UNIVERSITI PUTRA MALAYSIA

PERCEPTIONS ON MONEY CREATION AND IMPACT OF ACCOUNTING TREATMENT FOR COMMERCIAL BANKS' MONEY LENDING ACTIVITIES IN MALAYSIA

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GSM 2018 33

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By

MD SHAMIM HOSSAIN

Thesis Submitted to the Putra Business School in Fulfillment of the Requirements for the Degree of Master of Science

July 2018

DEDICATION

I dedicated this thesis to my beloved wife and daughter. I highly appreciated for all their support. And this thesis also dedicated to all those people who are struggling for social justice.

Abstract of thesis presented to the Senate of Universiti Putra Malaysia in fulfillment of the requirement for the degree of Master of Science

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July 2018

Chairman : Ahmed Razman Abdul Latiff, PhD
Faculty : Putra Business School

It has been empirically proven from earlier study that commercial banks can individually create money when they extend a new loan. When banks extend new loans they do not need to wait for the customers to make deposits, rather they use a simple accounting entry to create a loan and transfer the loan amount into the borrower's account. This easy credit creation was one of the major reasons for the Global financial crisis 2007/2008. Banks continue to create money through lending in this manner because neither consumers nor governments have called them on it over the decades. In addition, excess supply of money as a result of accumulated commercial banks' deposit could lead to devaluation of the Malaysian currency. Excessive money supply through accumulated credit creation may result in inflation. In fact, the relationship between debt, money supply and inflation is not only true for Malaysia but also for other countries as well. More so, a large portion of money in Malaysia is backed by debt. From the monetary balance sheet of the *Ringgi*t it is apparent that fiat money is 99.6% backed by debt. Commercial banks' current money lending practice leads to development of credit creation which indicates that there are threats that may lead to potential financial crisis. This study aims to explore the perception of stakeholders on the impact of the accounting treatment on commercial banks' money lending activity.

Phenomenological approach has been employed to explore the perceptions of stakeholders through sharing of their experiences. A semi-structured interview approach has been used to collect the data. Seven individuals from different stakeholder groups have been interviewed with their prior consent. For the data analysis, this study has adopted the inductive thematic approach.

Findings of the study show that perceptions on money creation are influenced by the respondents' own understanding and awareness on the research issue. Respondents agreed on the accounting treatment (debit Loan and credit Deposits) but they explained the impact of this accounting treatment in different ways. There is a strong indication that money creation is happening in Malaysia like in other countries and it is happening through accounting treatment in commercial banks money lending activity. In addition, having the opportunity to use the accounting treatment, commercial banks can create money as they want and hence, the excess money created can create inflation and consequently may give rise to a potential financial crisis. Contrary to this belief, it has been argued that money creation is the result of the systematic approach of fractional reserve banking in Malaysia. According to this argument, money creation is not a threat to the economy as long there is a strong controlling role by Bank Negara Malaysia (BNM). Therefore, it is apparent from the respondents' discussion that money creation will pose a big challenge to the economy if the controlling role of BNM weakens.

In addition, respondents believed that accounting treatment for commercial banks' money lending activity has several impacts on the economy. First, respondents claim that money creation through lending is a big fraud because only private commercial banks can use this accounting treatment (debit the loan and credit customer account/deposit) while no other institutions can use this accounting treatment. Secondly, respondents stated that this lending system along with the accounting treatment has created a debt based monetary system. This is because, during the accounting treatment, there is creation of matching deposit for extended loan and, hence, there is no real money is involved which implies that using this accounting entry allows commercial banks to create money without having money in the first place. More so, this research has also uncovered respondents' opinions on other possible alternatives for alignment of accounting treatment of commercial banks' money creation. Respondents suggested two proposals. A few respondents have the opinion that fiat money should be removed from the monetary system and money backed by real assets like gold and silver should be issued and controlled only by BNM. Along with the above alternative, other respondents highlight that the accounting entry for commercial banks' money lending needs should be similar to the accounting entry of non-bank or trading institutions. Hence, the scope of commercial banks to create money in the lending system will be reduced.

A study of stakeholders' perception is of crucial importance for money lending activity. In addition, findings of this study may stimulate the chief regulatory body like BNM, the central bank of Malaysia, to be more cautious in controlling commercial banks' money lending activity in order to prevent the future crisis. Furthermore, the findings may help to explain conflicting concepts of accounting treatment of money lending activities for Fractional Reserve Banking (FRB) under current commercial banks' practice as compared to the explanations given in text books. Finally, in view of the scarcity of literature on this research matter, this research can become the basis of essential study for future research. In addition, future studies can look at views of the key regulator (e.g. BNM) on this research issue along with the other respondents' arguments. Since the practical operation is different from the academic explanation on this research issue; hence, further research can be carried out to explore the practical aspect on this research matter which may provide a more comprehensive view of money creation through the accounting treatment.

