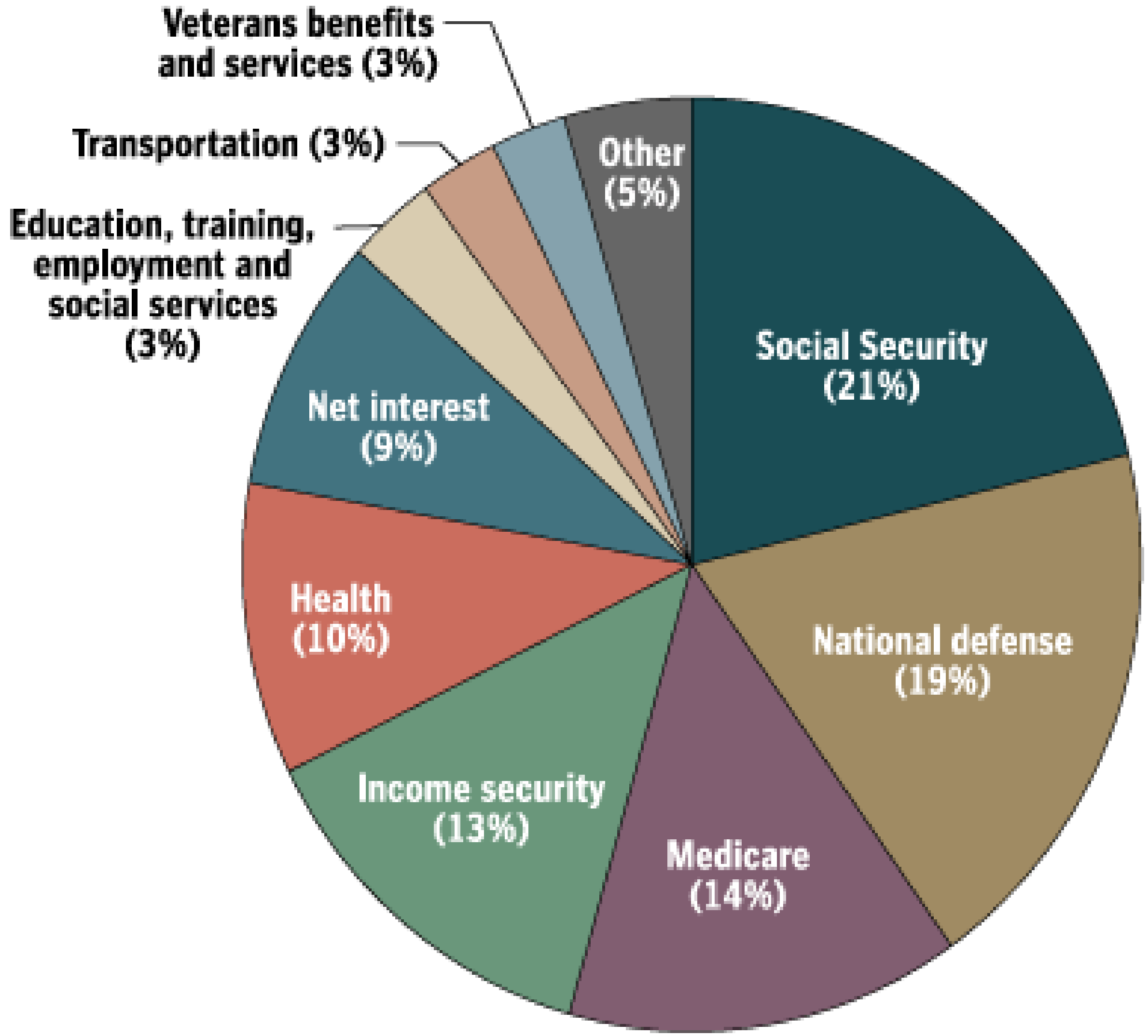
When the new money creates new goods and services, prices remain stable.

