

# IN WHOSE INTEREST?

***“Money is like an iron ring we put through our nose.  
It is now leading us wherever it wants.  
We just forgot that we are the ones who designed it.”***

Mark Kinney

Money matters. More specifically, the kind of currency used in a society and the manner in which money is created and administered, deeply molds values and relationships within that society by encouraging, or discouraging, specific emotions and behavior patterns. All money systems facilitate exchanges among people. But given the remarkable motivating power of money, whenever a specific money system is designed, it has invariably been loaded with a host of other objectives as well— sometimes conscious, oftentimes unconscious—from prestige of the Gods or a ruler to collective socio-economic motivations.

While payment and banking technologies (i.e., how we do things financially) have continued to dramatically change and improve, the fundamental objectives pursued by our current system (i.e., why we do them) have not been seriously revisited since Victorian England.

Indeed, *every* modern society, independent of its cultural or political background, has accepted the current money system. When the French and the Russian revolutions overthrew the established order in their countries, respectively in 1697 and 1917, they changed just about everything else—but not the money system. Both societies completely rebuilt their legal systems. The French overhauled the entire measuring system (the metric system dates from then), and even tried to change the calendar. The Russians threw out the very concept of private ownership and they nationalized the banks. But the money system remained exactly as before, with the only significant, or rather, *insignificant* difference being that the bills now adorned new mottoes and different heroes—but nothing else. When Mao’s communist takeover occurred in China, or when one hundred developing countries gained their independence over the past half-century, the same exact thing transpired.

To more fully appreciate the profound affects that our money has upon our lives, individually and collectively, and to appreciate the choices that are available to us, we must first understand what money actually is, and examine the rules of our current monetary game more closely.

## WHAT IS MONEY?

It is quite common when considering money to think of it in terms of its material representations. Down through the ages, money has definitely *appeared to be a thing*, in fact, an incredible variety of things. Without even mentioning the most recently prevailing forms of money, such as paper, gold, silver or bronze, Glyn Davies created a full money alphabet with a small selection of objects

which had this purpose: amber, beads, cowries, drums, eggs, feathers, gongs, hoes, ivory, jade, kettles, leather, mats, nails, oxen, pigs, quartz, rice, salt, thimbles, umiaks, wampum, yarns and *zappozats*—decorated axes.<sup>1</sup>

Money has indeed appeared to us in many material forms. However, money itself is *not* a thing.

### ***Money is Not a Thing***

A simple thought experiment distinguishes the aura of money from any, and all, things. Stranded alone on a deserted island, a *thing*—say a knife—is still useful as a knife. However, a million dollars in money, in whatever form it takes—cash, gold coins, credit cards, or even *zappozats*—*has ceased to be money*. It becomes paper, metal, plastic or whatever, but it is no longer money.

For any “thing” to act as money, it requires a community to agree that the particular object in question has a certain value in an exchange.

Events in recent decades have further made evident the non-material nature of money. In 1971, the United States ceased to define the value of the dollar in terms of gold. Since that time, the dollar has represented a promise from the U.S. government to redeem the dollar with...what? *Another dollar!* At least when the dollar was backed with gold, we could more easily *believe* it had some material value. With the demise of the dollar-gold equivalency, such self-deception has become more difficult to accept.

No self-respecting magician’s routine is complete without a decent disappearing act. Money has been performing this feat in a rather spectacular fashion. Once upon a time, when money was mostly gold and silver coins, banks started issuing pieces of paper that in effect, just pointed out where the metal really was. The next step in the disappearing act is already well under way. Even our paper money is rapidly dematerializing into binary bits in computers belonging to our bankers, brokers, or other financial institutions. There is now serious talk that all of it may soon join the virtual world. Must we wait until the last dollar bill has disappeared into an electronic purse to wake up to its true non-material nature?

In short, although money has taken many forms throughout human history, money itself is not a material object, but rather merely represented as such.

What then *is* money?

### ***A Working Definition of Money***

Money may be defined as an *agreement*, within a *community*, to use something as a *medium of exchange*.

As an *agreement*, money lives in the same space as other social contracts, like marriage or lease agreements. These constructs are real, even if they only exist in people’s minds. The money agreement can be attained formally or informally, freely or coerced, consciously or unconsciously.