Abstrak tesis yang dikemukakan kepada Senat Universiti Putra Malaysia sebagai memenuhi keperluan untuk ijazah Master Sains

PERSEPSI KE ATAS PENCIPTAAN WANG DAN IMPAK RAWATAN PERAKAUNAN BAGI AKTIVITI PEMINJAMAN WANG OLEH BANK-BANK KOMERSIAL DI MALAYSIA

Oleh

MD SHAMIM HOSSAIN

Julai 2018

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Telah terbukti secara empirikal dari kajian awal bahawa bank komersial secara individu dapat mencipta wang apabila mereka memperkenalkan pinjaman baharu. Apabila bank-bank memperkenalkan pinjaman baharu mereka tidak perlu menunggu pelanggan membuat deposit, sebaliknya mereka hanya menggunakan kaedah perakaunan yang mudah untuk mewujudkan pinjaman dan memindahkan jumlah pinjaman ke dalam akaun peminjam. Penciptaan kredit mudah ini adalah salah satu penyebab utama berlakunya krisis kewangan global 2007/2008. Bank-bank terus mencipta wang melalui pemberian pinjaman dengan cara ini kerana selama berdekad tiada sesiapa atau pihak kerajaan telah membangkitkan mengenainya. Di samping itu, lebihan bekalan wang daripada deposit simpanan bank komersial yang terkumpul boleh menyebabkan penurunan nilai mata wang Ringgit Malaysia. Bekalan wang berlebihan melalui penciptaan kredit yang terkumpul boleh menyebabkan inflasi. Malah, hubungan antara hutang, bekalan wang dan inflasi bukan hanya berlaku di Malaysia tetapi juga di negara-negara lain. Tambahan pula, sebahagian besar wang di Malaysia disandarkan kepada hutang. Daripada kunci kira-kira kewangan Ringgit jelas menunjukkan bahawa wang fiat adalah 99.6% disandarkan kepada hutang. Amalan semasa pemberian pinjaman wang oleh bank-bank komersial membawa kepada peningkatan dalam penciptaan kredit yang menunjukkan terdapat potensi berlakunya kepada krisis kewangan. Kajian ini bertujuan untuk meninjau persepsi pihak berkepentingan mengenai kesan rawatan perakaunan terhadap aktiviti pemberian pinjaman wang oleh bank-bank komersial.

Pendekatan fenomenologi telah digunakan untuk meninjau persepsi pihak berkepentingan melalui perkongsian pengalaman mereka. Pendekatan wawancara separuh berstruktur telah digunakan untuk mengumpul data. Tujuh individu dari

pelbagai kumpulan berkepentingan telah ditemuramah dengan persetujuan awal mereka. Untuk analisis data, kajian ini telah menggunakan pendekatan tematik induktif.

Penemuan kajian ini menunjukkan bahawa persepsi tentang penciptaan wang dipengaruhi oleh pemahaman dan kesedaran responden mengenai isu kajian. Responden bersetuju dengan rawatan perakaunan (Debit Pinjaman dan Deposit kredit) tetapi mereka menjelaskan kesan dari rawatan perakaunan ini dengan cara yang berbeza. Terdapat petunjuk yang kukuh bahawa penciptaan wang berlaku di Malaysia seperti di negara lain dan ia berlaku melalui rawatan perakaunan dalam aktiviti pinjaman wang oleh bank-bank komersial. Di samping itu, mempunyai peluang untuk menggunakan rawatan perakaunan, bank-bank komersial mampu menghasilkan wang yang mereka kehendaki, dan seterusnya lebihan wang yang dicipta menyebabkan inflasi yang akhirnya berpotensi menimbulkan krisis kewangan. Bertentangan dengan kepercayaan ini, penciptaan wang dikatakan adalah hasil daripada pendekatan sistematik perbankan rizab pecahan di Malaysia. Menurut hujah ini, penciptaan wang bukanlah ancaman kepada ekonomi selagi ada peranan kawalselia yang kuat oleh Bank Negara Malaysia (BNM). Oleh itu, adalah jelas dari perbincangan responden bahawa penciptaan wang akan menimbulkan cabaran besar kepada ekonomi jika peranan kawalselia oleh BNM semakin lemah.