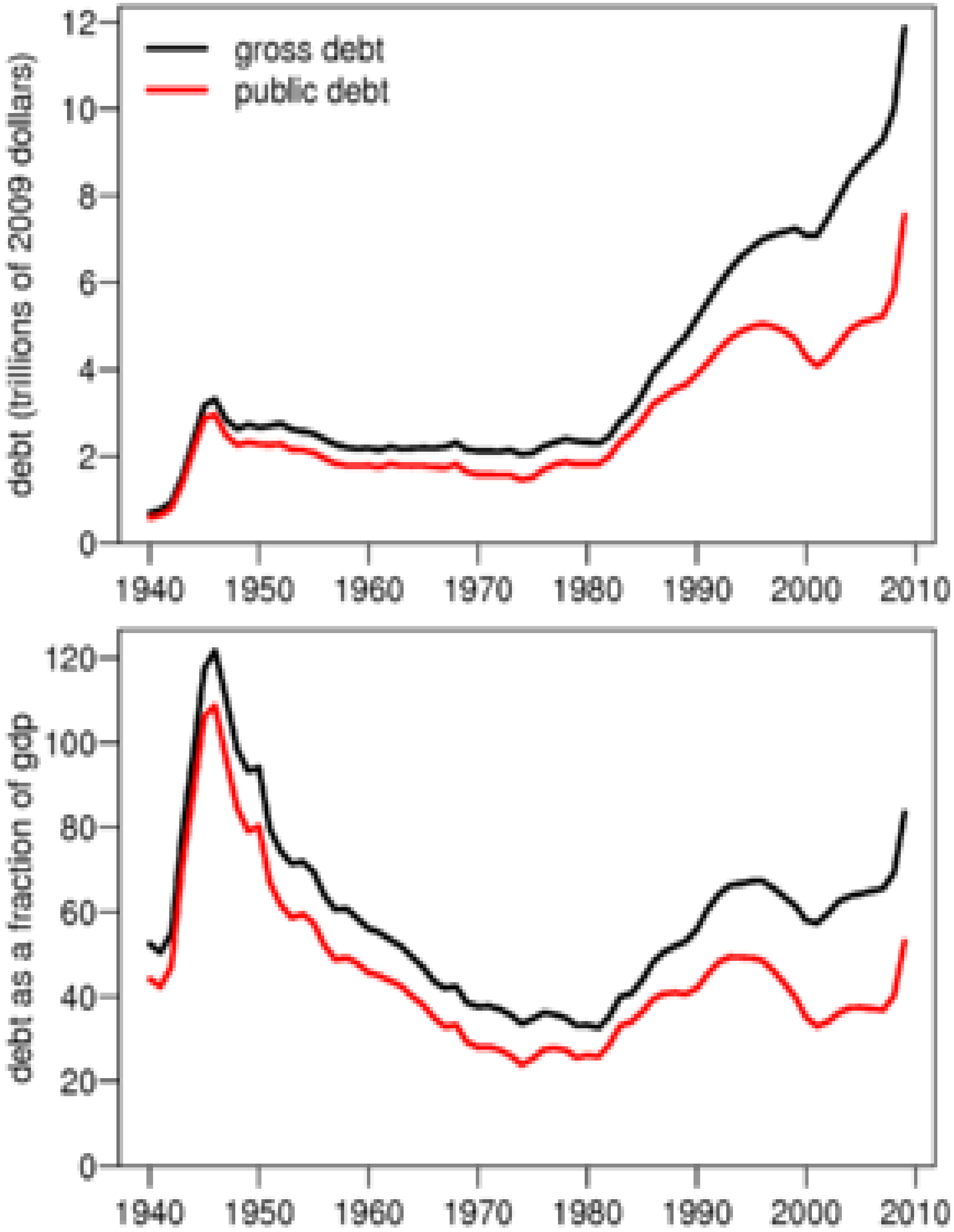


- Interest-free loans from the state's own bank could be added without adding to the budget burden.
- This is because, while governments have to balance their budgets, "balancing the budget" only means paying the interest on the debt.



- CA’s total debt is $53 billion. Paying it off is not part of the budget.
- When President Clinton “balanced the budget,” the federal debt was still $6 trillion.

