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**Democratizing Money:  
From the Federalist Papers to the Community Currency Movement**

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**COMPULSORY DECLARATION**

This work has not been previously submitted in whole, or in part, for the award of any degree. It is my own work. Each significant contribution to, and quotation in, this dissertation from the work, or works, of other people has been attributed, and has been cited and referenced.

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### **Abstract**

This thesis examines the political idea of democratic money, within the historically specific capitalist democracy (Wood, 1995: 213), and critically evaluates counter claims to be democratizing money made by advocates of community currencies.

The global economy is currently dominated by one type of money creation, capitalist credit-money (Ingham, 2008). Credit-money, “the use of bills and notes signifying a ‘promise to pay’” developed between the sixteenth and eighteenth centuries (Ingham, 1999: 84). What this system of money creation relies on is a set of social and political institutional arrangements to manage the quantity and value of this money, “modern credit-money is itself, first, a social relation and second; that as such its elasticity of production is entirely a social construct” (Ingham, 1999: 80). This is a claim that money preceded the emergence of the capitalist mode of production and therefore it is not something that has simply emerged in response to the requirements of the capitalist system, but rather consists of its own forces of production (Ingham, 1999: 82).

To examine this premise the thesis has three chapters. The first chapter looks at the creation of the Federal Constitution and concepts of inequality and private property as expressed in the Federalist Papers. The second chapter looks at three phases in America’s financial history and includes a close reading of hundreds of financial pamphlets published during the nineteenth century. The third chapter looks at the rise of the Community Currency movement and their concept of democratic money. It highlights the claim made by CC advocates that no centralized authority, be it the government or a bank, is needed for citizens to create money. CC advocates believe all citizens and local communities have the right to create their own decentralized, localized and individualized currencies. The claim that this new system of currency<sup>1</sup> creation will be more just, equal, ecological, sustainable and fair ultimately resulting in a more democratic economy.

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<sup>1</sup> Due to the complicated nature of defining money and credit, and the ways in which different texts quoted use the terms currency, credit and money interchangeably I have chosen, whenever possible, to use the term currency to mean money, credit and any other medium of exchange.

The conclusion drawn is that capitalist credit-money is neither natural nor given, but is rather the product of a series of decisions made by society. These decisions have historically been aimed at reinforcing a system of currency creation that is compatible with America's capitalist democracy. The highlighting of the way in which currencies are a social construct points to the possibility that the CC movement represents a unique, and potentially far reaching challenge to the dominance of capitalist credit-money. This is reinforced by two additional trends; first, the rise of new technologies that enable decentralized networks and forms of organization and secondly, the current financial crisis which has highlighted the continued and renewed weakness and fragility of the current financial system. All radical shifts in the creation of money and credit have followed financial crises. The chances are that this period will be no different.

**Keywords:**

Capitalism, Money, Credit, Community Currencies, Finance, Banking, Federalists, Federal Constitution, United States of America

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University of Cape Town

## Introduction

This thesis examines the political idea of democratic money, within the historically specific capitalist democracy, and critically evaluates counter claims to be democratizing money made by advocates of community currencies.

The global economy is currently dominated by one type of money creation, capitalist credit-money (Ingham, 2008). Credit-money, “the use of bills and notes signifying a ‘promise to pay’” developed between the sixteenth and eighteenth centuries (Ingham, 1999: 84). This form of money creation is based on two sets of promises – the debtors promise to pay back the loan and the banks promise to accept the money bills in payment of these loans. What this system of money creation relies on is a set of social and political institutional arrangements to manage the quantity and value of this money, “modern credit-money is *itself*, first, a *social relation* and second, that as such its ‘elasticity’ of production is *entirely a social construct*” (Ingham, 1999: 80). This is a claim that money preceded the emergence of the capitalist mode of production and therefore it is not something that has simply emerged in response to the requirements of the capitalist system, but rather consists of its own social forces of production (Ingham, 1999: 82).

The production of this capitalist credit-money varies across countries, but has certain fundamental features:

“(i) the private credit and the banking system ‘money multiplier’; (ii) state debt as the ultimate foundation of credit money; (iii) the pivotal role of the central bank; and (iv) the three-cornered struggle between state, money market and taxpayer.” (Ingham, 2008: 75)

Money that is created through the interplay of these characteristics has come to dominate every nation-state in the world, including the “communist” economies of China, Cuba and North Korea. Capitalist credit-money creation is accepted as the natural form of money creation by almost every level of society and every state around the world.

This thesis is built off the premise, along with several other theorists, that money is not natural or fixed, nor does it need to be a physical object;<sup>2</sup> money is more accurately theorized as a social construct (Mellor, 2005; Ingham, 1996; Hart, 2001). This idea, that money is produced by the historically and geographically specific society it is found in, and is not a spontaneous outgrowth of the economy (Ingham, 2008), is a critical step in theorization of an alternative political economy. Many political economists fail to explore the socio-political dynamic of money, often assuming that it will spontaneously emerge in the political economy. The majority of the theorists that advocate alternative political economies fail to engage, critically, this understanding of money (for an example see the work of Samir Amin, 1982; and for comments on this particular issue see Mellor, 2005). In many cases theorists theorize an alternative political economy while retaining the elements of capitalist money creation, or assume the creation of money without paying attention to how this is to occur. This is a serious failure in many of the theorists work and the creation of money deserves a much more critical exploration within alternative political economic theories (Mellor, 2005). The limited group of theorists that have engaged in critical analysis of the creation of money have pointed to the role that characteristics like debt/credit, interest and centralized control, play in the reinforcement of the current political economic arrangement, and several of these theorists believe that by changing some, or all of these characteristics, the possibility opens up for alternative political economic societies to flourish (Douthwaite, 1999; Kennedy, 1995; Lietear, 2001).

The first chapter of this thesis is focused on illustrating the historical specificity of the American “capitalist democracy” (Wood, 1995: 213).<sup>3</sup> The chapter looks specifically at how the Federalists frame class inequality as natural and claim that certain classes are better suited to represent the interests of all other classes, to the benefit of the entire political economy. The Federalists were deeply concerned with the impact that colonial paper money experiments had

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<sup>2</sup> In essence this is an argument for a non-commodity conceptualization of money. The realization of money created through credit/debt relationships means that the “commodity theory of money” is problematic to our understanding of money is something that several theorists are grappling with. (See Ingham, 1998; Hart, 2001; Mellor, 2005).

<sup>3</sup> E.M. Wood uses the phrase and the concept of a “capitalist democracy” in her book, “Democracy Against Capitalism” (1995: 213). Her central argument is that the concept of democracy that we assume today was a historically specific creation of the U.S.A. during the writing of the Federal Constitution. The American concept of democracy separated the political and economic spheres of life, removing them from the concept of democracy, as it had previously been understood. This was achieved through the creation of a new concept of democracy that could accommodate capitalism by removing questions of property and socio-economic equality from the political sphere. Wood states that, “In that sense, political equality in capitalist democracy not only coexists with socio-economic inequality but leaves it fundamentally intact” (1995: 213)



on class inequality. The result of these Federalist concerns is a clause being placed in the Federal Constitution that ends the ability of individual state legislatures to issue their own money or credit. This marks the moment when money creation is fundamentally changed so as to be made compatible with the Federalist ideas of class inequality. The Federalists believed that the colonial state legislatures, during the 1770's, were creating paper money with the express purpose of creating inflation. The Federalists argued that this would destabilize class relations threatening the rights of property and the continued operation of the political economy. The Federalists were first and foremost concerned with designing a political system that would be compatible with and protective of the continued free flow of the commercial economy. These requirements, built into the Federal Constitution, set the terms of the financial debates within the U.S.A. for the next two hundred years.

Chapter two looks at how the federal government spends the next two hundred years guaranteeing that whatever system of currency<sup>4</sup> creation is implemented is one that is compatible with the free flow of commercial exchange. The chapter explores three phases in the financial debates. The first looks at the failed efforts of the federal government to create a national bank from 1791 to 1841. The second phase turns to the 1860's when the federal government creates, for the first time, paper money. This section explores in detail the debates that emerge paying particular attention to the arguments made by the Greenback Party in support of paper money. The third section looks at the creation of the Federal Reserve System and the claim by President Wilson that it represented the "democracy of credit" (Wood, 2005: 165). This chapter looks at how in each phase the questions of quantity and value are resolved in ways that guarantee that the resulting system of currency creation will reinforce the free flow of the commercial economy. This meant that the solutions always had to be compatible with class inequality and private property. The final solution represented by the Federal Reserve System is what Ingham (2004) calls capitalist credit-money - a historically specific system of money creation that has been designed, over the course of the last two hundred years in a way that has focused on guaranteeing its compatibility with America's capitalist democracy.

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<sup>4</sup> Due to the complicated nature of defining money and credit, and the ways in which different texts quoted use the terms currency, credit and money interchangeably I have chosen, whenever possible, to use the term currency to mean money, credit and any other medium of exchange.

It is important to note, for the reader, that chapter two acts as a bridge in which the ideas of the bullionists and Greenbacks are explored in great detail. The need for this detail becomes apparent in chapter three where the long-term influence of these forgotten debates is fully demonstrated. Though the bullionists and Greenbacks were both focused on the same project - the continued expansion of the capitalist economy – they offered very different solutions to this goal. Without fully exploring the nuances and philosophical foundations of these differences their influence on the community currency movement cannot be fully expressed and explored.

Chapter three explores the most recent phase in the financial debates. This new phase, loosely termed the, “Community Currency” (CC) movement, represents a mix of radically new theories of currency creation. Though these theories still engage the classic questions of quantity and value, their solutions challenge the historical ideas underpinning the dominant system of capitalist credit-money creation. CC advocates claim importantly, that currencies can be created without any centralized authority. They claim that decentralized, localized and individualized currency creation is not only viable, but that it is the right of every citizen to create their own currency. They claim that this new way of creating currencies is not only more democratic, but that it will result in more equal, just, ecological and sustainable political economies. Their notion of democracy is radically different from that of the Federalists, and the CC advocates claim that the creation of the Federal Reserve System represents the centralization and privatization of currency creation, and is certainly not the democratization of credit.

The purpose of these three chapters is to show how our current system of capitalist credit-money creation is a result of specific decisions made by society. This challenges the idea that money is natural, or that today’s dominant system is the only way of creating currencies. The CC movement is challenging the dominance of the capitalist credit-money system. It may be worthwhile paying attention to them. The first few decades of the twenty-first century have been marked by the proliferation of new technologies, which enable new forms of organization and communication, at the very moment when the dominant system of currency creation is experiencing yet another crisis. Assuming that capitalist credit-money is the only (and natural)

way of creating currencies is wrong. It may just be the only way of creating money in a way that is compatible with capitalist democracies.

## **Chapter One**

### **America's Capitalist Democracy:**

#### **The Federalists Entrench Class Inequality and Private Property as Natural**

To explore this political idea of democratic money it is necessary to clarify the specific character of democracy within which today's capitalist money came to dominate. This process is most easily examined within the context of the United States of America. The type of democracy that emerged from the constitutional debates of 1787 was one that explicitly supported private property and accepted class inequality as natural. And, any effort by government to level these inequalities or threaten the existence of private property was viewed as a threat to liberty. During the period leading up to the writing of the Federal Constitution there were a number of financial policies enacted by state legislature's aimed at promoting the 'leveling spirit' that advocates of original democracy favored.<sup>5</sup> The Federalists framed these policies as a threat to liberty, to the rights of private property and persons, to the stability of class relations and finally, but most importantly, to the free flow of commerce (Carey, 2001: 231 [Federalist No. 44]). One of the most important consequences of the Federal Constitution was a move towards a new monetary regime under the Federalist system of governance; this included ending the ability of individual states to print or mint money or to declare legal tender. This shift in money creation authority was the beginning of a historical process in which the creation of money was increasingly centralized under the authority of the federal government. This consolidation of authority helped guarantee that currency creation policies were enacted by a government friendly to the needs of the capitalist economy. This resulted in a financial system that reinforced the existence of private property and the free flow of commercial exchange, while mindful of the need to limit any disrupting influence this may have on existing class relations. The success of this system of currency creation was critical to the continued existence of America's capitalist democracy.