Di samping itu, responden percaya bahawa rawatan perakaunan bagi aktiviti pemberian pinjaman wang oleh bank-bank komersial mempunyai beberapa kesan terhadap ekonomi. Pertama, responden mendakwa bahawa penciptaan wang melalui pemberian pinjaman adalah penipuan besar kerana hanya bank komersial swasta yang boleh menggunakan rawatan perakaunan ini (debit pinjaman dan akaun pelanggan / deposit) sementara institusi lain tidak boleh menggunakan rawatan perakaunan ini. Kedua, responden menyatakan bahawa sistem pinjaman ini bersama-sama dengan rawatan perakaunan telah mewujudkan sistem monetari berasaskan hutang. Ini adalah kerana, semasa rawatan perakaunan terdapat penciptaan deposit yang sepadan untuk pinjaman yang dilanjutkan, oleh itu tidak ada wang sebenar yang terlibat yang menunjukkan bahawa menggunakan entri perakaunan ini membolehkan bank komersial menghasilkan wang tanpa mempunyai wang langsung semenjak awal. Malahan, kajian ini juga telah menemui pendapat responden mengenai alternatif lain yang mungkin boleh digunakan untuk menjajarkan rawatan perakaunan dalam penciptaan wang oleh bank komersial. Responden memberikan dua cadangan. Beberapa responden berpendapat bahawa wang fiat harus dikeluarkan/disingkirkan dari sistem monetari dan digantikan dengan wang yang disandarkan kepada aset sebenar seperti emas dan perak serta dikawal hanya oleh BNM. Bersama dengan alternatif di atas, responden lain menekankan bahawa entri perakaunan bagi keperluan pinjaman wang oleh bank komersial harus sama dengan entri perakaunan oleh institusi perdagangan bukan bank yang lain. Oleh itu, ruang bagi bank komresial untuk mencipta wang dalam sistem pemberian pinjaman akan dapat dikurangkan.

Kajian mengenai persepsi pihak berkepentingan adalah sangat penting bagi aktiviti pinjaman wang. Di samping itu, penemuan kajian ini boleh merangsang badan kawalselia seperti BNM, sebagai bank pusat Malaysia, untuk lebih berhati-hati dalam mengawal aktiviti pinjaman wang oleh bank komersial untuk mengelakkan krisis kewangan pada masa depan. Penemuan ini juga dapat membantu menjelaskan konsep yang bertentangan dengan rawatan perakaunan dalam aktiviti pemberian pinjaman wang bagi perbankan rizab pecahan di bawah amalan semasa bank-bank komersial berbanding dengan penjelasan yang diberikan dalam buku teks. Akhir sekali, memandangkan kekurangan literatur mengenai topik yang dibincangkan, kajian ini boleh menjadi asas penting untuk penyelidikan masa depan. Di samping itu, kajian masa depan boleh melihat pandangan badan kawalselia utama (contohnya BNM) mengenai isu kajian ini bersama dengan hujah responden yang lain. Oleh kerana operasi secara praktikal adalah berbeza daripada penjelasan akademik mengenai isu kajian ini, kajian lanjut boleh dijalankan untuk meneroka aspek praktikal mengenai isu kajian ini yang dapat memberikan pandangan yang lebih komprehensif mengenai penciptaan wang melalui rawatan perakaunan.

ACKNOWLEDGEMENTS

In the name of Allah, the most Gracious, the most Compassionate

First and foremost, syukur Alhamdulillah, All praise to Allah S.W.T for his blessings that make this testing journey come to an end. And, All praise to our greatest and beloved Prophet Muhammad P.B.U.H.

My sincerest gratitude to my advisor and supervisor Dr. Ahmed Razman Abdul Latiff and Dr. Mohammad Noor Hisham Bin Osman for the spark that ignite my interest in this field. Their endless support, patience, motivation, and immense knowledge have helped me in all the time for the research and writing of this thesis.

Special thanks to my beloved parents, wife and daughter for their persistent support and prayers and encouragement.

I certify that a Thesis Examination Committee has met on 20 July 2018 to conduct the final examination of Md Shamim Hossain on his thesis entitled "Perception of Stakeholders on the Impact of Accounting Treatment for the Commercial Banks' Money Lending Activity in Malaysia" in accordance with the Universities and University Colleges Act 1971 and the Constitution of the Universiti Putra Malaysia [P.U.(A) 106] 15 March 1998. The Committee recommends that the student be awarded the Degree of Master of Science.