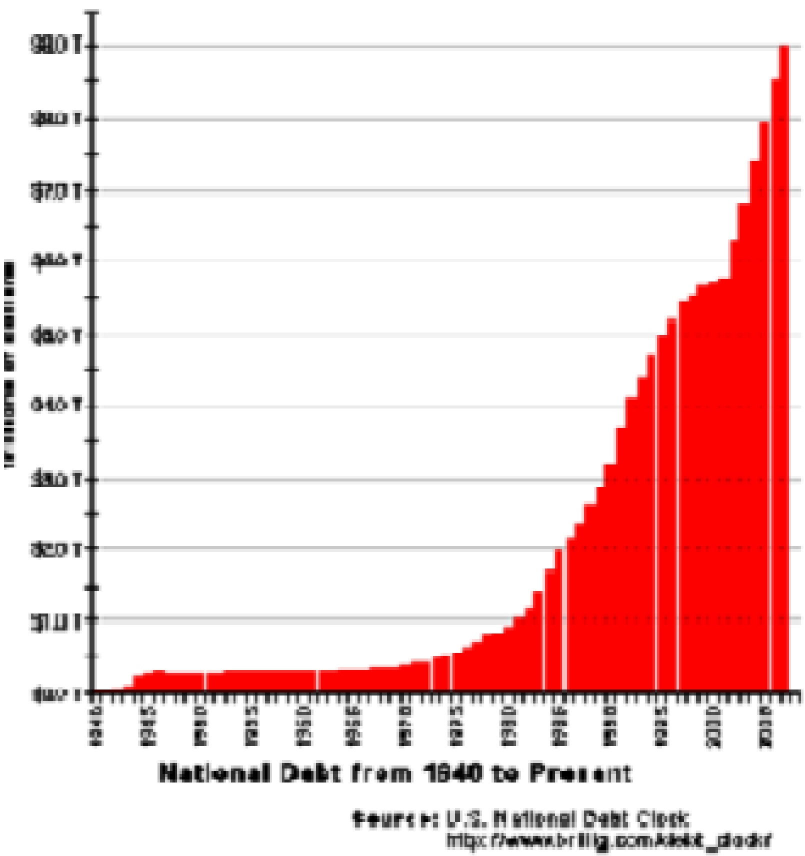




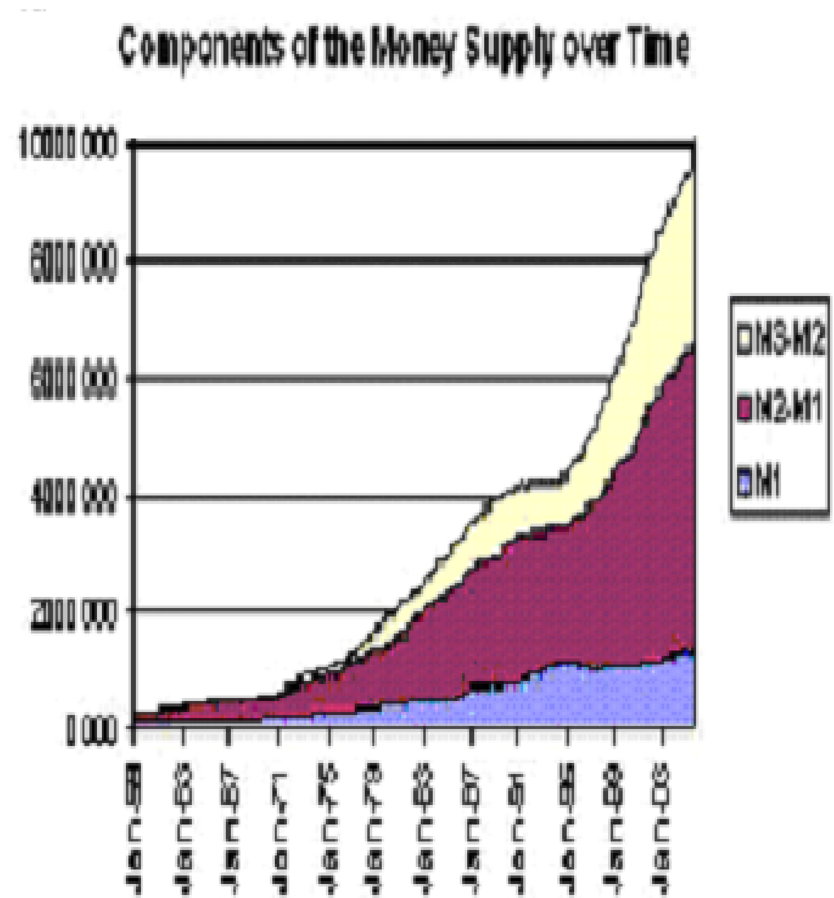
Our largest public debt was in our most productive period – World War II. Productivity and increased tax revenues absorbed it.

The federal debt is never repaid but is just refinanced from year to year. Only the interest is paid.
In effect, the money supply IS the public debt.

Federal debt 1940 to 2007 ($9T)



Money supply 1959 to 2006



Interest is the snag in our private banking system.

