

# A breakthrough in the battle over bank policy

By Elisa Barwick and Bob Butler

Who has the final call on banking—the government or central bank? The RBA has made a stunning concession in what has been a defining battle across Australian history.

For over 12 months a number of Senators have pressed the Reserve Bank of Australia (RBA) at every Senate Estimates hearing on why the RBA and government policy, which is expanding the speculative housing bubble with regular injections of cash, could not instead be used to inject funds into the real economy.

So far, the battlelines have been drawn along an ideological divide that neither the government, nor the RBA, want to cross. Governments control fiscal policy and central banks control monetary policy, therefore the RBA does not fund economic programs such as infrastructure building.

That line was restated by new RBA Deputy Governor Michele Bullock in answering a question put by LNP Senator Gerard Rennick at the latest, 6 April estimates hearing of the Senate Economic Legislation Committee. Rennick, who earlier sparred with recently departed RBA Deputy Governor Dr Guy Debelle over the issue, had asked what the RBA would do if “if the government directed [it] to create money through a quantitative easing program to build infrastructure such as dams, power stations and roads”? After a lengthy back and forth, Ms Bullock returned to the RBA refrain that building infrastructure is “a matter for the government”, Rennick’s insistence that he was referring only to the funding not the actual construction notwithstanding.

Rennick stated: “We’re not disputing whether or not we should build infrastructure. It’s how it gets funded. If we borrow \$1 billion offshore to build a dam, the first billion dollars we create in wealth goes back offshore. If we fund it here, domestically, the first billion dollars we create we keep here. We shouldn’t be paying other countries billions of dollars a year to use their printing press when we’ve got our own here. That’s my point.”

Significantly, Ms Bullock’s ultimate answer was: “If the government directed us to do that, that is a conversation that would have to be had.”

And here the rubber meets the road. Can the government direct the RBA on how to conduct monetary policy, or must the RBA be respected as an entirely independent entity despite its decisions impacting the welfare of the entire nation? Is it the RBA or the government which has ruled out directing the banks to serve the real economy?

## We have the power

A growing dossier of evidence points to the fact that the government does have the power to direct the banks *through existing banking legislation*, but that both parties—the government and RBA—have put up blockades. Armed with that knowledge, the urgent requirement to generate credit flows into the real economy, and a handful of parliamentarians from various parties refusing to back off on the question, a breakthrough is potentially within reach.

Per the prescription of politicians committed to the principle of the Common Good, rather than the neoliberal dikats that dominate today, the banking sector in Australia is still bound by these realities:

- The preamble of the *Reserve Bank Act 1959*—which senators have quoted in various estimates sessions—commits monetary policy to fostering “the economic prosperity and welfare of the people of Australia”.
- The 2 February *Australian Alert Service* (“RBA review



Senators Gerard Rennick and Nick McKim putting the RBA through its paces. Photos: Screenshots

must jettison neoliberal mandates”) revealed that the *Reserve Bank Act 1959* also outlines a procedure (in [Section 11](#)) for resolving disputes between the RBA and government over monetary policy, which ultimately “allow[s] the Government to determine policy in the event of a material difference”, as expressed in numerous [Statements on the Conduct of Monetary Policy](#), semi-regular documents issued jointly by the Treasurer and RBA Governor. So, if the government directs the RBA to issue credit for the economy, it will prevail. (This is likely an artefact of the 1937 banking royal commission, see below.)

• In Senate hearings on 16 February, another MP who has doggedly pursued the banking issue, Greens Senator Nick McKim, drew attention to existing RBA powers to “direct the class of loans that banks can make”, contained in the *Banking Act 1959*. Answering the question on notice, the RBA revealed the bank indeed has this power—a remnant of the old Commonwealth Bank.

McKim asked Dr Debelle whether the RBA has considered using the powers granted to it under Section 36 of the *Banking Act 1959*, which states that:

(1) *Where the Reserve Bank is satisfied that it is necessary or expedient to do so in the public interest, the Reserve Bank may determine the policy in relation to advances [loans] to be followed by ADIs; and,*

(2) *Without limiting the generality of subsection (1), the Reserve Bank may give directions as to the classes of purposes for which advances may or may not be made by ADIs.*

McKim suggested the power would “allow the RBA to direct a bank to limit the number of housing loans it makes with any particular basket of money that it might get, for example from the RBA’s money printing”. McKim also asked whether it might, to the same end, be used to “establish a different cash rate for lending for housing, as opposed to lending for business”.

Answering on notice, the RBA bluntly responded that: “This power dates from the era prior to the deregulation of the financial system in the early 1980s, when there were wide-ranging controls on the financial system.” Government guidance of bank lending ended in June 1982 and “monetary policy now operates by influencing interest rates”, RBA said.

Evidently lacking any internal understanding of clause 36, RBA went searching for explanatory memoranda they may provide a clue. In the absence of any guidance on “the scope of, or intended use of, the RBA’s powers under section 36”, RBA chose to cite a revealing section of the explanatory memorandum for the equivalent clause in the predecessor of the 1959 Act, the *Banking Act 1945*. That explanatory reads:

*‘Regulation 7 of the National Security (War-time Banking Control) Regulations provides that “in making*

advances a trading bank shall comply with the policy laid down by the Commonwealth Bank from time to time." This power has proved helpful under war-time conditions, and will be useful as a continuing power to ensure that at all times the credit resources of the nation are put to the best use, and that the making of advances by banks **does not lead to an unbalanced expansion of credit in any particular field.** This clause will enable the Commonwealth Bank to determine the policy in relation to advances which is to be followed by all banks, without giving it control over individual advances.' (Emphasis added.)