This agreement is valid only within a given *community*. Some currencies are operational only among a small group of friends (like chips used in card games), for certain time periods (like the cigarette medium of exchange among front-line soldiers during World War II), or among the citizens of one particular nation (like most “normal” national currencies today). Such a

community can be a geographically disparate group (such as Internet participants) or the entire global community (as in the case of the U.S. Dollar as long as it is accepted as reserve currency)

Finally, the key function that transforms the chosen object into a currency is its role as a *medium of exchange*. There are other functions that today's money tends to perform, such as unit of account, store of value, tool for speculation, and so on. However, these other functions may be considered secondary, as there have been perfectly effective currencies that did not perform some or all of these other roles.

In summary, the magic of money is bestowed on something as soon as a community can agree on using it as a medium of exchange. Our money and monetary systems are therefore not de facto realities, like air or water, but rather are choices, like social contracts or business arrangements, and, as such, are agreed to, and are subject to, review and amendment.

Let us now look at some of the finer points on the agreements that have been made with regard to our money.

### ***Our Monetary Agreements***

The fundamental components of our modern-day monetary and banking systems were agreed to, mostly unconsciously; not by the many, but by a powerful few; not in today's world with its present conditions and requirements, but, rather in another age, with vastly different perspectives, sensibilities, objectives and realities.

It was in pre-Victorian England at the beginning of the Industrial Revolution, in a world impervious to pollution, greenhouse effects and overpopulation, in an age that encouraged nationalism, competition and colonization and viewed the earth as indestructible and its resources never-ending, that the vast majority of our prevailing monetary characteristics and features were molded. Whether by design or by happenstance, the monetary and banking systems that emerged were very much in keeping with that former mindset, and would become the most persuasive instruments of the primary objectives of that bygone period.

Our world today continues to be thoroughly influenced and profoundly affected by the most powerful and persistent designer and enforcer of the Industrial Ages' values and dominant emotions—the monetary system. Four seemingly benign features of our money maintain this influence.

## **EFFECTS OF OUR MONEY**

All Industrial Age currencies have in common four key characteristics that continue to persist to modern-day as unquestioned features of “normal” money systems:

- *Attached geographically* to a nation-state;
- Its creation out of nothing—*fiat money*;
- By *bank-debt*;
- *Incurring interest*.

These seemingly innocuous components of our money system have wielded profound influence upon our society, the affects of which, will now be discussed.

## ***National Currencies***

The creation of a national currency has proven to be a most powerful tool to bolster national consciousness. National currencies are designed to facilitate economic interactions with fellow citizens rather than with foreigners. A common currency translates into a common information system, so that its inputs and outputs can be measured and compared across the parts.”<sup>2</sup> It draws an information border between “us” and “them,” and makes tangible in everyday life boundaries that would otherwise be visible only by means of an atlas. In effect, it reinforces both our unity within one nation, and our separation more globally.

During the breakup of the Soviet Union, one of the first acts by each of the newly independent republics was issuance of their own national currencies. The Euro, the single currency that officially replaced a dozen national currencies, aimed similarly at creating European national consciousness and unity.

While it might be difficult today to imagine any currency other than those issued on a national level, the vast majority of historical currencies were, in fact, private issues made by the local authority.

## ***Bank Debt & Fiat Money***

The Latin word *fiat* is found in the bible. According to Genesis, *Fiat Lux* (translation: "Let Light Be") were the first words pronounced by God. The next sentence states: “And light was, and He saw it was good.” We are dealing here with the seemingly godlike function of creating something out of nothing (*ex nihilo*) by the power of the Word.

All conventional national currencies in our world today are *fiat*-based currencies. A fiat currency is created by an authority who declares that something, although it may be worthless, to be a currency or valid “legal tender.” These fiat currencies are created as bank-debt, under the hierarchical authority of a national Central Bank.<sup>3</sup>

The convoluted money-creation process by means of bank-debt (as described in the previous chapter in *Money Alchemy*) is particularly inventive at resolving the apparent contradiction between two types of objectives pursued in pre-Victorian England: that of creating and reinforcing the nation-state on the one hand, while relying on private initiative and competition, on the other. Specifically, it provides a smooth way to privatize the creation of the national currency (theoretically, a public function) via the private banking system as a whole, while maintaining pressure among individual banks to compete for the deposits of their clients.

A very important built-in aspect of bank-debt, fiat money systems is summarized by economists Jackson and McConnell: “Debt-money derives its value from its scarcity relative to its usefulness.”<sup>4</sup> For a bank-debt based currency to function at all, scarcity has to be artificially and systematically introduced and maintained. This is one reason why today’s currency system is not self-regulating, but rather, requires an active role of Central Banks to maintain that scarcity. Actually, Central Banks compete to keep their own currency in short supply internationally, so that the relative value and scarcity of their currencies are maintained as well. They accomplish that for instance by making borrowing more expensive whenever they want to “tighten money supply.”