paulgrignon.netfirms.com

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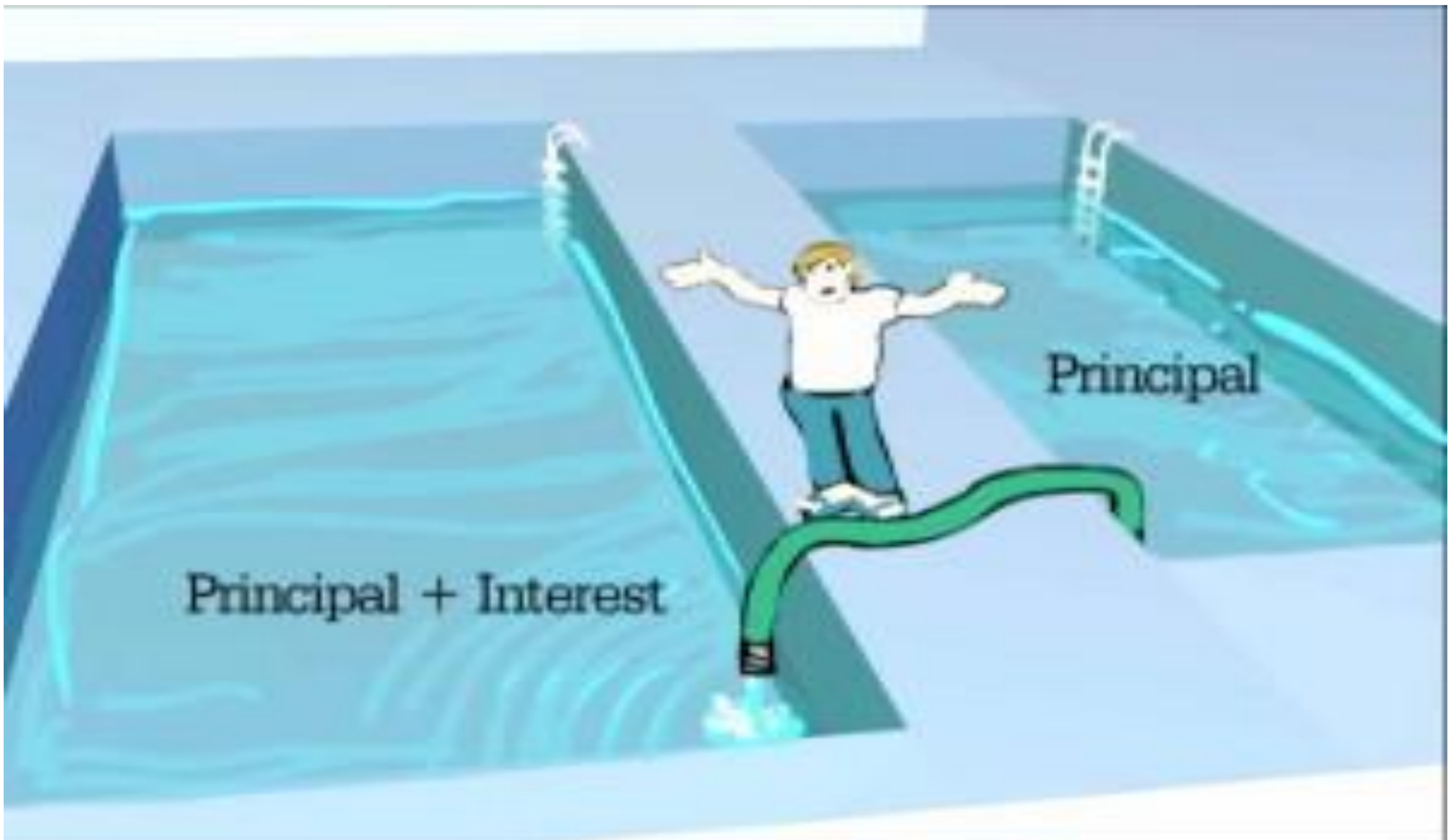
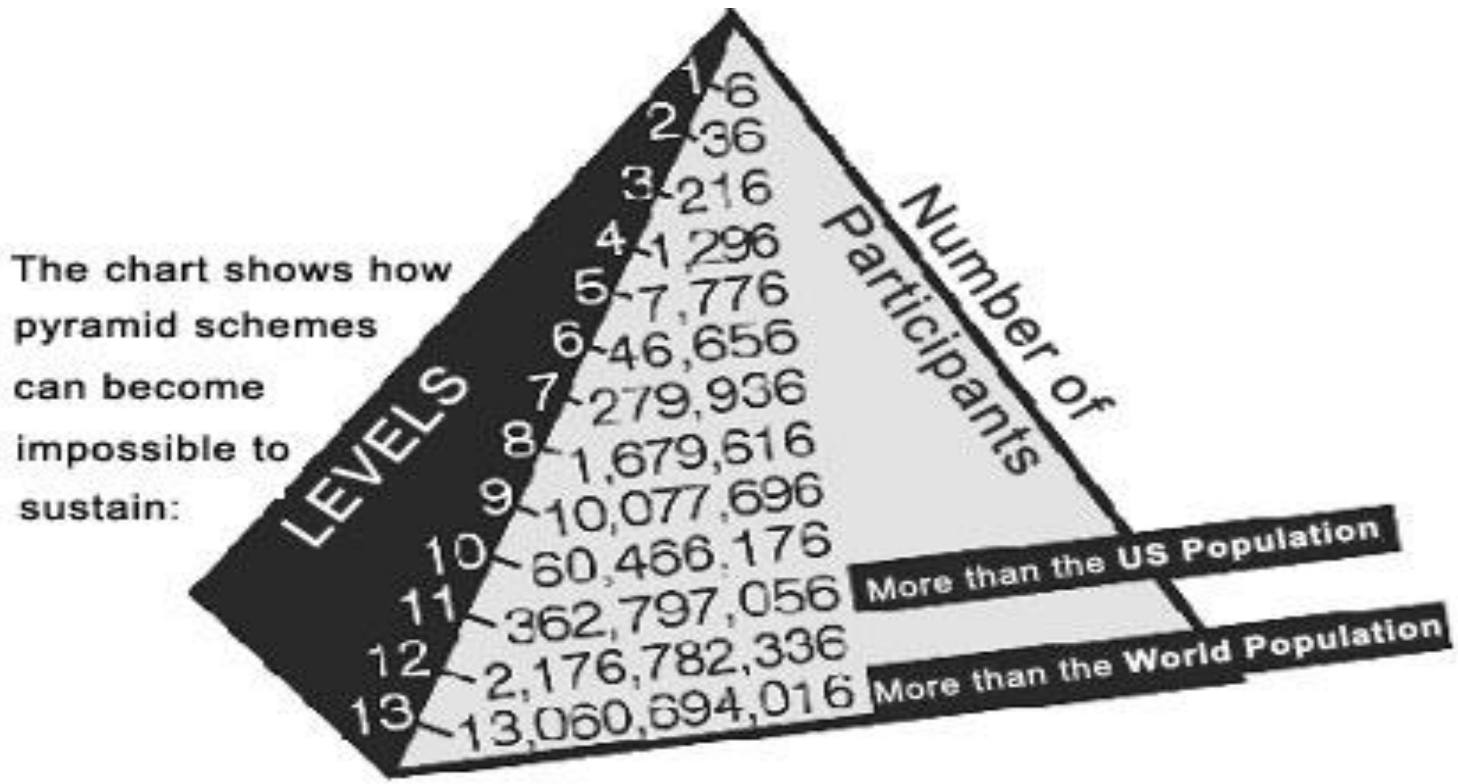