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<sup>5</sup> The use of the term "leveling spirit" was used to identify efforts at reducing class inequality (Ferling, 2003: 283)

In order to create America's political economic system several ideas had to be re-conceptualized: the role of elections and representation, the idea of democracy, the role of private property and how to manage the creation of money and credit. G.S. Wood describes this era in his book, "The Creation of the American Republic, 1779-1787":

"Although the vocabulary of the period was familiar, I found the meaning of much of that vocabulary strange and peculiar, and I learned that words such as 'liberty,' 'democracy,' 'virtue,' or 'republicanism' did not possess a timeless application. Indeed, even within the very brief span of years that I was studying, it soon became clear that the terms and categories of political thought were undergoing rapid change, beset by the strongest kinds of polemical and experiential pressures...I realized that a fundamental transformation of political culture had taken place." (1993: viii)

Wood (1993) is highlighting shifts that would be strongly influenced by ideas and principles that the Federalists promoted and ultimately entrenched in the Federal Constitution. These shifts in the political culture were strongly influenced by the sanctity of the rights of private property and the belief in the idea that class inequality was natural and unavoidable. One of the central goals of the Federalists was to create a republic based on principles of representation that were built off these ideas. It was clearly not the Federalist's goal to create a state that was built off the principles of original democracy.<sup>6</sup> The fact that today, in this twenty-first century, the U.S.A. is associated with the idea of democracy, and is in fact held up as a model of democracy was never the goal of the Federalists. Rather, it was viewed by the Federalists that a republican government was the only choice before the American people; "The first question that offers itself is, whether the general form and aspect of the government be strictly republican? It is evident that no other form would be reconcilable with the genius of the people of America" (Carey, 2001: 193-4 [Federalist No. 39]). Between 1776 and 1787, the very idea of democracy was reworked, creating, "an entirely new kind of 'democratic' politics" (Manicas, 1988: 137). This would usher in a system of governance that would directly reflect the interests of the landowners and

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<sup>6</sup> When I refer to original democracy I am drawing on one of the central ideas of Athenian democracy which is described by E. M. Wood as having no separation between political and economic freedom meaning that political equality "substantially modified, socio-economic inequality" (1995: 212). In essence this original concept of democracy saw inequality amongst citizens as undemocratic, this was extended to include ideas of elections and representation, which were, prior to this era, associated with oligarchy (Wood, 1995).

merchants. E. M. Wood describes the way in which republicanism and democracy would be merged together:

“Where classical republicanism had solved the problem of propertied elite and labouring multitude by restricting the extent of the citizen body (as Athenian oligarchs would have liked to do), capitalist or liberal democracy would permit the extension of citizenship by restricting its powers (as the Romans did).” (1995: 208)

The creators of the Federal Constitution were tasked importantly with calming the democratic impulses and demands of the citizens of the colonial states. To do this the Federalists needed to create a system that, while protecting private property and leaving class inequality untouched, would give citizens a sense of political influence and inclusiveness. The rights of citizenship under the capitalist democracy ultimately created by the Federal Constitution would do exactly this while limiting many of the powers that democratic citizenship had historically implied; there would be no guaranteed socio-economic equality or rights under the Federal Constitution.

During the period following the American Revolution ideas of original democracy (centrally the idea that citizenship would have a direct impact on one’s socio-economic standing) were spreading throughout the colonial states. During the Federal Constitutional Convention several delegates expressed a concern with, “the ‘symptoms of a leveling spirit’ coursing the land” (Ferling, 2003: 283). It was these ideas of leveling that threatened the Federalists ideas and theories of society. James Madison, a Federalist, believed that democracies were, “spectacles of turbulence and contention; have ever been found to be incompatible with personal security, or the rights of property; and have, in general, been as short in their lives, as they have been violent in their deaths” (Carey, 2001: 46 [Federalist No. 10]). Clearly the Federalists were concerned that the demands of the majority were a threat to the entire political economy and the foundational rights of property and personal security. And, clearly the solution for the Federalists did not rest in the creation of a government that included the ideals of original democracy. This is because they saw existing inequality as natural and a fundamental element in the way the political economy operated. By naturalizing class inequality, the Federalists were

able to claim that government had no ability to reduce this inequality. The logical reason for why government couldn't do this was because of the reinforcement of an individual's right to private property. Class inequality after all is reflected, materially, by the inequality of property ownership. By arguing that inequality was natural questions of 'how' or 'why' this exists become irrelevant. The logical conclusion of this line of thinking, at least that made by the Federalists, is that the best that you can do as a society is to regulate the negative impact these inequalities may have on the overall operation of the political economy. The system that emerged relied heavily on elements (elections and representation) that had previously been, "perceived as the antithesis of democratic self-government," which ultimately became, "not only compatible with but constitutive of democracy" (Wood, 1995: 216).

The Federalists saw the inclusion of these elements, though on the one hand curtailing several ideas critical to the theory of original democracy, as a necessary part of their effort to regulate the potentially destabilizing impact of the varying and clashing interests, which were a direct outcome of the inequality of property ownership. The Federalists claimed that, "the diversity in the faculties of men" resulted in, "the possession of different degrees and kinds of property... from which the rights of property originate" (Carey, 2001: 43 [Federalist No. 10]). Madison claimed that it is from these different degrees of ownership that, "ensues a division of the society into different interests and parties" (Carey, 2001: 43 [Federalist No. 10]). These interests came to represent different factions, which Madison defined as, "a number of citizens, whether amounting to a majority or minority of the whole" who are driven by some sort of passion that is, "adverse to the rights of other citizens, or to the permanent and aggregate interests of the community" (Carey, 2001: 43 [Federalist No. 10]). Madison elaborates this further by stating that, "the most common and durable source of factions, has been the various and unequal distribution of property. Those who hold, and those who are without property, have ever formed distinct interests, in society" (Carey, 2001: 44 [Federalist No. 10]). The use of the phrase "have ever formed" by Madison highlights the acceptance and the naturalization of this inequality (Carey, 2001: 44 [Federalist No. 10]). The source of this inequality is not the product of political economic decisions but of the natural, God-given faculties of men, whose actions result in

varying levels of property ownership. The retention of the product of your labor forms a central notion of the Federalist concept of liberty, and threatening this ownership (liberty) clashed directly with their notion of class inequality. If supporters of original democratic ideas were viewed as “adversaries to liberty” (Carey, 2001: 42 [Federalist No. 10]) then a system was needed that would guarantee a form of political equality (a sense of democracy) while leaving socio-economic inequality unexplored or unresolved (a form of classical republicanism).

How then do you mediate these interests? How are you going to reduce the power of individuals, communities or states to threaten the rights of property? A central concept that forms part of the solution is one that centers on the concept of political representation. This idea of representation is in part built off the belief that some people, specifically merchants and bankers (and other property owners), were the best endowed to represent the interests of all classes. Alexander Hamilton wrote that, “The idea of an actual representation of all classes of the people by persons of each class is altogether visionary” (Carey, 2001: 206 [Federalist No. 35]). The logic used to justify this claim was that:

“Mechanics and manufacturers will always be inclined, with few exceptions, to give their votes to merchants, in preference to persons of their own professions or trades. Those discerning citizens are well aware, that the mechanic and manufacturing arts furnish the materials of mercantile enterprise and industry. Many of them, indeed, are immediately connected with the operations of commerce... They know that the merchant is their natural patron and friend; and they are aware, that however great the confidence they may justly feel in their own good sense, their interests can be more effectually promoted by the merchant than by themselves. They are sensible that their habits of life have not been such as to give them those acquired endowments, without which, in a deliberative assembly, the greatest natural abilities are for the most part useless; and that the influence and weight, and superior acquirements of merchants, render them more equal to a contest with any spirit which might happen to finesse itself into the public councils, unfriendly to manufacturing and trading interests. These considerations, and many others that might be mentioned, prove, and experience confirms it, that artisans and manufacturers will commonly be disposed to bestow



their votes upon merchants and those whom they recommend. We must therefore consider merchants as the natural representatives of all these of the community.” (Carey, 2001: 206-207 [Federalist No. 35])

This long quote illustrates the Federalists focus on giving power to those in society that are most friendly to, and supporting of, the growing system of commercial exchange. This framing is driven by the recognition that surplus value extraction (profits), which would accrue to the newly emerging capitalist merchants, was dependent on the protection of private property and class inequality. Under feudalism this extraction required forms of juridical and political power (the empowerment of feudal lords and barons), while under capitalist property relations the extraction occurred through normal and life-supporting economic exchanges (Wood, 1995). This new system of surplus value extraction required that the foundational assumption – that of the rights of private property and inequality – be entrenched, protected and removed from questions of political governance. These elements were not up for debate, or left to the whims of policy decisions – they are recognized as being the very constitutive element of the entire political economy and no act of government should threaten the existence of these elements in society. The Federalists knew that the best way to protect these elements was to put the property owners and merchants into positions of political power, thereby guaranteeing the perpetuation of the political economy. As much as this shift in forms of extraction allowed the expansion of political equality (increasing suffrage), it also required the installation of people that would create laws and regulations favorable to the system that enabled these new forms of extraction.

The outcome of the Federalist’s reconceptualization of the impact of inequality and the introduction of ideas like elections and representation, “had the effect (and the intention) of diluting the meaning of democracy” (Wood, 1995: 208). Despite this intention the way in which inequality is framed helped reinforce the revolutionary character of the American system. This is because the Federalists are not laying claim to power, or surplus value, based on hereditary forms of noble power. Rather, the inequality of power and wealth is a product of natural skills of individuals. This is very different from being born into a position of power. Under the

Federalist's conception anyone can acquire a position of power if they move up through the different classes of society, ultimately reaching the position of merchant or landowner. It doesn't matter who your family is, but it can be assumed that if you are a wealthy merchant that you will be more inclined to protect the foundations of that wealth and prosperity. Anyone, theoretically, can become a merchant or landowner, the possibility was only limited by your natural skills; this is vastly different from a system of nobility where there was nothing you could ever do to improve your socio-economic standing. Regardless of how "skilled" you were under feudalism, if you didn't have the right blood and family connections, there was nothing you could do about your lot in life. The liberty that the Federalists promoted was dependent on the protection of private property. This meant that no one individual, faction, or government policy has the right or ability to suddenly deny you the right to accumulate or retain your property. Government can do nothing, in fact it must not even attempt to do anything, about the distribution of "natural abilities" but it can, and must, protect the "acquired endowments" that result (Carey, 2001: 206 [Federalist No. 35]). For Madison there were "two methods of curing the mischief's of faction; The one, by removing its causes; the other, by controlling its effects" (Carey, 2001: 43 [Federalist No. 10]). Madison dismisses any effort at *removing* the causes of factions, as this would violate liberty (and liberty, by definition, includes the right to private property). This leaves only one choice: controlling the effects of these factions. This conclusion creates the ideological space for two elements to be introduced that had both, previously, been regarded as incompatible with original democracy: an enlarged state and the introduction of elections. The use of these concepts was, as a constitutional delegate said at the time, introduced to "inhibit democratic excesses" (Ferling, 2003: 283). Wood, when describing the Federalist form of democracy, states that "it meant that something hitherto perceived as the antithesis of democratic self-government was now not only compatible with but constitutive of democracy: not the exercise of political power but its relinquishment, its transfer to others, its alienation" (1995: 216). The introduction of both helped to distance citizens from direct engagement in policy choices, leaving those choices in the hands of those who understood what was needed to guarantee the political economy's smooth operation.