Scarcity reinforces competition rather than cooperation, and has profound effects upon our society and nearly every aspect of our lives, as will be explored next.

## ***Interest***

Albert Einstein, when asked what he considered the most powerful force in the universe to be, it is rumored that he caught his inquisitor by surprise, supposedly offering up the unexpected quip: “Compound Interest.” Whether he did indeed reply so, this response is not without some merit.

Charging interest on money was prohibited on both moral and legal grounds for more than 20 centuries, until the reign of King Henry VIII who, after his break with Rome, first legalized interest in Britain in 1545. For most of history, all three “religions of the Book” (Judaism, Christianity, and Islam) emphatically outlawed usury, intended here as any interest on money. It is sometimes forgotten that the Catholic Church remained prominently in battle against the “sin of usury” until the 19th century (see insert).

### ***Usury and Religion***

*It is written in the Old Testament: “Unto thy brother thou shalt not lend upon usury, that the Lord thy God may bless thee in all that thou settest thine hands to.” (Deuteronomy 23:20). Islam is even more encompassing in its condemnation: “What ye put out as usury to increase it with the substance of others, shall have no increase from God.” (Koran Sura 30:38).*

*However, since modern money systems evolved predominantly under Christian influence, it is this religion’s changing view of usury over time that merits particular attention.*

*Usury was one of the most persistent dogmas of the Catholic Church. Clement of Alexandria, an early Church father, specified: “the law prohibits a brother from taking usury; designating as a brother not only him who is born of these same parents, but also one of the same race and sentiments...”*

*More than a dozen councils upheld the condemnation of the practice of usury, from the Councils of Elvira (305-306AD) to the Council of Lyons (1274). The Council of Vienna (1311) went so far as to warn that any ruler who would not criminally punish anybody committing usury in his realm would be himself excommunicated. The 5th Lateran council (1512-1517) reiterated the definition of the sin of usury as: “receiving any interest on money.”*

*The original doctrine against usury was finally questioned within the Catholic Church itself in 1822, after a woman from Lyons, France was refused absolution unless she returned an interest she had earned. Clarification was requested from Rome that responded: “Let the petitioner be informed that a reply will be given her question when the proper time comes ...meanwhile she may receive sacramental absolution, if she is fully prepared to submit to the instructions of the Holy See.” A forthcoming resolution was promised again in 1830, and once again in 1873. This promised clarification never came.*

*Thus, the sin of usury, never officially repealed by the Church, was simply forgotten.*

Though the implications of the loans that create our money are seldom understood, its effects upon society are pervasive and quite powerful. Three well-known consequences of interest as a built-in feature of our money system are:

1. Interest encourages systematic competition among the participants in the system.
2. Interest continually fuels the need for endless economic growth.
3. Interest concentrates wealth by taxing the vast majority in favor of a small minority.

### **1. Encouraging Competition.**

When a bank creates money by providing, say, a \$100,000 mortgage loan, it creates only the principal when it credits the account. However, it expects a return of perhaps \$200,000 over the next twenty years or so. The bank does not create the interest; it sends the lender out into the world to battle against everyone else to bring back this second \$100,000 which has never been created, hence the shortage. So how does the loan get repaid? To put it simply, to pay back interest on a loan, someone else’s principal must be used. In other words, the device used to create the scarcity indispensable for this type of bank-debt money system to function, involves

having people compete with each other for the money that was never created—and penalizes them with bankruptcy should they not succeed.

This is one important reason why interest rate decisions by Central Banks are paid so much attention. Increased interest costs automatically determine a larger proportion of bankruptcies in the future. When your bank checks your creditworthiness, it is really verifying your ability to compete successfully against the other players, i.e., managing to wrestle out of them something that was never created.

The following story, “The Eleventh Round,” illustrates the way interest is woven into our money fabric and how it stimulates competition among the users of our currency.

### *The Eleventh Round*

*Once upon a time, there was a small village where people knew nothing about money or interest. Each market day, people would bring their chickens, eggs, hams, and breads to the marketplace and enter into the time-honored ritual of negotiations and exchange for what they needed with one another. At harvests, or whenever someone’s barn needed big repairs after a storm, the villagers simply exercised another age-old tradition of helping one another, knowing that if they themselves had a problem one day, others would surely come to their aid in turn.*

*One market day, a stranger with shiny black shoes and an elegant white hat came by and observed the whole process with a sardonic smile. When he saw one farmer running around to corral six chickens wanted in exchange for a big ham, the stranger could not refrain from laughing. “Poor people,” he said, “so primitive.”*