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On behalf of,
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Declaration by graduate student

I hereby confirm that:

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This is to confirm that:

- the research conducted and the writing of this thesis was under our supervision;
- supervision responsibilities as stated in the Universiti Putra Malaysia (Graduate Studies) Rules 2003 (Revision 2012-2013) were adhered to.

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BNM	Bank Negara Malaysia
GFC	Global Financial Crisis
FRB	Fractional Reserve Banking
IFRS	International Financial Reporting Standards
IIUM	International Islamic University of Malaysia
INCEIF	International Centre for Education in Islamic Finance
MASB	Malaysian Accounting Standard Board
MIA	Malaysian Institute of Accountants
MOFM	Ministry of Finance of Malaysia

CHAPTER 1

INTRODUCTION

1.1 Background of the Study

Money determines the flow of business in human lives in the modern world. It plays a significant role in the operation of the national and international economy. Defining money is always faced with complexity from a historic point because over several generations, money has changed its shape, nature of use, creation and circulation systems, as well as its recording systems. Moreover, the form of money kept by the people is difficult to define it and there has been no consistency on the origins of money. In the barter system people do not require payment in money as a medium of exchange; rather they exchange goods or services directly for other goods or services and even creditworthiness of buyer is not essential for the economy especially in hyperinflation situation where money devalues quickly (Humphrey, 1985).

Subsequently, commodity money replaced the barter system because in the barter system experienced issues, for example, no standard of exchange, indivisibility of goods, the double coincidence of wants, and insufficient storing capacity of goods. Generally, accepting goods as a medium of exchange has assisted the commodity money to lead the trading systems because the intrinsic value of commodity made it more reliable to the people. As economies developed, complexity of carrying commodity money along with credit expansion had forced people to use the representative money. This money could be exchanged for a fixed amount of valuable commodity, usually gold or silver using a specified standard (Jevons, 1875).

However, the problem with representative money is that its acceptance depended on the reputation of the issuer that ultimately led to the fiat money which has no intrinsic value and cannot be redeemed for specie; rather its value originates from government decree. After declaring fiat currency by the government, it is then considered as a legal tender; hence, rejecting fiat currency as a payment mode is considered unlawful (Deardorff, 2008; Black, 1910).

In the economy, fiat money worked through three different formats; currency, bank deposit and central bank reserves and all these are functioning as an IOU (I owe you) from one to another (McLeay, Radia, and Thomas, 2014a). In modern economy there are misconceptions about money creation in the sense that a) banks act simply as intermediaries, lending out the deposits that savers place with them, and b) the central bank determines the quantity of loan and deposits in the economy by controlling the quantity of central bank money - the so-called ‘money multiplier’ approach (McLeay, Radia, and Thomas, 2014b). McLeay et al., (2014b) investigated the first misconception and found that commercial banks are creators of deposit money because banks create the deposit money through its accounting treatment while it grants loan to the customer and the simple journal entry for that transaction is debit the loan and credit the deposit.

debit and credit identification of this particular transaction. The term "deposit" means money deposited by an investor or general people to his bank account. Here, the owner of this deposited money is the person or entity who deposits it to the bank's account and such depositor has the right to withdraw his deposited money in accordance with the agreement with the banks. This deposit is a liability for the banks as per definition of the accounting standard because the bank has a contractual obligation to deliver cash as per the terms of the loan agreement to the account holder. However, the accounting equation, Assets = Liabilities + Equity (A = L + E), can reflect every transaction that impacts either two sides in the same direction (increase or decrease) or one side in opposite direction (increase and decrease in same account or multiple accounts). For example, when deposit is received from the customer, two things will be changed in the bank's recording process (Table 1.1): the bank's vault cash (asset) increases, which is a debit; the increase in the customer's account balance (liability) is a credit.

Table 1.1 : Recording process by the bank for customers' paid deposit

Journal for Deposit by the people to bank	Accounting Equation Impact
Cash ………………………..Dr. *Deposit …………...............Cr.	+Cash (Assets) = +Deposit (Liabilities)
* This is real deposit money.	

In this transaction, cash is considered as assets to the bank which matches the definition of International Financial Reporting Standards (IFRS) because cash represents itself an asset as cash, as an equity instrument of another entity (customers') and there is a contractual right to exchange financial assets for example cash (principal plus interest) with another entity (customers). At the same time, the deposit in the same transaction refers to a liability for the bank because it consists of a contractual obligation to deliver cash (principal plus interest) to another entity (customers). On the other hand, banks' created deposit through the accounting treatment for money lending is not a normal deposit but rather it is a reclassification of account payable for the account of loan borrower and Werner (2014a) explained it more precisely:

> The bank reduces its 'account payable' item by the loan amount, acting as if the money had been disbursed to the customer, and at the same time it presents the customer with a statement that identifies this same obligation of the bank to the borrower, but now simply reclassified as a 'customer deposit' of the borrower with the bank.