Prior to the creation of the U.S.A., democratic states had always been associated with geographically small countries so as to enable citizen's direct engagement in politics. There was a similar concern with size of states within the dominant theories of republican states. Montesquieu's theory of state formation, which dominated at the time, claimed that no republican government could exist across a large territory.<sup>7</sup> In Federalist No. 9, Hamilton cites the many new innovations in the science of politics that gave a, "powerful means, by which the excellencies of republican government may be retained, and its imperfections lessened or avoided" (Carey, 2001: 38). For Madison when you, "Extend the sphere" of the representative republican state:

"you take in a greater variety of parties and interests; you make it less probable that a majority of the whole will have a common motive to invade the rights of other citizens; or if a common motive exists, it will be more difficult for all who feel it to discover their own strength, and to act in unison with each other." (Carey, 2001: 48 [Federalist No. 10])

The creation of a large state limited the direct influence of every class of society on government's policies, by creating distance between citizens and the government's policy decisions. By limiting the influence of the demands of any dangerous majority or minority they had also found part of the solution to the danger of "factions". It is fair to note that the Federalists, at least in their rhetoric, were concerned about a minority claiming control over the government as much as they were afraid of a majority doing the same. However, the minority, which the Federalists were more than happy to protect and install in a position of power, were those that understood and directly benefited from the protection of private property and the class inequality.

In the twenty-first century a country is often called democratic based on whether they have had elections. Prior to the creation of the Federal Constitution elections and democracy were viewed as mutually exclusive. Aristotle associated the institution of elections with oligarchy and believed that it gave the power to the few over the rights of the majority (Wood, 1995).

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<sup>7</sup> Hamilton refers to the ideas of Montesquieu specifically in Federalist No. 9 in which he questions several of Montesquieu's key points (Carey, 2001: 37-41).

However, the Federalists made a series of counter claims. They argued that the House of Representatives was designed to limit the number of representatives therefore, “securing a sufficient number for the purposes of safety” rather than a house filled with many representatives that would inevitably tend towards one where “passion over reason” is the norm (Carey, 2001: 304 [Federalist No. 59]). Madison dismissed claims that the House of Representatives did not adequately represent all of the citizens (Carey, 2001: 37-41 [Federalist No. 9]). Madison turned the question of elections and representation on its head by arguing that a, “government may become more democratic; but the soul that animates it, will be more oligarchic” (Carey, 2001: 304 [Federalist No. 59]). What Madison had done is associate democracy with oligarchy, while elections, which are aimed at limiting original democracy, prevent the political economy from devolving into oligarchy. Implicitly Madison is refuting Aristotle’s claim that elections are the cause of oligarchy, instead placing them in the position of preventing the rise of oligarchy. What Madison is able to construct is a claim that republican forms of government, with electoral representation, tended towards a greater degree of democratic governance than did original democracy and its lack of elections. It was not that Madison and the Federalists were attempting to rework democracy so that they could create a democratic state, but rather they were attempting to incorporate democratic ideas into a form of republican government that would both be more inclusive politically, thereby calming the demands of the majority, and at the same time protect the interests of the merchants and propertied classes of society. All of this was aimed at guaranteeing a political economic system that enabled the free flow of commercial exchange dependent on the perpetuation of class inequality.

Madison made sure to frame this system of electoral representation as being able to respond to the influence of all classes and citizens. He knew that the majority was supportive of direct engagement and other crucial and defining elements of original democracy. Madison makes the argument that:

“we may define a republic to be, . . . a government which derives all its powers directly or indirectly from the great body of the people; and is administered by persons holding their offices during pleasure, for a limited period, or during good behaviour. It is *essential* to

such a government, that it be derived from the great body of the society, not from an inconsiderable proportion, or a favoured class of it.” (Carey, 2001: 229 [Federalist No. 39])

Madison frames and justifies elections as a way of guaranteeing that, “hereditary and aristocratic principles would be entirely excluded” from the political economy (Israel, 2010: 66). This is Madison’s attempt at recognizing the demands of citizens throughout the colonies for a direct voice and role in government and policy decisions. However, there is no acknowledgement of the elevated status of the merchant and landowner classes, or the protection of the basis of and ability to accumulate wealth. Class inequality is as natural in this conceptualization of society, as was noble power and the associated inequality under feudalism. Under the Federalist system having a noble bloodline no longer gave you access to the means of extraction. Rather, it was about an individual’s ability to compete and utilize their natural skills that guaranteed you access to the fruits of surplus value extraction. This ability was the result of your own natural God-given abilities and not the result of any action taken by government. Government could never endow one class with better skills, what government could do was remove itself from the equation as much as possible, and regulate any potential negative fallout of this inequality.

Something fundamental had shifted in European and American society; a recognition that the extraction of surplus value no longer required the same social structure that had previously existed.<sup>8</sup> The rise of capitalist property relations meant that economic power was no longer related to extra-economic relations and that, “political privilege gave way to purely ‘economic’ advantage” (Wood, 1995: 208). The writings of the Federalist’s suggest their recognition of this change. Hamilton had claimed that the role of the Federal Constitution was to create a form of government that would fit with what, “Hamilton called ‘the commercial character of America’ ” (Hamilton qtd. in Wood, 1993: 467). In this way politics was being redefined so as to accept the naturalized elements of capitalist exchange. E. M. Wood (1995) describes the development of political thought under Federalist philosophy resulting in the emergence of capitalist democracy,

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<sup>8</sup> The history of the breakdown of feudal relations and the associated forms of extra-economic surplus extraction has been well covered in the works of E.M. Wood (1995) and K. Polanyi (2001).

that both enlarged the suffrage but at the same time accepted socio-economic inequality. "In that sense, political equality in capitalist democracy not only coexists with socio-economic inequality but leaves it fundamentally intact" (Wood, 1995: 213). The ability to do this was driven in part by the philosophical separation of the rights of person and the rights of property and making this separation, "the two cardinal objects of Government" (Madison qtd. in Wood, 1993: 221). For the Federalists the protection of private property is a political question, but its origins are natural and unquestionable. Any effort by government to challenge its existence will inevitably meet with failure and the collapse of the government and, potentially, the free flow of commercial exchange. All of this meant that the Federalists could safely expand the right to vote to include all classes of society, because the elements critical to the functioning of the political economy (private property and inequality) were effectively removed from any political debate. G. S. Wood claims that:

"The isolation of property as a distinct ingredient of the society that must be separately embodied in the government marked an extraordinary change in American thinking, reflective of a general re-appreciation of the nature of American society taking place in the 1780's." (1993: 219)

The Federalists claimed that the final version of the Federal Constitution that emerged was designed to provide, "additional securities to republican government, to liberty, and to property" through a system that consists chiefly of, "restraints, which the preservation of the union will impose upon local factions and insurrections and upon the ambition of powerful individuals in single states" (Carey, 2001: 452 [Federalist No. 85]). Madison knew that, "Only a minority... can be interested in preserving the rights of property" (Madison qtd. in Wood, 2001: 411). The logical conclusion was to design a system of political governance that guaranteed this minority political power. The final vision was what Hamilton called, a commercial republic, built on the liberty of individuals and property (Wood, 1993: 467).

It is at this point that the introduction of the debates around the politics of money becomes possible. During the period leading up to the ratification of the Federal Constitution, colonial

state legislatures were attempting to utilize financial policy in ways that encouraged rising levels of socio-economic equality. The printing of paper money, the creation of pro-debtor legislation and other actions all threatened the power of the creditors and property owners. James Madison claimed that:

“The loss which America has sustained since the peace, from the pestilent effects of paper money on the necessary confidence between man and man: on the necessary confidence in the public councils; on the industry and morals of the people, and on the character of republican government, constitutes an enormous debt against the states, chargeable with this unadvised measure, which must long remain unsatisfied; or rather an accumulation of guilt, which can be expiated no otherwise than by a voluntary sacrifice on the altar of justice, of the power which has been the instrument of it.” (Carey, 2001: 231 [Federalist No. 44])

This framing of paper money’s impact on the overall political economy is used to argue against the right of states to create their own money. Madison believed that, “Had every state a right to regulate the value of its coin” the result would impede commercial activities between the states (Carey, 2001: 231 [Federalist No. 44]). The large variety of paper money, coinage (stamped with different sovereign denominations) and forms of credit that each state circulated and authorized was creating confusion and instability in the economy. These inflationary policies were framed as being anti-liberty and upsetting the balance of class relations. The result of these actions, according to the Federalists, was to create, “mutual distrust in the breasts of all classes of citizens” (Carey, 2001: 453 [Federalist No. 85]). These financial experiments were an outgrowth of the ending of monarchical control over currency creation. The logic of money at that time led citizens to believe that they could create money in a way that would be more beneficial to their interests, and specifically the interests of the poor, landless and indebted. However, the Federalists made a specific point of limiting these powers by creating, in the final version of the Federal Constitution, “precautions against the repetition of those practices on the part of the state governments, which have undermined the foundations of property and credit” (Carey, 2001: 453 [Federalist No. 85]). The Federalists had come to realize that they needed to control the way in

which money was created, and that the authority to do so could certainly not remain in the hands of state legislatures. The recent history had shown that, given the opportunity, citizens would create money in a way that was perceived to benefit the indebted and landless of society. During this period paper money, specifically, and currencies more generally had been shown, and used, as a tool to promote the interests of one class over another. The Federal Constitution specifically removes this right from the states – no state that is part of the U.S.A. retains the right to create its own money. The Federalists knew that, based on the design of the federal system with its acceptance of class inequality and private property that any system of currency creation had to reinforce these elements. The Federalists understood that they needed a financial system that is compatible with a commercial state. During the next two hundred years the debate over how much power the federal government has over the creation of money and credit would rage on, going through multiple phases. One thing is clear, all the decisions made by the federal government with regards to how to create money, were guided by the belief in the importance of protecting private property and enabling the free flow of commerce.



**Chapter Two:**  
**The Democratization of Credit:**  
**The Federal Government Builds a System of Finance Compatible with Inequality and**  
**Private Property Reinforcing the Free Flow of Commercial Exchange**

After the ratification of the Federal Constitution and despite the definitive inclusion of the clause removing currency creation authority from individual states, the debate over currency creation did not subside. It was immediately evident to the federal government and most citizens of the newly created U.S.A. that the expanding economy would need increasing supplies of currency – be it in the form of money or credit. This chapter looks at the evolution of the federal government’s involvement in the financial system, which was driven in great part by its effort to resolve the tension between the expanding capitalist economy of commercial exchange and the scarcity of money. The government had to find an acceptable solution to this tension within the context of entrenched understandings of class inequality and the impact of currency creation. With the efforts of the colonial legislatures during the late eighteenth century fresh in the minds of the banking and merchant classes, they knew that the solution to this tension could have profound implications for the entire political economy. They certainly did not want to disrupt class relations or threaten the rights of private property, either of these, in their minds, had the potential to disrupt the free flow of commerce. The solution that emerged in the early twentieth century rested on the creation of abundant supplies of credit, while specifically retaining a concept of money based on scarcity. This solution was believed to be the most compatible with the American capitalist democracy.