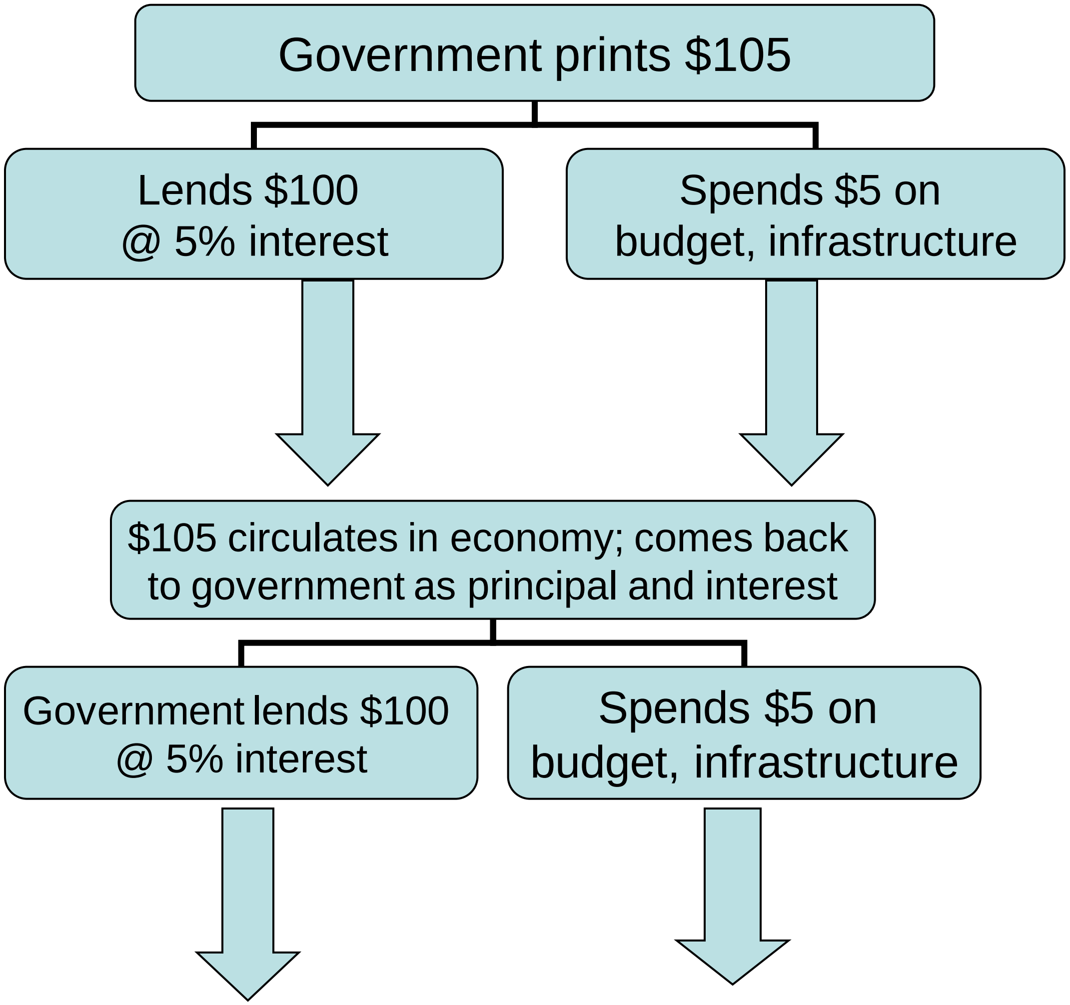
It's the interest that makes our debt-based system a pyramid scheme. When interest returns to the state or the community, the credit system is sustainable.