*Overhearing this, the farmer’s wife challenged him. “Do you think you can do a better job handling chickens?”*

*“Chickens, no,” responded the stranger. “But there is a much better way to eliminate all the hassles. Bring me one large cowhide. Then have every family meet with me. I’ll explain the better way.”*

*And so it happened. The families gathered, and the stranger took the cowhide, cut perfect leather rounds in it, and put an elaborate and graceful little stamp on each round. He then gave ten rounds to each family, stating that each round represented the value of one chicken.*

*“Now you can trade and bargain with the rounds instead of those unwieldy chickens.” It seemed to make sense, and everybody was impressed with the stranger.*

*“One more thing,” the stranger added. “In one year’s time, I will return, and I want each of you to bring me back an extra round, an eleventh round. That eleventh round is a token of appreciation for the technological improvement I just made possible in your lives.”*

*“But where will that round come from?” asked the wife.*

*“You’ll see,” said the stranger, with a knowing look.*

*Assuming that the population and its annual production remained exactly the same during that next year, what do you think happened? Remember, that eleventh round was never created.*

*Indeed, as the stranger had suggested, it was much more convenient to exchange the rounds instead of the chickens on market days. But this convenience had a hidden cost, beyond that of the demanded eleventh round—that of generating a systemic undertow of competition among all the participants. The equivalent of one out of each eleven families would have to lose all of its rounds, even if everybody managed their affairs well, in order to provide the eleventh round to the stranger.*

*The following year, when a storm threatened some of the farmers, there was a greater reluctance to assist neighbors. The families were now in a wrestling match for that eleventh round, the round that had not been created, which actively discouraged the spontaneous cooperation that had long been the tradition in the village.*

In summary, our monetary system obliges us to collectively incur debt and compete with others in the community, just to obtain the means to perform exchanges between us. No wonder “it is a tough world out there and that Darwin’s “survival of the fittest” is so readily accepted by those who live within our competitive money system. In point of fact, however, there is ample evidence to support less harsh interpretations of the natural world (see insert).

### ***What is Natural: Competition or Cooperation?***

*Bio-sociology Professor Imanishi, from Kyoto University, has shown that the Darwinian vision of nature as a struggle for life has been completely blind to the many more frequent cases of co-evolution, symbiosis, joint development, and harmonious coexistence which prevail in all domains of evolution. Even our own bodies would not be able to survive long without the symbiotic collaboration of billions of microorganisms in our digestive tract, for example.<sup>5</sup>*

*Elisabet Sahtouris points out that predominantly competitive behavior is a characteristic of a young species during its first forays in the world. In contrast, in mature systems like an old-growth forest, the competition for light, for instance, is balanced by intense cooperation among species. Species that do not learn to cooperate with the other species with whom they are co-dependent on invariably disappear.<sup>6</sup>*

*It is revealing that Darwin himself wrote another book than the famous "Origin of Species" in which he shows that the theory of evolution doesn't apply to human evolution, because once human consciousness comes into play everything can change. But this work was completely overlooked —not because it was less valid than his earlier works —but because it didn't fit with the bias in values of the age in which he lived.*

## **2. Need for Endless Growth**

The main simplifying assumption of the "Eleventh Round" is that everything remains the same from one year to next. In reality, we do not live in a world of zero growth in population, output, or money supply. The real process involves growth, and the money system just preempts the first slice of that growth, that is to say, to pay for the interest. In other words, if one doesn't pay back the interest on the loans, the bank forecloses on your property. It is ironic that in the old agrarian societies one customarily sacrificed to the Gods the first fruits of the harvest. Now, instead, we are giving the first fruits of our toils to the financial system....

In this dynamic view, it is much more difficult than in our Eleventh Round story to notice what is actually happening. The money system acts like a treadmill requiring continuous economic growth, even if the real standard of living remains stagnant. The rate of interest fixes the average level of growth that is needed to remain at the same place. This need for perpetual growth is another fact of life which we tend to take for granted as a natural component of our modern societies, rather than recognizing how it is fueled by our money system.