All of the financial debates and the solutions implemented are, in some way, guided by Federalist ideology. These ideas form the criteria by which any financial policy is judged. Most importantly, with the ratification of the Federal Constitution a particular view of class had become entrenched. This view centered on the natural character of inequality and the belief that one class could act as the representative of all other classes:

“... the influence and weight, and superior acquirements of the merchants render them more equal to a contest with any spirit which might happen to infuse itself into the public councils, unfriendly to the manufacturing and trading interests. These considerations, and many others

that might be mentioned, prove, and experience confirms it, that artisans and manufacturers will commonly be disposed to bestow their votes upon merchants and those whom they recommend. We must therefore consider merchants as the natural representatives of all these of the community.” (Carey, 2001: 206-207 [Federalist No. 35])

The role of the merchants, and their natural influence and weight, will serve to protect and enable the needs of manufacturing and trading. The assumption that class inequality is natural was discussed in detail in chapter one; both Alexander Hamilton and James Madison had argued for the natural character of this inequality claiming that any effort to reduce or change this inequality would result in a disruption of class relations, heightening tensions within society and threatening the smooth operation of the commercial economy. The Federalists claimed that there is no role for government with regards to creating greater equality and that the existing inequality is a fundamental and natural part of society. Therefore any financial policy enacted had to recognize this conceptualization of class and if it did not it was framed as a threat to liberty and the entire political economy.

Hamilton believed that the creation of this paper money by the colonial states had created, “mutual distrust in the breasts of all classes of citizens” and that, “precautions against the repetition of those practices on the part of the state governments, which have undermined the foundations of property and credit,” was a necessary element in any Federal Constitution (Carey, 2001: 453 [Federalist No. 85]). The Federalists clearly sided with a system of currency creation that was the most compatible with existing class inequality - a natural and necessary part of the commercial economy. Hamilton believed that the, “most productive system of finance will always be the least burdensome” to the manufacturing and banking classes (Carey, 2001: 453 [Federalist No. 85]). Therefore, whatever system of currency creation existed, it needed to be, first and foremost, the least burdensome to these classes of society.

In many ways money is framed in a way that mirrors the entrenched ideas of class inequality. The Federalists viewed class inequality as natural and any effort to intervene by government was

a violation of liberty and would ultimately fail, disrupting the entire society. Similarly, for the Federalists the existence of money, and its source of value, is viewed as natural and not the outcome of any acts or policy of government. Furthermore any effort by government to create money was seen as both unnatural and a threat to the entire society by disrupting the smooth operation of the commercial economy. This belief rested firmly on the assumption that the origins of the monetary value of gold had nothing to do with the acts of government. The root of this idea in turn, rests on the belief that money was, “not socially constructed and that it rather belonged to an autonomous and natural sphere – the market – in which it was perilous for a polity to intervene” (Babb, 1996: 1580).

This conceptualization of money value was logically linked to the idea that this natural value was the result of the actions of an individual, who has the right to the fruits of his labor, represented by the accumulation of a commodity-based money. This naturalization of money’s value led to the conclusion that real money was neutral, that its long-term impact on the real economy was insignificant; therefore, the introduction of increased supplies of gold (and almost exclusively gold) would not influence the long-term price level (Laidler, 1991). In fact by the 1820’s it was claimed that the long-run price equilibrium was, “determined by the cost of producing the precious metals” used as money (Laidler, 1991: 11). Bullionists, advocates of gold money, argue that gold’s historical role as money gives it its particular role as money. Importantly the source of gold’s value is *intrinsic* and *natural* and not the result of governments actions or socially constructed.

Attached to this idea of natural value, is the associated idea of “true” and “honest” money whose value, having not been created “falsely” through acts of government, was therefore a reliable representative of value.<sup>9</sup> While the economy, as it grows, requires increasing supplies of money, the chosen form, gold, is naturally finite and therefore cannot reliably expand to meet the demands of the growing economy. It is this tension between continuous growth and scarce supply, which keeps debates over the creation of money politically relevant into the twenty-first

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<sup>9</sup> See Honest Money League (1878); Fonda (1895); Dwinell (1946). All of these publications feature a range of documents and pamphlets that explore ideas of honest and true money.

century. Geoffery Ingham, an academic who has written extensively on the history of money, has highlighted how, “The scarcity of money is always the result of very carefully constructed social and political arrangements” (Ingham 2004: 8). In the 1790’s, the Federalists wanted to reinforce a set of social and political relationships that would support their concept of class relations, which they believed were necessary for the continued operation of the political economy. For the Federalists, and Hamilton in particular, the question became how to increase the supply of currency in circulation in a way that would reinforce class stability and the free flow of commercial exchange.

With the ratification of the Federal Constitution in 1787, the individual states had lost their right to create their own currency. What they had not lost was the ability to issue state bank charters and endow those banks with the right to issue their own forms of credit.<sup>10</sup> This was driven by the individual states’ realization that if they could not issue money (as they had been doing prior to 1787 in the form of paper), while the expanding economy was crying out for additional liquidity (in the form of a reliable medium of exchange), the only available solution was to increase the supply of credit.

The credit issued by the state banks was always issued on the assumption that there were equivalent reserves of gold held by the issuing bank. This meant that banks had to compete over the scarce supply of gold money in order to be able to provide reliable forms of credit. Over the next sixty years the amount of state banks with credit issuing charters grew steadily. From just three in 1790, “their numbers rose to 28 in 1800, 102 in 1810, 327 by 1820 and 584 by 1835,” (Sylla, 1998: 85) and by 1840 there were over eight hundred banks issuing their own forms of banknotes (Rousseau, 2004: 23). This meant that there were hundreds, if not thousands, of differently denominated or valued paper banknotes circulating through the economy. During the first half of the eighteenth century banks were, “in the minds of the average citizens anywhere” charged with overcoming, “the scarcity of money” (Unger, 1964: 40). In the minds of citizens

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<sup>10</sup> My use of the term credit applies specifically to banknotes issued by individual banks. These banknotes, prior to the arrival of computers, were issued as pieces of paper, and were supposed to represent real and existing supplies of gold money. The idea being that if you returned to the bank with your banknote you would be given an amount of gold money in return.

this scarcity of money was real and natural, because gold was a naturally scarce resource. They saw the solution resting on the creation of reliable forms of credit. In this way banks were viewed as not creating money but as issuers' of credit. Essentially, banks were charged with making available the credit needed to enable the free flow of commercial exchange. Despite the proliferation of these credit-issuing state banks and because of the scarcity of money, they often failed to issue reliable supplies of credit. The economy repeatedly experienced bank runs and crashes, throughout the eighteenth and nineteenth centuries, in great part due to the over issuance of credit, hoarding of gold, and the inability to increase the supply of money.

Class interests entered the financial debates almost immediately. The debates centered on the belief that bankers represented and worked to the benefit of the merchant and banking interests, over the interests of the agrarian and laboring classes.<sup>11</sup> Hamilton had explicitly said that the interests of the laboring classes, “can be more effectually promoted by the merchant than by themselves” (Carey, 2001: 207 [Federalist No. 35]). This sense that the banks were focused on serving the needs of the merchants over the needs of the farmer was reinforced by the fact that the majority of banks were based in New England and the Middle Atlantic States, which were dominated by wealthy property owning merchants and bankers (Sylla, 1998: 85). This concentration of money in the northeast was linked (at least in political rhetoric) with the economic hardships experienced in the predominantly agricultural south. The agrarian south, during the harvesting and planting seasons, needed large but periodic increases in the supply of currencies but due to the lack of money held by southern banks, currency supplies were unreliable. These problems included one bank not accepting another bank's banknote (credit note), or only accepting them at a great discount. The continuous instability of this system of credit issuance, and the negative ramifications this had for the overall political economy, helped drive the repeated efforts of the federal government to create a system of national banking. The efforts of the federal government centered on the idea that the creation of a national bank, which issued its own credit, would provide the greatest amount of stability to the political economy. The thinking was that this credit would be accepted at face value by all banks (unlike state bank

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<sup>11</sup> For an in-depth look at these class conflicts and the shifting interests see Sharkey, (1959); Unger, (1964); Sylla (1998).

issued credit), because they would trust the ability (in other words the liquidity) of the national bank to exchange the credit for gold money. This would create stability and hopefully reduce the negative impacts of scarce supplies of money and credit on the political economy.

Importantly, there was no attempt by government (federal or state) to create more money (unlike the colonial states of the 1770's), all efforts were focused on creating credit, while gold would continue to form the scarce monetary base and act as the only "true" and "natural" form of money. This shift away from money creation and towards credit creation is a fundamental political shift, one that would set the tone for many of the subsequent financial policy debates. This shift would, for at least the next sixty years, limit the solutions to ones centered on guaranteeing the continued scarcity of money and that its value would be "naturally" created. With this attachment to a scarce monetary base, driven by the belief that it was the most compatible with the commercial economy, the Federal government attempted to create a national bank.

The U.S. Congress chartered The First Bank of the United States (hereafter referred to as The First Bank), on February 25, 1791 supported and driven by the concerted efforts of then Treasury Secretary Hamilton (Davies, 2002: 471).<sup>12</sup> Hamilton was driven by his belief that having a functioning credit system was the route to the Federal government's fiscal and political survival and was of the "full conviction that banks are essential to the pecuniary operations of the government" (Hamilton qtd. in Chernow, 2004: 247). In order for the government to survive financially the economy needed to grow; a growing economy would result in a growing tax revenue base.<sup>13</sup> The historian, Charles Beard described Hamilton's efforts as:

"...primarily capitalistic in character as opposed to agrarian...and constituted a distinct bid to the financial, commercial, and industrial classes to give their confidence and support to the government in return for a policy well calculated to advance their interests

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<sup>12</sup> This section dealing with the creation of the National Banks relies heavily on the work of Chernow (2004) and Davies (2002).

<sup>13</sup> Prior to the introduction of the federal income tax a huge portion of the federal government's revenues were the result of export/import tariffs and customs duties (Chernow, 2004).

...He knew that it [USA] had been created in response to interested demands and not out of any fine spun theories of political science.” (1915: 131)

Hamilton had no intention of attempting to level society or remove property from a given class. Rather he was driven by the very pragmatic realization that a compromise had to be reached between the needs of the expanding commercial economy and the linked need to increase supplies of currency. Hamilton’s solution was to create a national bank that would, “issue paper currency in the form of banknotes redeemable for coins” (Chernow, 2004: 348). This was a direct bid by the federal government to interfere with the creation of credit, and ease the impact of the scarcity of currency, in a direct bid to fulfill its role of enabling the free flow of commerce.

The First Bank was capitalized with ten million dollars worth of gold, while the average bank at the time held less than one million dollars in capital (Chernow, 2004: 348). This difference in capitalization gave The First Bank a disproportionate influence over the issuance of credit, with the potential that federally issued credit would drive out the existence of state bank issued credit. The potential influence that the federal government would gain by being able to control the supply of credit, met with the banking and merchant classes fears that the government would issue credit to their disadvantage. Hamilton attempted to guard against this fear by limiting the government’s ability to manipulate or control this national bank:

“To attach full confidence in an institution of this nature, it appears to be an essential ingredient in its structure that it shall be under a *private* not a *public* direction, under the guidance of *individual interest*, not of *public policy*.” (Hamilton qtd. in Chernow 2004: 349)<sup>14</sup>

Despite this effort, the First Bank would have to shut its doors by 1811, having lost its congressional bank charter, in great part the result of political conflicts and certainly not due to a lack of financial success. However, within five years, the Second Bank of the United States

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<sup>14</sup> This model of private control, with limited government influence, would act as the model for all future federal attempts at building a national banking system, including the Federal Reserve System created in 1913.