AAS can confirm that this power, contained in that 1945 Act, was retained in the 1959 Act.

On the possibility of adopting targeted interest rates for different economic sectors, the RBA stated that it "cannot set a different cash rate for housing and other purposes". It is also clear from the RBA's responses to McKim's questions that it was by mutual agreement that the government and RBA settled on the current policy to ditch interest rate controls and sideline the power to provide guidance on bank loans. The removal of controls "was a joint decision of the RBA and the government", responded the RBA. "This decision was supported by the Campbell Committee, which also recommended that the power to impose direct interest controls should be removed from section 50 of the *Banking Act 1959*."

However, for whatever reason, the powers in section 36, allowing the RBA to determine bank policy in relation to advances, was not removed or neutered.

### Reviving the Chifley legacy

In his first estimates interrogatory with DeBelle on 24 March 2021, McKim had foreshadowed the intention of this power: "In the post-war era, central banks were much more prescriptive about where any newly created money was directed. In particular, they used credit guidance to steer central bank money to productive purposes. Is there any impediment to the RBA doing that?" Over one year later, we have finally arrived at the answer. If the political and ideological blockages are cleared, legally there is no impediment.

Extending as it does from the *Banking Act 1945*, the power contained in the *Banking Act 1959* is the legacy of Labor Treasurer and Prime Minister Ben Chifley. Chifley served on the Royal Commission into Monetary and Banking Systems which commenced in 1935 under the Joe Lyons government. The inquiry had resulted from contentious debates about who had the ultimate authority in the financial system—the elected government, or the central bank? This came to a head in 1930 during the Great Depression when Treasurer Ted Theodore instructed the Commonwealth Bank to issue £18 million for public works to deal with the crisis, but the central bank's chair Sir Robert Gibson, had refused, declaring, "I bloody well won't." ("Desirable objectives of a monetary and banking system: method of achievement", AAS, 27 Feb. 2019.)

The final report of the Royal Commission, released in 1937, confirmed that the elected government is the ultimate authority in the financial system. "The Federal Parliament is ultimately responsible for monetary policy, and the Government of the day is the executive of the Parliament." In a dispute between the government and the Commonwealth Bank board, the government's view must prevail, it confirmed. These findings established the principle of democratic control over the banking system, at odds with the neo-liberal tenets of financial deregulation that has taken control since the 1980s.

Regarding control over bank lending, the final report stated that, "In order to promote a wise distribution of credit, the Commonwealth Bank ... can advise trading banks as to the directions in which it is desirable in the national interest that advances should be made."

Chifley, intent on achieving the best financial order to develop the nation, issued a dissenting report in which he argued that private trading banks must be treated as "other public utilities—for example, gas companies—that in the public interest there should be some restriction on the profit which they are able to make from the supply of necessary services that the community is unable to obtain from other sources."

If left up to their own devices, the private banks will always "act much as any other company of individuals formed for the purpose of gain", however their importance is much greater than that of other companies, with access to banking and funding being the lifeblood of the nation.

Wrote Chifley: "Banking differs from any other form of business, because any action—good or bad—by a banking system affects almost every phase of national life. A banking policy should have one aim—service for the general good of the community. The making of profit is not necessary to such a policy. In my opinion the best service to the community can be given only by a banking system from which the profit motive is absent, and thus, in practice, only by a system entirely under national control."

On bank lending, Chifley shot down what the RBA today considers the single arrow in its quiver: "I disagree with the contention often made that the raising of interest rates is a suitable or effective method of checking undesirable expansion. In my opinion, this end can better be achieved by restricting the volume of advances."

As treasurer in the Curtin government, Chifley ensured that the Royal Commission's best recommendations, largely ignored by the previous Lyons and Menzies governments, were adopted. Not only did the Curtin-Chifley government effectively use the Commonwealth Bank to fund the war mobilisation, it also legislated to make permanent its war time controls over finance and the economy. This is reflected in the language of the *Banking Acts 1945* and *1959* and the advances explanatory memo cited by the RBA in response to McKim's questioning.

A number of amendments made over the course of the late 1940s and 1950s did not touch this advances power. In part this may have been due to the far greater preoccupation of the banks and their political puppets with fighting Labour's 1947 bank nationalisation law ("When fascists cried freedom to protect the banks", AAS, 2 Sept. 2020) and their effort to split off the central bank from the Commonwealth Trading Bank, so that private banks would not have to compete with a government bank.

It is time to seize this kernel of hope from the Chifley era and run with it, placing banks once more under real regulation and forcing them to serve the nation.



Ben Chifley in the 1930s, when he participated in the Banking Royal Commission. Chifley asserted then that the government must give directions to the banks, which he later inserted into the *1945 Banking Act*, and which power still exists to this day. Photo: Wikipedia