> The bank, having 'disbursed' the loan, remains in a position where it still owes the money. In other words, the bank does not actually make any money available to the borrower. No transfer of funds from anywhere to the customer or indeed the customer's account takes place.

Furthermore, this bank's created deposit through lending does not match the definition of normal deposit because deposit indicates that money is owned by the customer not the bank, but in case of loan, the owner of money is owned by the bank, hence, in the same time money cannot be owned by the both parties (bank and account holder). According to Werner (2014b), the bank creates an imaginary deposit when extending credit though there is no new deposit taking place and there is no scope to create this deposit for other institutions (Table 1.2). Therefore, the bank‘s practice is to classify the customer loan as a deposit which is created out of thin air, and result of study shows that 97% of the money held by the public counts as the bank deposits money rather than currency (McLeay et al., 2014b; Wolf, 2014) that the maximum portion of the broad money is on the bank recording process, not the real paper currency.

Table 1.2 : Changes in the balance sheets of companies, non-bank financial intermediaries and banks after the accounting of loans

Company		Non-bank financial intermediary		Bank	
Assets	Liability	Assets	Liability	Assets	Liability
Loan: +100		Loan: +100		Loan: +100	Client's current account balance +100
Deposit: -100		Deposit: -100			
Balance: 0.00	0.00	0.00	0.00	+100	+100

(Source : Werner 2014b:73)

However, earlier studies including Wicksell (1898 and 1907), Withers (1909), Schumpeter (1912), Hahn (1920), Faure (2013) and Jha (2013) among others mostly focused on the theoretical explanation of the accounting treatment for money lending activity. In addition, few studies including McLeay et al., 2014b, Ryan-Collins, Greenham, Werner, & Jackson, 2011, Ábel, Lehmann and Tapaszti, 2016, and Faure & Gersbach, 2016 among others discuss the economic and financial consequence of money creation. Very few studies have explained money creation together with the accounting issue and only one study (Werner, 2014a) provides empirical proof along with the impact of money creation through the accounting treatment. Therefore, this study will consider empirical evidence from this particular study (Werner, 2014a). This limitation is one of the major motivations for carrying out this study. Werner's (2014a) study considered the accounting journal entry for credit transaction as shown in Table 1.3; that is, debit loan and credit deposit.

Table 1.3 : Accounting journal entry for a credit transaction though which commercial banks create money

Journal for Loan given by the bank to the people
Loan ……………………………..Dr. ** Deposit …………................Cr.
**This is bank created deposit.

Werners' study (2014a) considers the impact of the loan transaction on the balance sheet for granting loan to identify which theory is going to be reflected through the said transaction:

> There is no equal reduction in the balance of another account to delay (to provide money to pay) the borrower. Instead, the bank simply re-classified its liabilities, changing the 'account payable' obligation arising from the bank loan contract to another liability category called 'customer deposits'.

One of Werner's findings (2014a) shows that the accounting treatment for granting loan matches with the transaction as shown in Table 1.3 that bank creates the matching deposit for granting loan out of thin air and this result is consistent with the credit creation theory's principle. This credit creation feature is the unique ability of the commercial banks (Stoop and Sornette, 2010) that allows them to create money through the accounting treatment. Generally, commercial banks extend the loan to customer (borrower) in deposit form which increase the deposits instantaneously in the bank and this practice of commercial banks help to achieve money creation (Xi, Ding, & Wang, 2005).

In addition to the above accounting treatment for money lending (Table 1.3), we can also look at another accounting treatment on one of bank's products, namely housing loan. Referring to Table 1.4 below, no real cash movement has occurred between the buyer and seller account, but the balance sheet is expanded in both assets and liabilities and, hence, money is created. Therefore, without initial cash disbursement, commercial banks can create credit during lending activity which ultimately turns into money creation.

Table 1.4 : Accounting journal entry for a credit transaction of housing/car loan though which commercial banks create money

Journal for House/Car Loan given by the bank to the people
Loan (House/Car Buyer)Account……………………………..Dr. *** (House/Car) Sellers Account …………................Cr.
***This is bank created money, no cash transfer either for customer or seller.