(hereafter referred to as the Second Bank) was chartered. The Bank was created by many of the same congressmen who had refused to renew the charter of the First National Bank. However, Madison and the other congressmen had realized that they needed a way of raising reliable supplies of credit during the height of the War of 1812. This was because the war was placing massive constraints on the political economy, with shortages of currency threatening the continued free flow of the commercial economy and of the federal government's war efforts. Despite its success the Second Bank would also lose its bank charter in 1841, a victim of President Andrew Jackson's "bank wars" of the 1820's and 1830's (Davies, 2002: 475-478). The National Banks may have failed but they also reinforced the federal government's commitment to an idea of money that accepted government's inability or right to create money. The only potential role, at least argued for by some members of the federal government, was to regulate the supply of credit. The focus on credit was reinforced by the belief that creating increased supplies of credit only had short-run impacts on price levels, therefore limiting its inflationary impact (Laidler: 1991).

This meant that credit was framed as not being disruptive to class relations. If credit could be created in a way that was reliable, then it had the potential to offer a solution to the tension between the expanding commercial economy and a scarce supply of gold money. It was a very different solution from the one that the colonial state legislatures of the late eighteenth century had attempted to do when they explicitly set out to create higher levels of inflation via the creation of increased supplies of paper money. Those legislatures had attempted to print paper money (with the same value as gold), and not new supplies of credit. Many of the legislatures viewed this as a beneficial process because it was assumed that the increased quantity of money and the resulting higher inflation would benefit the majority of the population. It would reduce debt burdens and increase the ability of businesses to pay wages, benefiting the majority who were dependent on wages for economic survival. The federal government's attempts at creating a national system of credit showed its desire to reinforce the theories of scarce and natural money. The six decades between the creation of the First Bank and the end of the Second Bank was a period marked by the failure of the federal government to create a national system of



reliable and flexible credit supplies. The lack of a reliable system of national credit would force the government to take a new approach to currency creation a mere twenty years later.

In light of the federal government's previous focus on creating credit, and not duplicating the efforts of the colonial state legislatures, the decision in 1862, to issue new money into circulation, in the form of paper, was a surprise to many and led to a series of challenging and illuminating debates.<sup>15</sup> Put into the context of the previous failed attempts at creating a national bank, the federal government was in desperate need of a reliable supply of currency to fund both its military operations and guarantee the free flow of commerce.

The Civil War was placing great strains on the political economy and the federal government could not rely on the banks to create adequate supplies of credit. At the outset of the war, "A supply of gold and silver coin could in no way be depended on. It has been noted that hoarding had begun even before the suspension of specie payments" by banks (Sharkey, 1959: 34). The hoarding of gold by banks, businesses, and citizens placed massive constraints on the flow of money, reducing the ability and willingness of many banks to issue credit. Seriously complicating the situation was the inability of the federal government to sell Treasury bonds, further limiting the federal government's ability to finance its war operations. In those few cases when banks did issue credit, it was often assumed that they were over-leveraged and their creditworthiness was questioned. All of this resulted in a real shortage of available currency, and without a national bank system in place there was very little the government could do to increase the supply. In the end, the decision taken by the federal government was to protect the continued operation of the commercial economy, "it seems that the "necessity" of the situation was not in protecting the credit of the government but in supplying a medium of payment, in other words a currency" (Sharkey, 1959: 33).

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<sup>15</sup> This section covering the debates over the creation of paper money during the Civil War is based on archival research performed at the University of California at Berkeley, while a Visiting Student Researcher in the Department of Geography. In particular the section draws on five-volume set of original financial pamphlets that were published and distributed between 1820 and the late 1890's (see Pamphlets of Finance, Vol. 1 – 5).

The decision to print paper money opened up a debate, for the second time in America's history, over the source of money's value and the role of government in the creation of this value.<sup>16</sup> These debates, "established that the way in which that institution [of money] worked was itself the result of human intervention" (Laidler, 1991: 188). During what was a relatively brief moment in history, government's role in the creation of money's value, not just in the supply of credit, was established and confirmed. Those that supported the right of the federal government to issue this paper money would marshal arguments that placed the source of money's value, and therefore the creation of money, in the hands of government. These arguments challenged the very foundation of the then accepted theory of money. These arguments and the actions of the federal government threatened, in the eyes of many, existing class relations and property rights, and therefore the entire political economy.

The first Legal Tender Act went into effect on February 25, 1862 giving the right to the United States Treasury to create, for the first time, paper money (United States. Cong., 1862: 345). The second and third Legal Tender Acts were issued in 1863 and under them a total of four hundred and fifty million dollars worth of paper money was issued (Davies, 2002: 487).<sup>17</sup> This paper money was officially issued at a one-to-one relationship to gold. This meant that the paper money had the same purchasing power as gold.<sup>18</sup> The important point to note is that when this paper money was originally issued it was *not* redeemable in gold. This meant it was not a "representation" of gold, but was presented as if it had the same value as gold. The fact that this paper, created and issued by the federal government, could not be redeemed for gold is what made it money, and not credit, in the eyes of many.

It was this part of the Act that caused the greatest concern. This paper money was meant to retain equal value with gold, and act as a monetary base upon which a bank could issue new credit. In other words, the federal government had increased the total supply of money, and not

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<sup>16</sup> The first debates over money's value and government's role occurred during the creation of the Federal Constitution and the colonial state legislatures creation of paper money in the 1770's.

<sup>17</sup> This paper money became known as greenbacks, a term still used to refer to the US dollar in the twenty-first century. These greenbacks are not to be confused with the Greenbacks who were members of the political party called the Greenback Party.

<sup>18</sup> One could also say that the paper money was issued on par with gold.

just of credit. The federal government assumed that this, based on the prevailing theories of money, would result in inflation. The federal government attempted to mitigate this inflationary impact by presenting this additional money supply as a temporary solution. By presenting it as a temporary solution the federal government was attempting to follow the historical argument that credit only had temporary impacts on inflation levels. If this paper money was only going to be around during the war, then its long-run inflationary impact will be greatly reduced. The federal government was claiming that it was just a temporary war measure, used to save the continued operation of the federal government and the overall commercial economy. And at the same time the government gave clear signals to the banking and merchant classes that it had not given up on gold as the true money or, for that matter, the idea of a naturally scarce supply of money. In the Legal Tender Act the federal government states that paper money:

“shall be receivable in payment of all taxes, internal duties, excises, debts, and demands of every kind due to the United States, *except duties on imports*, and of all claims and demands against the United States of every kind whatsoever, *except for interest upon bonds and notes, which shall be paid in coin*, and shall, also be lawful money and legal tender in payment of debts, public and private, within the United States.” (United States. Cong., 1862: 345) (Italics added)

The truth of the government’s action is betrayed by this clause, a clause that would be included in the two subsequent acts authorizing the issuance of paper money (United States. Cong., 1863: 709, 822). The government was not ending the role of gold as the monetary base. Instead, it was guaranteeing that bondholders and lenders to the federal government would have both their interest and principle paid in gold, signaling that it still gave preference to gold money and to the interests of those that held gold. The federal government knew that it would struggle to get buyers of its bonds to accept paper money.

Despite the fact that at first glance it may appear that the federal government was following in the footsteps of the eighteenth century colonial state legislatures, it was in fact doing nothing of the sort. It certainly was not trying to reduce class inequality or benefit the indebted, what it was

attempting, in a time of crisis, was to guarantee the free flow of commerce and the continued operation of the political economy. The federal government knew that it would continue to need access to gold, and that paper would not, and had not, historically held its value.

Despite the federal government's stated commitment to gold, the Legal Tender Acts met with the immediate protest from the banking and merchant classes.<sup>19</sup> The advocates of gold money resorted to arguments centered on the immorality of paper, the fact that it held no intrinsic value, that it would have inflationary impacts on price levels and very importantly, represented a loss of private property. The summation of all of these arguments was that paper money would threaten the existence of private property, class relations and the continued operation of the commercial economy. George Curtis, a lawyer who argued against the legality of the Legal Tender Acts said, "It is apparent that no question of greater magnitude, touching the rights of property" has come before Congress and the idea that, "Congress can compel a private creditor to receive his debt in the latter, when this debtor contracted to pay only according to the former standard" is of grave concern (1862).

Another voice on the side of gold money was Representative Blair, a member of congress, who claimed that even if the federal government were to demonetize gold, by ending its legal tender status, it would retain its value and therefore its natural ability to act as money (1876). Blair's words echo a long standing belief that, "real money is property, and not a creation of government" and that gold had been, "universally used as such by civilized people" for centuries (1876).<sup>20</sup> These are not concepts of money introduced by Blair or Curtis, these are long held beliefs of money that were articulated clearly by the Federalists starting in the 1780's. This bullionist conception of money reinforced the idea that any attempt to reduce money's value or threaten one's ownership of it, was a violation of your private property rights. This is exactly what Blair articulates when he states that the, "essential and inalienable right of every man to the

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<sup>19</sup> This led to a series of legal cases that went all the way to the U.S. Supreme Court. The first of these cases, *Hepburn v. Griswold* (1870), overturned the Federal government's right to issue legal tender. However, in 1871, the question over the legality of legal tender returned to the court. And, in two cases, *Knox v. Lee and Parker v. Davis* (1871), and, again in, *Julliard v. Greenman* (1884), the constitutionality of the Legal Tender Act's were confirmed, resulting in the overturning of the court's 1870 decision and the retention, by the federal government, of the right to declare and create legal tender.

<sup>20</sup> Representative Blair, is one of several voices in congress that spoke of gold in this way. A reading of financial pamphlets of the 1870's and 1860's will highlight the commonness of these understandings of money. See the Financial Pamphlets Vol. 1-5.

ownership of that which his labor has produced and to dispose of it as his inclination of wants require” is of paramount importance and applies importantly to money (1876).

The clause in the Legal Tender Acts had said nothing about private debts contracted between private citizens, and it was argued by Curtis, Blair and others that the government was forcing people to give up gold (and therefore their property rights) for paper which held no natural or intrinsic value, and were threatening the political economy. They believed that the paper money would result in negative socio-economic consequences, and ultimately upset the structure of society and threaten the existing political economy. Curtis argued that:

“The passing of such tender-laws was expressly prohibited to the States. It was not expressly prohibited to Congress, because it never was imagined that a government, on which was imposed the duty of creating and maintaining a metallic standard of value, could do anything so inconsistent with the purpose of its own existence as to make the market value of paper a measure of the legal obligations between creditors and debtors.”  
(1862)

Curtis goes on to say that, “this law lies outside of the measure of the authority given to Congress...it is repugnant to a great trust and duty imposed upon Congress” (1862).