- www.answers.com

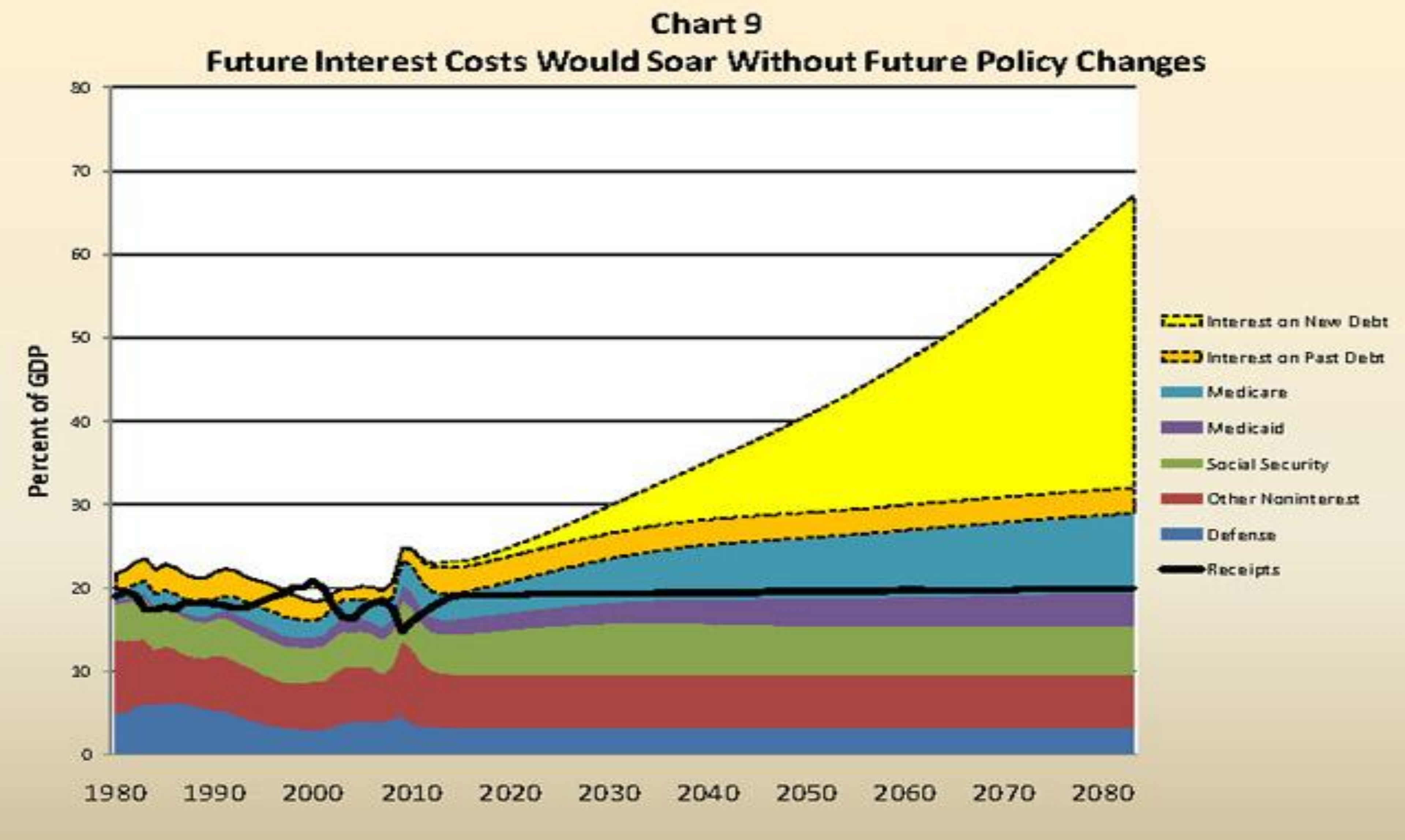


That was actually the model of the first U.S. public bank, in Benjamin Franklin's province of Pennsylvania. Money was printed and *lent* into the community. It was recycled back to the government and could be lent and relent.