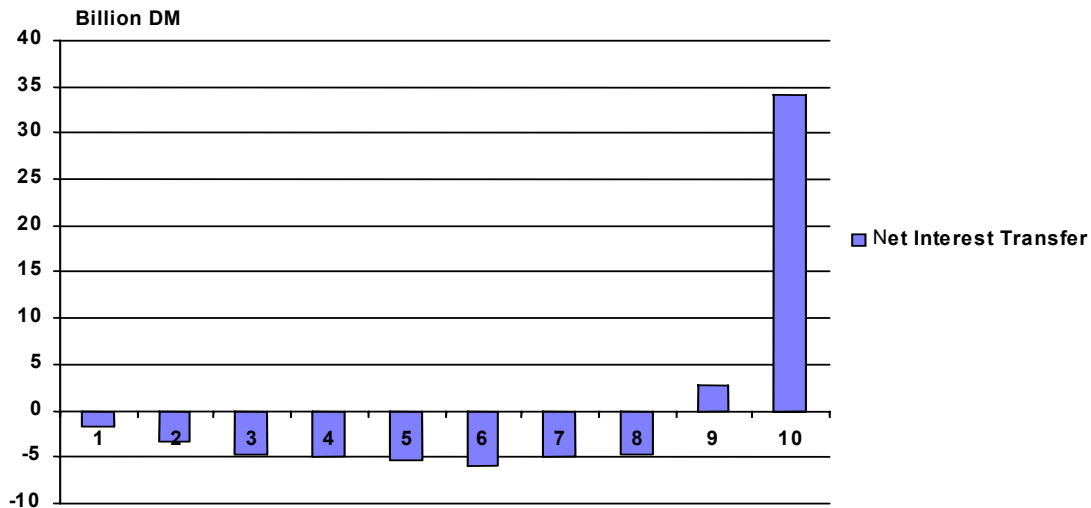
## **3. Concentration of Wealth Effect**

A third systemic effect of interest on society is its continuous transfer of wealth from the vast majority to a small minority. The wealthiest receive an uninterrupted rent from whoever needs to borrow to obtain the medium of exchange. A revealing study on the transfer of wealth via interest from one economic group to another was performed in Germany in 1982 (Figure 2.1).<sup>7</sup>

All Germans were grouped in ten income categories of about 2.5 million households each. During that year, transfers between these ten groups involved a total of **270 billion DM** in interest payments (approx. U.S. \$120 billion at the time). A stark way for presenting the process is to graph the net interest transfers (interest gained minus interest paid) for each of these 10 household categories.

The highest transfers of interest occurred from the middle class categories (3 to 8), each of which transferred about 5 billion DM to the top 10 percent of the households (category 10). Even the lowest income households transferred a substantial 1.8 billion in interest, per year, to the highest group.

The net effect is that the top 10 percent of households received a net transfer of DM 34.2 billion in interest from the rest of the society during that year. The graph illustrates the systematic transfer of wealth from the bottom 80 percent of the population to the top 20 percent, especially the top 10 percent, due *exclusively* to the monetary system used, and *independent* of the degree of cleverness or industriousness of the participants and recipients—a classical argument so often presented to justify large differences in income.



**Figure 2.1 Transfer of Wealth via Interest, Germany 1982**

Though no study on the effects of interest payment on the concentration of wealth is available for the United States, the overall concentration of financial wealth is even more dramatic than for that of Germany. The only group that has increased its percentage of overall income over the past 20 years in the United States has been the top five percent of households. Though the next 15 percent of households held their own, all other groups have seen a decrease in their piece of the national pie.

It is true that between 1975 and 1995, the combined income of all U.S. households rose from \$2.7 trillion to \$4.5 trillion in constant 1995 dollars. However, the benefits of this growth were not the same for all, given that the top five percent increased their average income by a whopping 54.1 percent, absorbing, the bulk of the new growth, at the expense of the middle 60 percent of the population. The cumulative result of this process explains the excessive imbalance in U.S. and world wealth distribution.

Was it a concern for social justice and stability that previously motivated three major religions— Judaism, Christianity, and Islam—to unanimously prohibit the practice of charging interest? It is intriguing that after interest became officially legal, almost all countries have felt the need to create income redistribution schemes to counteract at least part of this process.

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The three side effects of interest: competition, the need for perpetual growth, and wealth concentration, have been the hidden engines that have propelled us into and through the Industrial Revolution.

## ENDNOTES

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1. Davies, G. *A History of Money from ancient times to the present day* (Cardiff: University of Wales Press, 1994) pg. 27
2. Handy, C. *The Empty Raincoat* (London: Arrow Business Books, 1995) p. 108.
3. A detailed description of this process was provided in *The Future of Money* (Chapter 2 and Primer).
4. Jackson and McConnell. *Economics* (Sydney: McGraw Hill, 1988).
5. Thuillier, P. "Darwin chez les Samourai" in *La Recherche* No. 181 (Paris, 1986) pp. 1276-1280.
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7. Kennedy, M. *Interest and Inflation Free Money* (Okemos, Michigan: Sava International, 1995) p. 26.