According to these views the federal government was attempting to do something that was completely outside of the bounds of its authority, and was threatening its very existence. For Curtis and others this creation of paper money and of unnatural value was a threat to the very roots of the American capitalist democracy. In 1868, an advocate for gold said:

“We may invent, and devise, and try to circumvent the natural laws on this subject to the end of time, and we shall end just where we began. There can be but one universal standard of value, and the attempt to substitute anything else for it will inevitably fail.”  
(Pike qtd. in Babb and Carruthers, 1996: 1572)

Supporters of gold money were emphatic in their arguments against attempting to place the source of monetary value in government. Bullionists, who were inevitably from the merchant and banking classes, had the added bonus of being the classes with the most direct political power and influence. They believed, as had been assumed by the Federalists, that they understood best how to protect the continued free flow of commercial exchange. General Garfield, a Civil War hero and future president of the U.S.A. believed that, “Money is a reality, a weight, of a certain metal, of a certain fineness. But a paper dollar is simply a deed, the legal evidence of the title that I hold to a dollar” (Garfield qtd. in Babb and Carruthers, 1996: 1568). Blair (1876) summed up the dominant understanding of gold, and the source of its monetary value in a speech he made to congress on May 18, 1876. He argued that the money value of gold is, “independent of and more necessary than any government” because it, “possesses value as a commodity” while there are those on the side of paper who are claiming that, “real money is not intrinsically property, but a mere token or sign, endowed with power to cancel debts” (Blair, 1876).<sup>21</sup> Highlighted in this distinction is the perceived difference between an assumed and natural source of value, belonging to gold, verse the legislated or assigned value of paper money created via government.

These arguments, and the reinforcement of gold as money, seemed to have won when Congress passed the Public Credit Act, in March 1869. This act affirmed the Treasury’s commitment to paying all principle and interest to bondholder’s in gold (Unger, 1964: 43). And, on the January 14, 1875, Congress passed the Specie Payment Resumption Act, which stipulated that all federally issued paper money be returned to the Treasury and redeemed for gold, at face value, by January 1, 1879 (Davies, 2002:496). Confirm congresses belief that paper could not be money, a report presented to the U.S. Congress in 1877, stated that money value, “inheres in the quality of a material thing, and not in mental estimation” (Babb and Carruthers, 1996: 1567).

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<sup>21</sup>. The cancelling of debts mentioned in this quote is picked up by Babb and Carruthers (1996) who argue for a theory of credit-money based on the idea that all money is actually credit with a matching debt. This means that money can never be created, under our current system of finance, without a corresponding debt (see the works of Babb and Carruthers (1996); Ingham (2000, 2004); Hart (2001).

The passage of the Specie Resumption Act and the possibility that the supply of currency (money and credit) in circulation would contract, led advocates of paper money to form a political party that would go on to make some of the most nuanced arguments in support of government issued paper money. In 1875, these individuals would form the Greenback Party and by 1878 they secured, “over a million voters and returned fourteen members to Congress” (Davies, 2002: 496).<sup>22</sup> The Greenback Party’s efforts, in part, were driven by the concern that a reduced volume of currency would have a negative impact on the overall political economy. The Greenbacks argued that removing the supply of paper money from circulation would reduce the ability of businesses to hire labor, further exacerbating the level of unemployment and the resulting social instability.

In the process of making their arguments the Greenbacks challenged several of the fundamental assumptions made by advocates of gold money; they began to articulate a theory of currency creation that placed government at the center. Representative William Keeley, an advocate for paper money and a member of the Greenback Party, argued that the addition of the paper money was a positive development, having saved the economy of the USA:

“It may have been unwise to use that ‘great enemy of the nation, the greenback,’ and thus increase the volume of money and enhance prices; but let it remind gentlemen, who say that the greenback is an enemy to the country, that they decry their country’s savior” (1877).

Keeley is arguing that this money supply increase did not disrupt or upset the political economy, in fact it enabled it the economy to expand. The goal of this paper money, according to Keeley (1877), was *not* to disrupt class relations or threaten the free flow of commerce. Rather, it was about enabling those that wanted to work to work and to help make this happen the government was being asked, “to maintain a familiar medium of exchange whereby capital and enterprise may pay labor for its work” (Keeley, 1877).

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<sup>22</sup> The Greenback Party would not survive past the late 1880’s losing political support rapidly (Davies: 2001)

A subtle but critical shift is happening here; the Greenbacks are arguing that paper money has the ability to save the political economy. In fact, they see it as the savior of the commercial economy and that it had prevented any serious disruption to class relations and the overall political economy. This challenged the historical belief that paper money was disruptive and a danger to the free flow of the commercial economy, instead the Greenbacks were arguing that it does the exact opposite. In 1877, Representative Ewing claimed that, “business distress was least when currency was fullest, and that the contraction of the currency... arrested prosperity” and that this shook, “the firm foundations of order and prosperity” (1877). Keeley, in his argument against the Specie Resumption Act, states that the government must:

“Allow the millions of working men and women who are living in despair to go to work upon our raw materials, and supply each others’ wants, while the merchant, who makes the exchange between them, shall levy toll for profit as he did before this madness seized upon us.” (1877)

Further, Keeley sees the inflationary impact of increased monetary supply as a positive force on the operation of the economy and boosting the ability of workers to obtain work. He states that, “There is an inflexible law regulating the relation between prices and the volume of money in circulation” and with increased prices come increased profits, resulting in the increased ability to do business and purchase labor (Keeley, 1877). Even though it is evident that Keeley and the Greenbacks are pro-capitalist there is a subtle but critical shift in their understanding of the source of money’s value. By assuming government has the ability to create the money needed to fuel commercial exchange, the source of value is being socialized and consciously politicized. Or, to put it another way, the source of money’s value is being denaturalized.

In a pamphlet published in 1870 the author writes, “we do not need gold or silver for money, or as a basis for paper currency. All the money we need is legal tenders issued by the government” (Smith). The author is challenging the role of these natural sources of monetary value and shifting the source of money onto government. The Greenbacks argued that the value of money has everything to do with the legal authority of government, and nothing intrinsic to gold,



“Money is a creature of law, it is created and upheld by law” (Wolcott qtd. in Babb and Carruthers, 1996: 1572). The notion that government could create money through acts of law, placed the source of monetary value in its hands, and challenged the theory that money’s value was natural and outside of any legal act of government:

“All money, whether it be gold, silver or paper, derives its chief value from the fact that governments do enact arbitrary laws declaring money for the payments of debts, thereby creating the chief demand for it.” (Ensley qtd. in Babb and Carruthers, 1996: 1570)

This conclusion raised deeper questions around what control over currency creation meant. An argument emerged that claimed the right of the voting citizens, whose demands would be expressed through their representative government, to control the creation of money:

“We, the people, make the government. We give the government power to make, provide and issue money under proper rules and regulations...We make our money, we issue it, we control it. We regulate it.” (Wolcott qtd. in Babb and Carruthers, 1996: 1572)

The advocates are not claiming their own right to create money or the right of an individual State to create money. It is also importantly not framed as an attempt to challenge the power of the federal government. Rather, the argument is to reinforce the existing system of government, and solve the tension between scarce money and the expanding economy, by placing the power to create money in the government’s hands. These are important distinctions, separating the Greenback debate from those of the 1770’s or of those that appear in the 1980’s.<sup>23</sup> In fact, it could be viewed as the historian Sharkey has claimed, that all of the debates including the radical ideas of the Greenbacks, were aimed at perpetuating the existing class relations and not disrupting the system of governance that relied on the idea of natural inequality and private property (1959: 33).

The Greenbacks had made a subtle shift, focusing attention on the source of value and raising the question of what it meant to have government control the creation of money; “The greenback

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<sup>23</sup> The debates of the 1980’s are those of the community currency movement, a subject that is dealt with in great detail in Chapter Three of this work.

debates contested the nature of monetary value and the proper role of democratic government in finance” (Babb and Carruthers, 1996: 1573). For advocates of gold money the source of money’s value depended on a separation between government and money creation, but supporters of paper money did not accept this separation. According to the Greenbacks the responsibility of government was to guarantee the supply of a sufficient amount of currency so as to enable the sellers of labor to find willing buyers. For the Greenbacks the historical idea of a limited or scarce supply of money was not natural, but rather the result of a social decision, one that can be changed.

The rise of a political force that articulated the need for an adequate supply of currency, and linked the source of money’s value to political decisions reinforced by legal tender laws, enabled them to place the responsibility for maintaining this currency in the hands of the federal government. The Greenback Party had managed to rearticulate the long running tension between a concept of scarce money and an expanding economy, by showing that there need be no real shortage of money. The solution that the Greenbacks were pursuing was one aimed at expanding the commercial economy by expanding the volume of money, not by increasing the volume of credit (and the associated trappings of debt and money scarcity).

This important distinction places the responsibility for sufficient supplies of currency on the government and not on the banks. Importantly, it attempted to break down an idea that claimed the creation of money was outside of government’s control. The Greenbacks central argument, according to Babb and Carruthers and Carruthers was that, “economic value could and should be subject to conscious, democratic control” (1996: 1573).

In challenging the historical notion of natural money they had articulated an idea that the source of money’s value was deeply imbedded in government and the types of laws and decisions it makes. Despite the fact that the Greenback Party never specifically argued for the “democratization” of money, they did argue for its politicization. They see it as a political conversation, driven by government who is voted into power on the assumption that they will

represent the interests of the people. However, placing this into the broader arch of history it is clear that those “representatives” are closely aligned with a particular view that argues for the naturalness of money value and class inequality. These elements are not political discussions, but rather facts of nature. They emerge regardless of any actions of government and therefore any effort by government to interfere with them will result in the disruption of class relations and natural inequality.

January 1, 1879, the date stipulated by the Specie Resumption Act by which all paper money was to be returned for gold to the Treasury, came and went, and over three hundred million dollars worth of greenbacks (as the paper money came to be called) remained in circulation and retained their status as money into the twenty-first century (Davies, 2002: 496). Due to their legal tender status, these greenbacks retained a privileged status as a form of currency that could be used to settle all debts and taxes with the government, and private creditors. This was very different from state banknotes, which could not reliably be used to pay federal taxes or customs, and often would be greatly discounted when redeemed at a non-issuing bank. The result was that greenbacks retained their value and started to build confidence in the ability of paper to be a reliable means of exchange, and eventually (by the late 1970’s) to become a replacement form of money.

This is a critically important moment in American history – the remaining paper flowing around as money and retaining its value on par with gold – because it subtly influenced and gave support to some of the emerging (and somewhat radical) theories of managed paper money systems that were currently being explored at least within academic circles (Laidler 1991: 198).<sup>24</sup> The Greenbacks had managed to introduce ideas into political debate that pointed to the role of government and showed the potential for alternative ways of creating money, that in fact would be, despite historical beliefs, compatible with the existing system of commercial exchange.

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<sup>24</sup> Knut Wicksell, and other monetary theorists of the late 1880’s and 1890’s, had begun to work hard on theorizing credit and exploring non-specie based monetary systems (Laidler 1991: 198). Their efforts were driven in great part by their desire to create a system that was more stable and that would give the capitalist economy a more reliable medium of exchange. The solutions and ideas that emerged during this period would impact the likes of J.M. Keynes who built much of his earlier work off the theories of Knut Wicksell (Laidler 1991: 198).

These ideas were subtly reinforced by the continued use of paper money by everyday citizens for decades to come.

Despite this acceptance, and appearance that the continued circulation of paper money was not damaging the economy, the concern of the banking class persisted. In a speech given during a Banking Association meeting in 1885, the argument persisted that, “History overflows with instances of suffering and disaster occasioned by governments experimenting with the money of the people” (Haven 1885:42). The efforts of the banking and merchant classes to end the role of paper money would finally gain the upper hand when, in March of 1900, the Gold Standard Act was passed confirming that, “gold monometallism had, belatedly, legally captured what was to be its most powerful convert”, the U.S.A. (Davies, 2002: 499). By passing this act the federal government had renewed its commitment to a scarce currency supply, and the belief that it could not create money.