During that period, *the colonists paid virtually no taxes, prices did not inflate, and there was no government debt!*

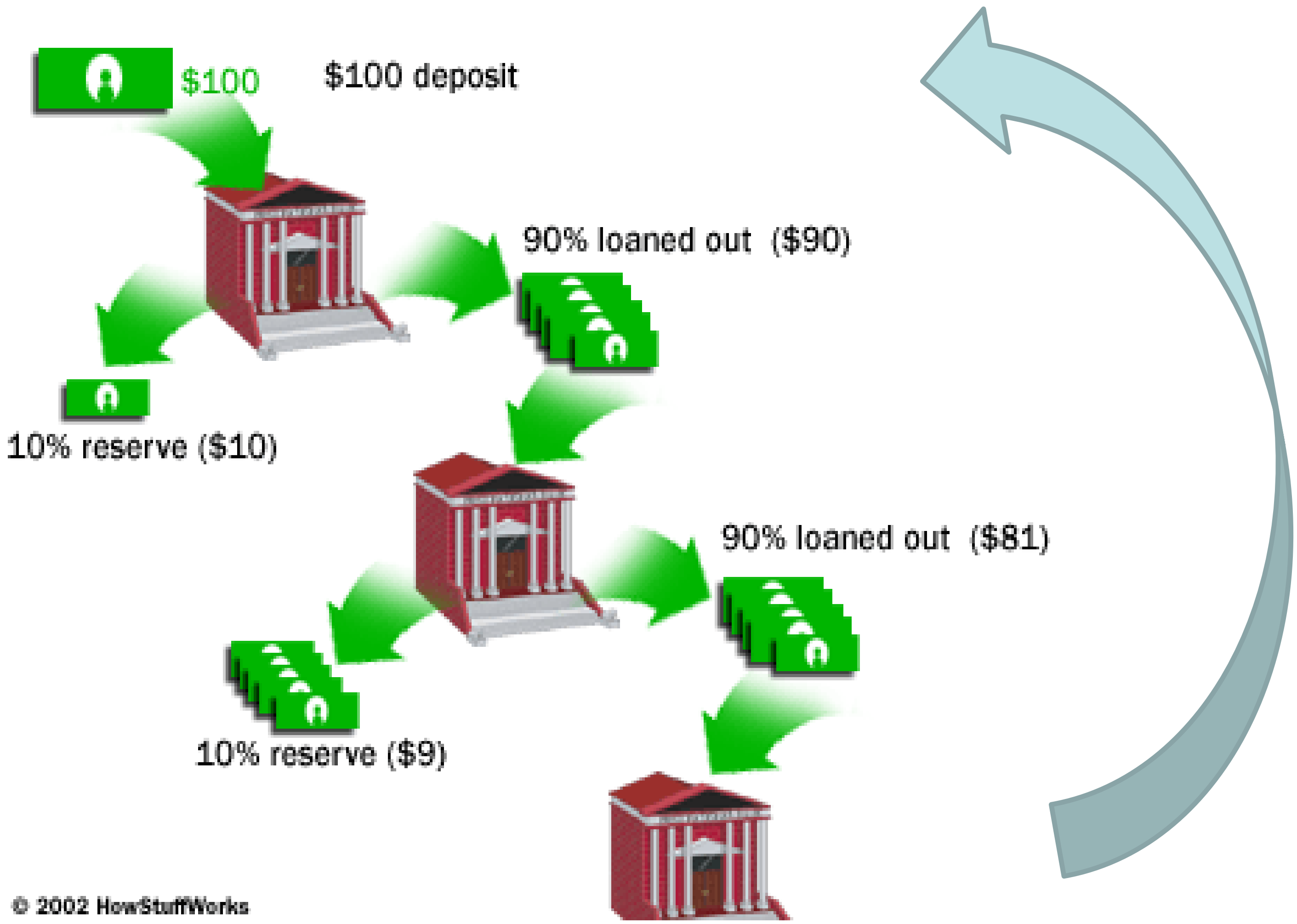


Eliminating the interest would allow the public debt to be carried and even expanded indefinitely.