Empirical evidence shows that money lending took less than an hour (35 minutes only) to complete the money creation out of thin air through the accounting treatment (Werner, 2014a). It was claimed that this practice has an economic consequence because it allows banks to exercise an uncontrolled money creation (Stiglitz and Weiss, 1988) through lending within an hour. In addition, it can make any money into debt in the economy (Ravn, 2015) as commercial banks can extend loans whenever they want.

Consequence of this money creation in the socio-economic environment makes it more crucial for the stakeholders to understand this issue. This practice (commercial banks' credit creation activity) has been tremendously criticized for causing the global financial crisis (GFC) during 2007- 2008 and this has also been acknowledged by the different group of stakeholders such as academia, business and politics (Acharya and Richardson, 2009; Farhi and Tirole, 2012; Kashyap et al., 2008; Liikanen, 2012; Stiglitz, 2009; Vickers, 2011).

It is claimed that enjoying this easy credit creation by the commercial banks has a major contribution, especially in enhancing inflation (Turner, 2012; Li et al., 2016), because greater expansion in currency supply in the economy leads to faster rise in the price of commodities; thus reducing the purchasing power of money leading to greater inflation. More so, banks are unable to get back their money in full because the price of houses and land do not reflect maturity price. This led to banks' liquidity crisis and issuing new home loans became increasingly difficult. This was the major contributor to the fallout from the sub-prime lending bubble. Therefore, the perceptions of the stakeholders on this issue may help to respond positively for the potential future economic consequences such as GFC 2007/2008.

Considering the significance of this phenomenon, discussion and debate have been going on all over the world. The Klynveld Peat Marwick Goerdeler (KPMG), one of the largest consulting firms in the world, had published an official report in September 2016 in their official website regarding political development in the developed countries on the nature of money and money creation since 2008. This report was commissioned by the office of the Prime Minister of Iceland.

According to the said report, The United States of America is trying to restore the authority for creating money to a Monetary Authority and as a result an act was formulated in December 2010 and September 2011. It was referred to the Committee on Financial Services, but it was not passed into law. For the first time in 170 years' a significant debate was held in the UK parliament on November 2014 on the topic of "Money Creation and Society". In the debate they proposed the formation of a monetary commission, but the proposal did not get voted on in parliament.

This KPMG report also stated that the Iceland Parliament had proposed a resolution in September 2015 for the establishment of a commission to carry out a review on the procedure of money creation in Iceland. Though most of the committee members (8 out of 11) supported the resolution, the Icelandic Financial Services Association reiterated its view and insists to follow the pattern of the European Economic Union. Also in December 2015, Switzerland was looking into conducting a referendum to decide whether to ban commercial banks from creating money or not. The Swiss government wanted to stipulate that the central bank be given the sole power to create money in the financial system. Following the announcement of a referendum which was held in 2016, both Federal Council and Swiss Bankers' Association made an initial reaction to reject the Swiss Sovereign Money Initiative. Lastly, The KPMG report covered development of financial services in Netherland. On March 16, 2016, the Dutch Parliament's plenary assembly discussed the possibility of transitioning towards a sovereign monetary system and consequently, the Assembly adopted two motions committing the government to carry out further research.

1.2 Problem Statement

Since, the practice of commercial banks' lending and its accounting treatment are identical all over the world, it can be assumed that similar practices are supposed to be conducted in Malaysia as well. This identical practice may raise the opportunity of deposit money creation through accounting treatment during commercial banks' money lending activity. Furthermore, creating of deposits by commercial banks does not match with the definition set by the Bank Negara Malaysia (BNM) in the Financial Service Act 2013. The Central Bank of Malaysia (BNM) established the definition of deposit for the banking business which stipulates that deposit is collection of money owned by the outsider (customer) and banks have to repay it. As per section 2(1), Financial Service Act 2013:

> Deposit means a sum of money received or paid on terms- under which it will be repaid, with or without interest or at a premium or discount.

Therefore, deposit money created by the commercial banks' lending activity raises the question that whether this created deposit money follows the definition set by the BNM. In addition, as per the law ((see section 62(1), Central Bank of Malaysia Act 2009), BNM is the only statutory body empowered to issue and print money. The Rules and Regulations of BNM have given the BNM power to control the commercial banks' money lending activity. For example, BNM, with prior approval from the Ministry of Finance, can take control of the entire or partial business of any commercial banks (see Financial Service Act 2013, section 167 (1)). From the above discussion, the fundamental question for this research study is that, despite the absolute power of BNM to control the commercial banks' money lending activity, how is it possible for commercial banks to conduct the money creation activity through the accounting treatment during money lending activity? This study looks at this question from the stakeholders' perceptions.

