Money and Liberty

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The U.S. monetary system has been a scandal for a long time; whether it can continue much longer without intolerable social, political, and ecological consequences is an open question. Yet most Americans don't have a clue about it. "It is well enough that people of the nation do not understand our banking and monetary system," Henry Ford said, "for if they did, I believe there would be a revolution before tomorrow morning."

Our current monetary system, to be blunt, is an unjustified monopoly granted to private interests to create public money for their private profit. For this they charge the public usurious (extortionary) rates of interest, creating an economic system that unnecessarily transfers wealth from debtors to creditors as it forces often needless and wasteful economic "growth."

The idea that a national currency should be a debt incurred by governments (and therefore taxpayers) to private interests for their profit was first institutionalized with the Bank of England at the end of the seventeenth century, and subsequently developed in the United States by Alexander Hamilton and his successors. Under this scheme, the power to "create" money is granted as a monopoly to a central bank, like the Federal Reserve, which then lends the money so created back to the government at interest in return for government bonds. These bonds are then sold to commercial banks, where they form the collateral for loans to the public, at additional rates of interest. As the agent of the major private banks, the Federal Reserve not only regulates the economy by raising and lowering interest rates to control the money supply and to protect creditors but also guarantees the private banks' monopoly over the further creation of money through fractional reserve lending.

This system, now triumphant worldwide under the rubric of "globalization," with the dollar as the world's reserve currency, has made possible, perhaps more than any other factor, the relentless concentration of wealth into fewer and fewer hands. Yet this money system is mostly ignored by social critics. Crucial to this system is the power given to the central banks and the banking system in general to vary interest rates freely and without limit. Interest charged beyond administrative and risk insurance costs is usurious. Such usurious interest constitutes the income of the banking system, the profit from which goes to the private investors in that system, not to the public. This institutionalization of usury allows the banking system to skim off what is essentially a private tax in return for providing what should be a free public service. It creates a system in which money is scarce and available only at a steep price.

Most Americans believe the Federal Reserve is accountable to the public interest, but nothing could be further from the truth. Although the Governors of the Federal Reserve are presidential appointees confirmed by Congress, when we consider their long fourteen year terms, the byzantine and secretive traditions of the Fed, its lack of any other public accountability (apart from the Chairman's reports to Congress), and the strong Fed role played by commercial banks (who sit both on the Federal Open Market Committee, which sets interest rates, and on the boards of regional Fed branches), it is hardly surprising that the Fed has been able to enjoy a gloss of public accountability while evading public control.

Economic inequality is rooted in a maldistribution of capital. The only access to capital today for those without is to borrow money at interest. Anyone with a mortgage, a car loan, a student loan, or a

credit card, is paying a hefty private tax to the banking and financial system for the right to use capital, which, as a public resource, should be freely and fairly available to the public. Being forced to borrow money at interest, individuals and businesses must pay off significant interest charges as well as the principal before they can see any of the fruits of their use of that money. Why should the banking system be allowed the monopolistic privilege, not only of creating money, but of charging excessive interest for the right to do so? Should not the creation of money, essential to the public welfare, be a proper matter for government, assuming democratic, publically accountable governments (which we currently do not have)?

This burden of usurious interest is the real engine behind economic "growth." Since borrowers must repay interest on top of principal before realizing any benefit from a loan, they are forced to additional labor and production. Money borrowed at 6 percent, compounded annually, will accumulate interest equal to the principal in only twelve years. This is insignificant at small amounts, but if I borrow $100,000 at 6 percent, it means I must pay my creditor a total of $200,000 within twelve years, which amounts to $16,666 a year. By contrast, at a nominal 1 percent interest rate, it would take 70 years before the interest burden equaled the principal, and it would cost only $2857 a year over that period to repay the $100,000 loan.

There is no reason that interest must be charged for the creation of money. There is no need to "rent" money from private bankers when we could just as easily create it ourselves at nominal cost. To do so would constitute a political revolution of the first magnitude. Traditional attempts to meet the challenges of social and ecological exploitation (socialism, communism, environmentalism) have failed insofar as they have not understood the underlying usurious monetary system that drives "growth." By contrast, nonusurious monetary policies in the hands of democratically accountable governments serving the public interest would be able, for the first time, to correlate the use of money with social needs.