This critical shift back towards a concept of money that retained ideas of scarcity and natural value, returned credit creation to a central role in the political economy. This was again presented as the solution to the tension created between a naturally scarce supply of money and an ever-expanding capitalist economy. This return to gold highlighted the influence of the banking and merchant classes on the policies of the federal government. The claim made by the bullionists was that a system of gold money with abundant supplies of credit was the most stable and compatible system of finance. This, according to the bullionists, was what would enable the continued existence of the American capitalist democracy.

Despite these claims the American economy experienced another in a long series of banking crises in 1907. This one started in New York City and spread through the entire country’s banking system, “which demonstrated that just being on the gold standard was no guarantee of either monetary stability or of the safety of the banking system” (Davies, 2002: 500). What had occurred since 1870 was a massive increase in the concentration of gold money in six banks, all based in New York City. These banks held over seventy-five percent of the country’s gold

reserves by 1907, up from forty percent in 1870 (Davies, 2002: 502). During the two years that marked the crisis, two of the largest financial banking trusts collapsed, further highlighting the reality that large financial institutions could collapse, and not just smaller supposedly less reliable state banks. Once again the scarcity and hoarding of gold money had contributed to the failings of the financial system. Not only this, but again, the federal government had no access to money or a central bank that could help make up for the sudden shrinking in the currency supply marked by the bank collapses.

Essentially there was no way for the federal government to help ease the impact of the collapse on credit supplies. From the perspective of those that would come to design the solution to this tension, the need was for an elastic supply of credit that would increase and decrease as the economy demanded without causing runaway inflation or deflation. The critical element was that this system *would not* threaten existing class relations and did not place the power of money creation in the government's hands because it retained gold as the monetary base. In response to the crisis of 1907, and compounded by the long history of banking collapses throughout the continental U.S.A., the U.S. Congress created the National Monetary Commission, which was part of the Aldrich-Vreeland Act, passed in May 1908 (Davies, 2002: 503). The National Monetary Commission was set up to explore the creation of a central bank that could issue adequate supplies of credit in an orderly and flexible manner, with the idea that this would limit the constant and erratic supplies and value of credit. The second part of the act was the creation of National Currency Associations that could, "issue temporary currency up to a maximum for the country as a whole of \$500 million" (Davies, 2002: 503). The federal government was showing its renewed willingness to get involved in the creation of credit. Importantly, it was not threatening to get involved in the creation of money, as it had done during the Civil War, but was rather renewing its commitment to a financial system of scarce money with a reliable, abundant and flexible form of credit. In many ways this was no different than the nineteenth century attempts of the federal government to create a national banking system.

The outcome of the National Monetary Commission's suggestions was the Federal Reserve Act, which became law on December 23, 1913, finally creating a national system of banking. For the first time America would have one form of currency, with a uniform unit of account, the dollar, that would be acceptable throughout the U.S.A. and would be both flexible and reliable in terms of its quantity and value.

In a letter that U.S. President Wilson wrote to a senator a few months before the passing of the act, he described the effort at creating a national banking system:

“Suffice it here to say ...it provides a currency which expands as it is needed and contracts when it is not needed: a currency which comes into existence in response to the call of every man who can show a going business and a concrete basis for extending credit to him.” (qtd. in Brands, 2003: 28)

This quote highlights the fact the federal government's solution is designed to fulfill its historical role of enabling the expansion and free flow of the commercial economy. The lack of a flexible supply of currency had been an oft-cited problem since the late eighteenth century. As radical as the Federal Reserve System appears, it was actually part of a centuries-long efforts at creating a flexible currency supply. In addition, the Federal Reserve includes and reinforces the federal government's commitment to a system of finance that is compatible with America's capitalist democracy.

Following in the footsteps of Hamilton, President Wilson claims that the, “power to direct this system of credits is put into the hands of a public board of disinterested officers of the Government itself who can make no money out of anything they do in connection with it” (qtd. in Brands, 2003: 28). This is almost identical to the clause that Hamilton had included when he created The First Bank in 1791. It was an attempt to make sure that the interests of the banking and merchant classes were directly represented, while also appearing to be designed to benefit everyone. The inclusion of a board comprising of private citizens meant that the interests of commerce, not of politics, would drive its decisions.

This is a repudiation of the Greenback Party's arguments for politicized money, money that would have been created by government for society, with no associated debt or credit. President Wilson stated that, "We shall deal with our economic system as it is and as it may be modified, not as it might be if we had a clean sheet of paper" (qtd. in Davies, 2002: 503-4). President Wilson and the federal government wanted to create a more stable financial system that would enable a flexible and more reliable source of currency, he claimed that the Federal Reserve System was created to, "furnish an elastic currency, to afford means of re-discounting commercial paper, to establish a more effective supervision of banking" (qtd. in Davies, 2002: 503).

President Wilson claimed that this new system would result in the, "democracy of credit" (qtd. in Wickware, 1915: 51). The democracy that Wilson is talking about is the version in which the democratization does nothing to change socio-economic inequality. It is safe for President Wilson to make this claim because credit is not associated with long-term disruptive inflation and therefore is not seen as a threat to the political economy. Yet the historical failure of the financial system to provide sufficient and reliable supplies of credit was seen as a danger to the overall smooth functioning of the capitalist democracy. It was because of this history of failures that the Federal Reserve System was targeted specifically at reducing the negative impact that the monopolistic power of the banks was having on the economy.

This effort fits with the Federalist notion of limiting the power of any one faction, but at the same time does not attempt to reduce the inequality that causes factions to emerge in the first place. Madison had argued in the Federalist Papers that there were, "two methods of curing the mischief's of faction: The one, by removing its causes; the other, by controlling its effects" (Carey, 2001: 43 [Federalist No. 10]). Madison and the Federalists clearly sided with, "controlling its effects" and in this way the Federal Reserve System is an effort at doing exactly that. President Wilson stated that, "No group of bankers anywhere can gain control; no one part of the country can concentrate the advantages and conveniences of the system upon itself nor its

own selfish advantage. The board can oblige the banks of one region to go to the assistance of the banks of another. The whole resources of the country are mobilized, to be employed where they are most needed” (qtd. in Brands, 2003: 28). President Wilson was not trying to end the existence of bankers, or their wealth, he wanted to be able to influence the system to the advantage of the entire capitalist democracy. The interests of bankers are important, but as the federal government had shown during the Civil War, the continued operation of the economy would take precedence over any faction of class interests.

As radical as President Wilson’s ideas may have appeared, and as much as it appears that he is challenging the power of the bankers. It is a very different approach from the one taken by the colonial state legislatures during the eighteenth century, or the one advocated by the Greenback Party in the 1860’s. For the federal government, any attempt at the democratization of credit (or money) had to be done in a way that would reinforce, and not threaten, the stability of class relations. In this way President Wilson’s actions and the creation of the Federal Reserve was aimed at this singular purpose – class stability. The monopolistic and inelastic financial system was continually threatening the operation of the federal government and more generally the capitalist economy. Attempts in the late eighteenth and early nineteenth centuries, the creation of greenbacks in the 1860’s and now the Federal Reserve System, were all efforts of the federal government to resolve this historical challenge. All of the solutions were driven by prevailing understandings of money and credit and the final solution rested on naturally scarce money with abundant credit. Over the next several decades credit would become central to the forward momentum of the capitalist economy.

Joseph Schumpeter, forty years later, would highlight the importance of this system of credit to the overall existence of the capitalist economy:

“Credit operations of whatever shape or kind do affect the workings of the monetary system; more important, they do affect the workings of the capitalist engine – so much so as to become an essential part of it without which the rest cannot be understood at all.”  
(qtd. in Ingham 2000: 80)



The federal government had finally achieved its goal of creating a flexible and abundant system of credit, based off a finite and scarce monetary base. One of the most critical assumptions underpinning and driving the return, over and over again, to a system of scarce money was the idea that class inequality is natural and not the result of any government action and that the creation of abundant supplies of money would result in the leveling impact of inflation. To emphasize this, the argument is made that any attempt by government to intervene in this inequality (to level society) is both unnatural and dangerous to the smooth operation of class relations, which are a key element in the successful and smooth operation of the commercial economy. Money as gold is framed in much the same way as class was framed by the Federalists – as natural and existing prior to any action taken by government. And, any attempt to create a more abundant form of money is viewed as disruptive to class relations and a threat to the already existing set of political economic arrangements. This approach relied on the continued reinforcement of natural and alienated value, separating the government and society from money's source of value and production. To do this the federal government had to entrench and reinforce ideas of gold as money, and build an institutional system that could provide the types of credit that were understood as necessary to the overall functioning of the economy.

Over the almost two hundred and sixty years since Hume's essays on money, the dominant theory of the source of money has stayed essentially the same (Laidler: 1991; Ingham: 2004). One realization that had not shifted was that, "a necessary condition for control over the general price level is control over the money supply" (Laidler, 1991: 33). If the amount of money was critical to controlling the price level, and inflation was detrimental to the overall capitalist political economy, and especially threatening to the banking and merchant classes, a type of money needed to be chosen that was naturally limited. This led to the continued reinforcement of the gold as the monetary base; despite evidence that bimetallism or government managed paper money systems were far more preferable to the overall political economy (Laidler, 1991: 187). The fact that policy lagged behind theory serves to highlight the role of particular interests,

political and economic, and the forward momentum of existing philosophies and theories of money. The fear at the time was that these conclusions, if carried out, could result in too much discretionary power being given to government and policy makers (Laidler, 1991: 188).

This point made by Laidler (1991) is important because some of those people who had intellectually recognized the advantage of a financial system not dependent on a scarce commodity, were hugely influential in policy circles during this period. They included the likes of Irving Fisher and Alfred Marshall who as, “leading quantity theorists also understood how a managed currency could be made to work” but they, “stopped short of advocating it” (Laidler, 1991: 188). Late twentieth century orthodox economists continued to cling to their “model of money supply” which was, “an empirical generalization of a naturally constrained supply of a metallic monetary base provided by a central authority (the mint) that was outside the market” (Ingham 2004: 21).

Despite the appearance that the closing of the gold window by President Richard Nixon in 1971 fundamentally ended the role of a scarce monetary supply, the theory was merely modified to account for the switch from gold to paper by saying that, “the stock of government debt, rather than the stock of gold” held by the central bank becomes, “high-powered money” (Ingham 2004: 208). This retains the illusion of a scarcity of money for several reasons: it is still built off the notion that government itself cannot create money. Government is required to take on debt in the form of Treasury bonds if it wants to create more liquidity. However, neither the Federal Reserve nor the general public has to purchase these bonds, and if they do they expect to earn interest.

This means the government has to constantly realize increased economic growth, for increased tax revenues, to make sure adequate supplies of money are coming into the government treasury so as to be able to repay bondholders. In this way the government cannot issue bonds indefinitely. If they do, one or both of two things will happen: firstly, the demand for government bonds will decrease as the market gets either flooded by the supply of bonds or,

secondly interest rates will rise due to the perception that the government is overleveraging itself and will not be able to repay its debts. This market-based approach to money also retains a sense of naturalized monetary value in that it is the market that determines the value of the money, not the government. Again, the source of money's value is not in government's hands but in the hands of the markets, in essence a naturalized space that exists regardless of any actions of government.