While major developed countries of the world are researching the issue, debating on the alternatives to commercial banks' money creation practice, and considering all the stakeholders' opinion, developing countries such as Malaysia are still conducting a few studies. Relevant documents published and issued by various sources including academia, financial institutions, private individuals among others, have confirmed the commercial banks' money lending practices (Salleh and Borges, 2015). Since commercial banks' money lending activity is identical throughout the world, Malaysia is not an exception. In addition, conventional deposit money creation through commercial banks' money lending activity has a major effect on financial instability in Malaysia (Abdullah, 2015). More so, excess supply of money as a result of accumulated commercial banks' deposit has led to the devaluation of Malaysian *Ringgit*. Earlier studies revealed that excessive money supply through accumulated credit creation has resulted in inflation and Malaysian fiat money (*Ringgit*) has been losing its purchasing power gradually since the adoption of fiat standard in 1970 (Abdullah, 2015). In fact, relationship among debt, money supply and inflation is not only true for Malaysia but also for other countries (Yasmin &Waqar, 2013). However, though BNM is supposed to maintain the value of *Ringgit* as per the Central Bank Act of 2009 but it is finding it increasingly difficult to do so. This is because fiat money in Malaysia is largely backed by debt. From the monetary balance sheet of the *Ringgit* (Table 1.5), it is apparent that fiat money is 99.6% backed by debt. The current practice of commercial banks' money lending activity is promoting a similar trend of credit creation (Table 1.6) which indicates that there are threats of potential financial crisis. Therefore, raising the question on the current commercial banks' practice makes this study more relevant especially by making the stakeholders re-think about this phenomenon in order to prevent potential future long term economic crisis such as GFC 2007/2008. In order to get better understanding of the research issue, this study examines stakeholders' perception regarding the money creation practices in Malaysia.

Table 1.5 : The monetary balance sheet of the *Ringgit* (RM) as at 31st December 2014

			(RM Billion)
Assets	RM	Liabilities	RM
Gold IOUs Owed to Banks	5.2 1,548.6	BNM Currency Bank Deposits	68.2 1,485.6
	1,553.8	M3	1,553.8

(Source : Abdullah 2015)

Table 1.6 : Balance of M3 and Gold as at 31st December 2016

Items	RM (Billion)
A.BNM Currency B. Bank Deposits	85.5 1,557.0
M3 (A+B)	*1,642.5*
Gold	6.4

(Source : BNM Annual Report, 2016)

Despite all the significant consequences of commercial banks' money creation, the earlier studies are still searching for unique alternatives that can be aligned with the different accounting treatment of commercial banks money lending activity. Unique alternative refers to any alternative that can merge different alternatives suggested by the earlier studies. Alternatives based on earlier studies include converting the bank notes into gold and the intensification of central banking (Faure, 2013), "full reserve banking" under gold standard (Huerta, 2009). There are also calls for an absolute discontinuation of this fictitious deposit money creation (Salleh and Borges, 2015 and 2016). On the other hand, studies are still supporting the commercial banks' money creation as they claimed that this money creation is backed by the existing (collaterals) assets and confidence in future cash flows (Becke and Sornette, 2014). In addition**,** they have also suggested that if commercial banks' money creation is stopped, it will lead to a collapse of the economy as the economic boom situation is influenced by the continuation of credit expansion, and hence, money creation is not excess of demand over supply in the economy (Becke and Sornette, 2014). Therefore, these conflicting arguments make it challenging in finding possible alternatives that will align the different accounting treatment regarding the commercial banks' money creation practices. However, seeking possible alternatives that will align the different accounting treatment for banks' money lending activity is absolutely dependent on stakeholders' awareness and understanding on the issue.

1.3 Objectives of the Research

The objectives of the Research are as follows:

i. To understand the perception on practice of money creation in Malaysia.
ii. To understand the perception on the impact of the accounting treatment for commercial banks' money lending activity in Malaysia.
iii. To explore possible alternatives in order to align the different accounting treatment regarding commercial banks' money lending activity in Malaysia.

1.4 Research Questions

The key questions that need to be answered to achieve the above objectives are as follows:

i. How do stakeholders perceive money creation practice in Malaysia?
ii. How do stakeholders perceive the impact of accounting treatment for commercial banks' money lending activity in Malaysia?
iii. What are the possible alternatives available that will align the different accounting treatment for commercial banks' money lending activity in Malaysia?