The Constitution prohibits the states not only from coining money but from emitting bills of credit or making "anything but gold and silver Coin a Tender in Payment of Debts." (Article I, Sec. 10) Given the failure of Federal monetary policy, its ruinous effects in exploiting persons and nature, and its key role in creating great relative wealth for a few and great relative poverty for many, it is incumbent to insist upon a devolution of monetary policy to the local level, whether this occurs through reform of Federal monetary policy, through Constitutional Amendment returning monetary policy to the various states, or through the secession of various states from the Union. It is essential to this end to understand how a nonusurious, publically accountable currency might work.

The most thoroughgoing and ingenious system of such a currency was thought out before the Civil War by Edward Kellogg (1790–1858), and is perhaps stated best in his posthumous work, *A New Monetary System* (1861, reprint 1970). Kellogg was a forerunner of free bankers and populists who mostly missed, however, his central idea of a decentralized non (or nominal) interest currency. He proposed to establish local public credit banks, one in each county. These banks, Federally mandated but locally run, would offer nominal (1 percent) interest loans to resident citizens. Kellogg envisioned land as collateral, but credit worthiness could be based, as it is today, on one's potential earning power. Once lent out, Kellogg's public credit dollars would flow into circulation, providing the basis of a new currency, backed by the productive labor power of individual borrowers. Individuals and private banks would be free to reloan public credit money at higher rates of interest, but the availability of nominal 1 percent loans would undercut their ability to charge usurious rates.

The beauty of Kellogg's system is its decentralized self-regulating nature. Instead of credit issued on a top-down basis from a central bank to national banks, and then to regional and local banks, all charging usurious rates of interest for the privilege of borrowing money they create without effort, credit would be issued by local banks directly to local citizens without interest on the basis of the economic prospects of those citizens. These prospects would vary considerably from place to place, with some areas needing and creating more currency than others. But whatever currency is created

would be equivalent to any other. The solvency of local public credit banks would be guaranteed by adequate reserve requirements, and the money supply would be stabilized by repayment of loans as they came due. The interchangeability of public credit bank notes would ensure a wide circulation for the new money.

Kellogg's public credit banks are a form of free banking, but done as an interest-free public service rather than as a private for-profit enterprise. Capital would become cheaply and widely available at local public credit banks to anyone minimally creditworthy. Students, for instance, could take out public credit loans instead of student loans. Public credit banks could offer no-interest credit cards. Homebuyers could take out public credit loans instead of mortgages. Small business (sole proprietorships and partnerships) could take out public credit loans instead of borrowing money from commercial banks. Corporations, however, would not be able to borrow from public credit banks, whose purpose is to serve the interest of flesh-and-blood citizens, not corporate entities. The latter would have to borrow on the secondary debt markets, at necessarily higher but still reasonable interest rates. No public credit currency would be issued at any other than the local level. National standards would determine uniform rules of creditworthiness, minimum reserve requirements, local public management, and a fixed nominal (1 percent) rate of interest. A local public credit bank issuing too many bad loans, or refusing loans to otherwise creditworthy citizens, would be subject to legal penalties, including closure and reorganization.

Notice the profound implications of Kellogg's money system. There would be NO controlling central bank, no centrally controlled issuance of currency. The banking system would be set on its head. A bottom-up system of capital creation would replace the old top-down system. Most fundamentally, credit would be made available to the general public at a nominal (1 percent) interest rate, instead of being made available selectively to large commercial banks at high rates, who in turn lend it to others at even higher or usurious rates. With interest eliminated as a factor in monetary policy, the principle engine of wasteful and compulsive economic growth would be eliminated. There would be no need to labor frenetically to overcome the interest burden. Economic investment would be possible on the merits of the situation, not on an abnormally forced rate of return. A sustainable economics would become possible, perhaps for the first time. And, not least, the widespread availability of capital to individuals (unknown since the closing of the Western frontier in America in 1890) would do much to overcome the vast and growing discrepancies of wealth that exist because of usurious interest rates.

Kellogg's model of a decentralized but democratically regulated monetary system is worth pondering, not only for financial and economic reasons, but for political ones as well. Democracy is necessarily a decentralized, face-to-face affair, and it cannot be successful unless its citizens personally enjoy relative economic independence in a relatively decentralized economy. For only then can they come together as equals in a free community. Most citizens today, however, are economic dependents, having been forced into debt peonage by usurious interest rates for most of the necessities of life (education, housing, transportation, etc.). Not being free economic agents, they cannot oppose the harsh and destructive economic system that oppresses them. A key step in developing such opposition is the realization that a decentralized, self-regulating, noninterest monetary system, of the sort outlined by Kellogg, can provide the basis for widespread economic independence.