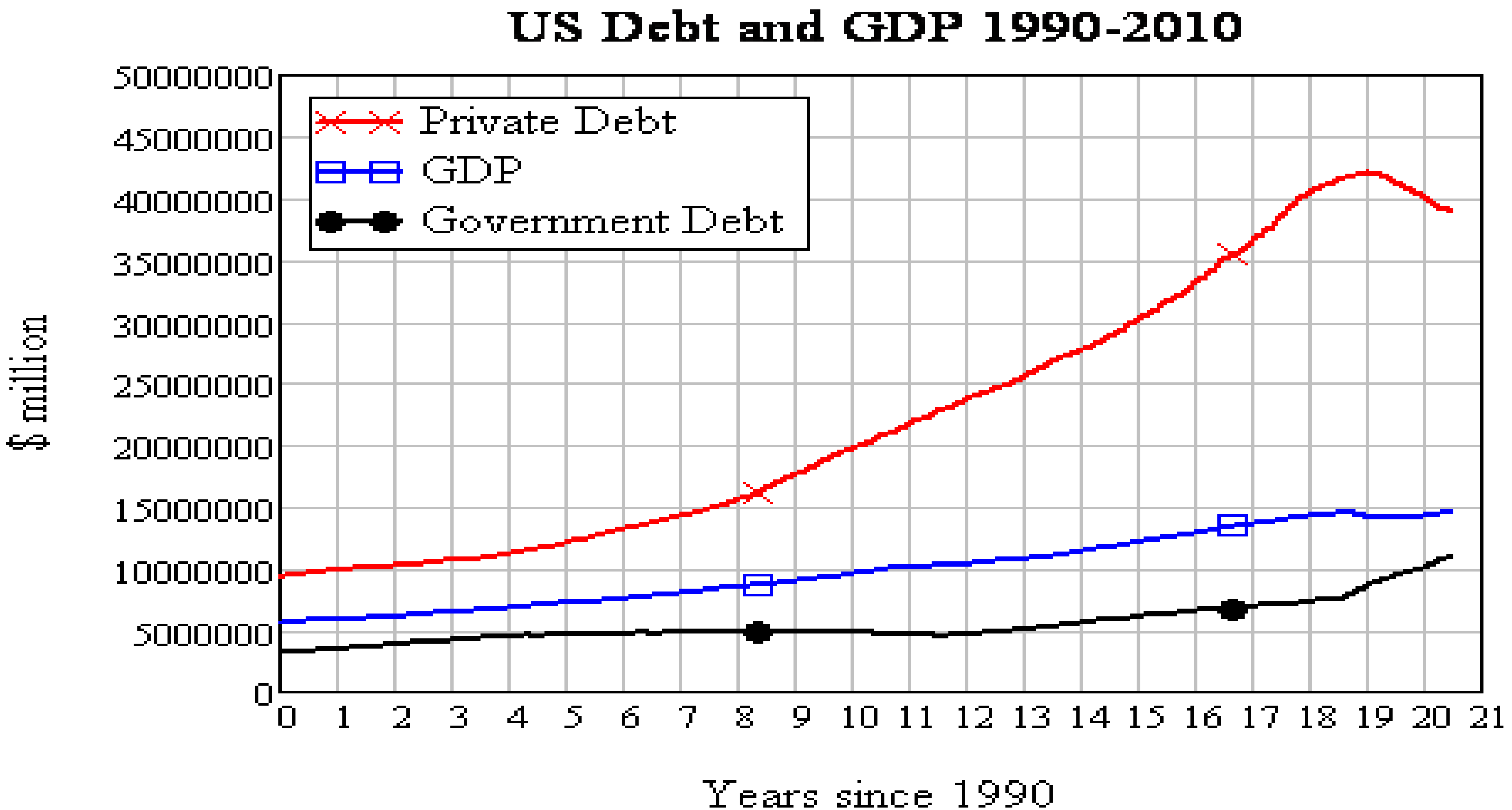


Today, we NEED more government debt. Nearly all money originates as debt, and private debt is shrinking.

Banks are “deleveraging.”
The money multiplier effect is working in reverse. The loss of $8 in capital removes $100 in loans.



Increasing the public debt when private debt shrinks is not inflationary. It is just maintaining the money supply at existing levels.



TAKING ACTION

- A number of state legislatures have initiated bills for state-owned banks, including WA, IL, MA, HI, MI and VA.
- In the last election, a number of candidates also proposed this solution, from all across the political spectrum -- Democrats, Republicans, Greens, and Independents.

How long would it take to have a bank up and running?

- 60-90 days, says banking law consultant Bruce Cahan.
- Here's how: buy a failed bank that is already FDIC insured, using the shelf registration process. First, get organizers approved and get approval to own a bank; then make bids on failed banks.
- He recommends building a pro forma balance sheet and income statement to establish the possibilities for a State Bank of California. (We've assembled a team for this, but we need help finding the data on municipal, county and state deposit activity at banks, the balances they hold, how they're held, and the turnovers.)

STEPS WE COULD TAKE

- Design a working model and bank balance sheet to show the possibilities.
- Network and mobilize groups: budget reform and advocacy groups, state financial officers, county assns, etc.
- Form a Political Action Committee.
- Draft a bill to study the feasibility and advantages of a state-owned bank.
- Petition representatives.
- Draft legislation.
- Draft an initiative. One now in the works is posted at californiagreenbacks.org.

As Buckminster Fuller said --

"You never change things by fighting the existing reality. To change something, create a new model that makes the old model obsolete."

For more information –
www.public-banking.com
www.webofdebt.com