1.5 Contribution of the Research

Banks have to create money through lending and neither consumers nor governments have questioned their money lending activity over the decades. However, commercial banks' credit creation activity was one of the major reasons for the GFC 2007/2008 (Turner, 2012; Salleh and Borges, 2105). Even with them knowing, policy makers failed to stop the bank's easy credit creation and still this money creation practice continue to flourish. In terms of contribution, this study can contribute to the existing literature because it examines the reason behind the continuation of the commercial banks' money creation activity by analysing stakeholders' perceptions. Findings of this study have shown that stakeholders have different perceptions regarding the impact of accounting treatment on money creation and the variation in perceptions is due to their own awareness and understanding of the research issue. Majority of them have admitted that money creation is happening in Malaysia like in other countries, but the explanation for this money creation along with accounting treatment is different. Some of them believed that due to the effective role of BNM, money creation may not be a threat as long as BNM has control over it. Contrary to this claim, others argued that there are no pre-existing loanable funds; rather banks provide financing through money creation and for this, banks merely make bookkeeping transactions, without actual resources (Jakab and Kumhof, 2015).

In addition, findings of this study on matters relating to money creation issue can help the regulatory body because these findings can be used as an input to the process of accelerating the BNM's controlling role for the commercial banks money lending activity in order to prevent the future potential crisis like GFC 2007/2008.

In addition, findings of this study can benefit the academics to explain the conflicting concept for commercial banks' money creation through accounting treatment because this research explores the basic understanding of money lending though accounting treatment from the respondents' banking experience. It may also be helpful in bridging the gap between the text book's explanation for Fractional Reserve Banking (FRB) and current commercial banks' money lending practices which is not covered in earlier studies of commercial banks' lending activity.

In view of the scarcity of literature on this research issue, this research will provide the essential study for future research by providing valuable and beneficial information on the impact of accounting treatment of commercial banks' money lending activity in actual practices.

1.6 Definition of Key Terms

SL No.	Key terms	Definition
01	Stakeholders	An individual, group of people or organization that has interest or concern in a specific organization. The activities, policies or objectives of the organization can affect the shareholders or vice-versa. In this study, stakeholders included the Administrative and Diplomatic Service (ADS) officers, Academic, Banks' Officers, and Members of Malaysian Institute of Accountants (MIA). How the interests of each of the above stakeholders are related has discussed in the chapter three.
02	Credit Creation	Credit refers to the money borrowed from one to another. Credit creation is the unique feature of commercial banks (Stoop and Sornette, 2010). It allows the commercial banks to create money through the accounting treatment during lending activity. When the commercial banks extend new credit to its customer in a deposit form, instantaneously deposit has expanded which ultimately turns into money creation (Xi et al., 2005).
03	Accounting Treatment	Treatment means application of applicable Accounting principles, weather its international Financial Reporting Standard/ US GAAP/ UK GAAP/ or Local regulations governing the accountancy in country of jurisdiction.
04	(FRB)	FRB works on the money multiplication form that based on the customers' savings. Here, money is collected from the customer deposit and then extend the loan after keeping a certain amount of fraction as a reserve. Banks can create loans and multiply the amount to money circulation in the economy. FRB posits that availability of deposits and minimum reserve requirement as per law can limit the amount of multiplication and lending (Becke and Sornette, 2014). Here money multiplication impact is the collective efforts of all commercial banks together; one commercial bank cannot do it alone (Huerta, 2009).

05	Deposit	Deposit indicates the money collected from the outsider (customer) of commercial banks which will be repaid with or without interest within the certain period of time as per agreement between the customer and the commercial banks. As per the section 2(1), Financial Service Act 2013:Deposit means a sum of money received or paid on terms-a) under which it will be repaid, with or without interest or at a premium or discount.
06	Deposit Money	The money kept as deposit in the customer accounts inside the bank. Deposit money is appeared in the liability side of the balance sheet of the commercial bank because this deposit has to repay as per the agreement between the commercial banks and its customer. However, as per research, more than 95% of the money is kept as deposit in the entire money circulation.

1.7 Thesis Structure:

This study is organized in five main chapters. In the first chapter, this study covers the background of the study, problem statement, research objectives, research questions and research contribution. Chapter two covers the Literature Review along with the theoretical underpinning. Chapter three covers the research design in detail including research method, data collection method and data analysis method. Chapter Four focuses on the Discussion and Analysis of the data followed by the identified themes. Finally, Chapter Five presents the summary of findings, implications of the findings, limitations of the study and future research direction followed by the conclusion.

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