The historical trajectory of the financial debates in the U.S.A. has always pursued the same goal – the reinforcement of the system of commercial exchange and the underlying inequality of class relations and property ownership. However, there is another debate that has run in parallel to this one, and that is marked by the efforts of the colonial legislatures in the 1770's, and in several critical ways by the Greenback Party of the 1870's, and a new movement that has risen since the 1980's known as the community currency movement.<sup>25</sup> These other debates have repeatedly attempted to challenge this notion of scarce money. The efforts of the community currency advocates in the late twentieth century pick up on some of these earlier arguments, highlighting the social element of money and claiming that individuals can create their own money. These advocates of community currencies argue for the democratization of money, and they see little necessity for a scarce supply of money believing that the current system of credit is deleterious to the economy, and the cause of rising inequality and economic instability and environmental destruction. Whether their analysis of the impacts is correct or not, what they are doing is claiming the right to create money, and attempting to end the idea of scarce and alienated sources of money. These efforts present a new and unique phase in the financial debates. They are importantly challenging the role and relevance of both the federal government and the banks in the currency creation process.

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<sup>25</sup> This is the subject of Chapter Three.

**Chapter Three:  
Democratizing Money:  
Ending the Role of the Federal Government and Banks in the  
Creation of Money and Credit**

Over the course of the first two hundred and thirty years of America's financial debates, the focus centered on designing a system of currency creation that reinforce the class relations underpinning the American capitalist democracy. The policies implemented by the federal government were always carefully calculated to do exactly this. Any effort to create a system of currency creation that seemed to threaten the existing class relations (and their underlying inequality of property ownership) was swiftly blocked by those classes, namely the banking and merchant classes, which stood to lose the most. What the federal government has attempted to do is find a compromise between protecting the commercial economy, while mitigating the negative consequences of the dominant theory of currency creation.

The solution that the federal government has focused on has two essential elements: the first, that money is a scarce commodity, and second, that the best way to relieve the tension created by a scarce money supply and an expanding economy is the creation of an abundant, flexible and stable supply of credit managed by a centralized authority such as the Federal Reserve Bank. The debates that raged over the course of this history, has many nuances and differences, however they have one element in common; they all in some way see a central role for government or banks.

In the 1980's a new series of financial debates emerged that both picked up on and reworked several historical themes in unique ways, while introducing new themes that had never previously been part of the debates. These new debates and their new theories of currency creation are loosely termed, Community Currencies (CCs).<sup>26</sup> The classic themes of quantity, value and inflation emerge again, though in unique configurations.

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<sup>26</sup> This term encompasses a broad range of monetary experiments that go by a range of names: local currencies, social currencies, time banks, local exchange trading systems, local money, complementary currencies. However, the term Community Currencies is used in most academic circles for example see the *International Journal for Community Currencies*, and the International Conference on Community and Complementary Currencies 2011 held in Lyon, France in February, 2011.

Then there is the unique claim that government and banks are not necessary to the currency creation process. This theory claims that individuals or local communities, in a decentralized way, can create their own money, in abundance and for free, with no negative consequences to the political economy. This decentralized and individualistic theory of currency creation flies in the face of the historical trajectory of the American financial debates. This claim is tied directly to a concept of democratization that differs in some fundamental ways to the type of democracy that President Wilson laid claim to in 1913.

CC advocates claim that by creating currencies on a localized and individualized level, without government or banks, both money and the economy will become democratized. For the CC advocates this democracy is one that is local, sustainable, ecological and fair. It is at this juncture that the CC advocates represent a wholly new concept of society. Though in many ways weakly theorized, their arguments anticipate a society in which class inequality is not accepted as natural.

Unlike the earlier financial debates, these ones are not centered on expanding and enabling the continued operation of the capitalist economy, but are rather looking at ways in which they can use the creation of money to shape new social relations. At times this gets slightly muddled as the CC advocates often call for increasing employment and expanding the economy, both of which are critical elements to any functioning capitalist economy. However, what is important is that they are challenging the very foundations of the dominant theories of currency creation, at the very time that the financial system is again showing serious signs of weakness and systemic failures.

Ever since the efforts of the colonial governments in the 1770's, debates over the quantity of currency have been central to the financial debates. Insufficient quantities of reliable money have been blamed, again and again, for seriously impeding the free flow of commercial exchange. Part of the fear, expressed most clearly by the Federalists and the federal government, has been that class relations would be seriously disrupted by the negative consequences of this

currency scarcity. The failed attempts of the Federalists to create a system of national banking, or the creation of greenbacks in the 1860's, or the creation of the Federal Reserve System in 1913, are all policies that the federal government implemented in an effort to expand the total currency supply. The federal government's policies have always respected the critical role of scarce money in support of bullionist ideas expressed by merchants and bankers. This led to an idea of money that claimed that government had neither the right nor ability to create money. During the 1860's and 1870's the Greenback Party was able to articulate an argument that centered on the claim that the scarcity of money was not a natural phenomenon beyond the control of government, but was rather a political economic choice and that we, as a society, through our government, could create money. The Greenbacks wanted government to take a central role in the money creation process, not just in managing the supply of credit. The efforts of the federal government were always made easier by the simple fact that all previous efforts at expanding the supply of currencies had centered on giving more power to the government (federal or state) or banks. These were considered the only two actors in the currency creation equation and it was never proposed nor imagined that individuals or disparate local communities could or would create their own money.

The CC advocates, in ways that are similar to those of the Greenback Party, stand firmly behind the belief that there is no need for scarce supply of money and currencies more generally. On the website of one of the oldest CC's called Ithaca Hours, based in Ithaca, New York, they state that they, "are expanding the money supply rather than merely shuffling money around" (Ithaca Hours). Michael Linton, a pioneer of one of the largest and most successful CC systems called the Local Exchange Trading System (LETS), states in his "Open Money Manifesto" that, "where conventional money is scarce and expensive, the new money is sufficient and free... imagine having enough money, sufficient to meet all our needs" (Linton).<sup>27</sup> Bernard Lietaer, an author and advocate of CCs, links the scarcity of work with the scarcity of money and believes that:

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<sup>27</sup> There are several thousand communities around the world utilizing the LETS technology, which is completely virtual based. Each community self-organizes and manages their accounts accordingly. The value of the currency in each community differs, though there are ways to exchange currencies from one community with another – however this is fairly limited in practice. The system is based on the idea of a mutual credit system, which means that at any time all credits match debits meaning that any moment the entire system can zero out (Linton).

“The problem with work is finding someone who will pay you dollars for it, i.e. make it a paid job as well. The scarcity in jobs is, therefore, a money scarcity, as economists have known since Keynes. But does money have to remain scarce? Why not create your own money in sufficiency to complement the scarce national currency, and thereby enable more work to be paid? Sounds crazy? Too simple?” (1999: 13)

In many ways Lietaer wants the same thing that paper money advocates of the nineteenth century wanted, “a familiar medium of exchange whereby capital and enterprise may pay labor for its work” (Keeley, 1877). The Greenback Party wanted to see the commercial economy continue to operate and for business to be able to create jobs, and they argued that the best way to do this was to increase the supply of money via the government’s creation of paper money.

While CC advocates may want to create jobs, and increase the supply of currencies, they make one critical distinction – they claim that individuals or local communities can create their own money without any involvement of the government or banks. While the Greenback Party had argued for the government to step more fully into the creation of money, supporters of the paper money claimed that, “we do not need gold or silver for money, or as a basis for paper currency. All the money we need is legal tenders issued by the government” (Smith, 1870). The Greenbacks saw government as the source of money and that it had the ability to end the scarcity of both money and credit. The Greenbacks efforts were singularly centered on socializing and politicizing the creation of money via giving this authority to the federal government, something deeply feared by advocates of bullion.<sup>28</sup>

The CC advocates see this increasing politicization and the Federal Reserve System resulting in the centralization of currency creation. They see it as an effort to privatize currency creation, and the resulting system as both unstable and singularly focused on benefiting the wealthy merchant and banking classes. On the website of Berkshares, a CC based in the northeastern U.S.A., they claim that, “The banking system is one of the most centralized institutions of our

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<sup>28</sup> This is the debate, in part, that Chapter Two engages in an effort to show how the battle over the role of government in the creation of money and credit settled on a compromise which resulted in the creation of a Federal Reserve System marked by scarce money and abundant credit.

economy and one of the major obstacles to strengthening regional economies and the communities within them” (“What Are Berkshares?”). However, the Federal Reserve was created, in great part, to do the very opposite. It was created to limit the negative impact of the nineteenth century pattern of hoarding and monopolization of gold money by the banks. And, in particular to deal with the resulting inadequate and unreliable supplies of credit, which were especially threatening to the free flow of commercial exchange and a threat to the entire political economy.<sup>29</sup>

The earlier system of decentralized banking and multiple paper currencies with different denominations had created massive and repeated economic problems. Despite this history, in a paper published in the early 2000’s, on the website of the E. F. Schumacher Institute, a major advocate of CCs, the authors claim that, “to keep banking honest it would be better to return to a banking system that utilizes competing currencies rather than to rely on a central system” (Swann, 1995).<sup>30</sup> This desire to end the centralized system, and to return to an era of competing currencies is also connected to the idea of ending the politicization of currency creation.<sup>31</sup>

The way to do this, according to CC advocates, is to end the government and bank’s monopoly over currency creation and to instead give power to small local communities and individuals to create their own money. In fact, government doesn’t even need to “give” this power to citizens; citizens just need to assert their power. Thomas Greco, an author and advocate of CCs, states that, “we have called for the separation of money and state, but since the people do not control their government, we believe that separation can only be achieved as the people assert their money power” (Greco, 2009: 111). Greco goes on to claim that it is the “politicization of money [that] has inhibited the widespread adoption of better alternatives” (Greco, 2009: 118).

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<sup>29</sup> See Chapter Two of this thesis.

<sup>30</sup> The E.F. Schumacher Institute, named after the author of the popular book, “Small Is Beautiful” (Schumacher, 1973), is an influential advocate of community currencies. The institute sponsored the 2004 conference, “Local Currencies in the Twenty-First Century: Understanding Money, Building Local Economies, Renewing Community” and have funded multiple CC initiatives across the USA. See <http://www.smallisbeautiful.org/> for more.

<sup>31</sup> Frederich von Hayek, the Nobel prize winning free-market economist, was a big advocate of what he called, “the denationalization of money” arguing for private companies to issue their own currencies and allow the market to determine the value of money (von Hayek, 1976). Part of his argument rested on his antipathy towards what he also saw as the politicization of money. This represents another of the several ways in which the CC movement comes to mirror or build off free-market capitalist economists.



Part of what the CC advocates see as unique about this current moment in history, is the rise of information and networking technologies, which offer a range of possible alternative decentralized approaches to creating money. CC advocates that run several websites and actively work to produce the technological systems that enable anyone to create a currency claim that, “given how much information technology has evolved recently, the members of a community can be their own arbiters” (Brock, “New Currency Frontiers”). The technology is essentially framed as replacing the role of government or banks; decentralized “currency design will mean the obsolescence” of any sort of dependence “on any form of central authority” (Brock, “P2P Currency”). These advocates recognize that they are challenging the history of centralized currency creation, “Almost all currency designs to date (dollars included) depend on either a scarce commodity (such as gold or paper notes) or a centralized authority to issue and/or track the currency (barter clubs, time-banks, etc)” (Brock, “P2P Currency”).<sup>32</sup> For these advocates, “The new frontier is about open currencies which do not exist by mandate of banks or government they are distributed and un-enclosable systems of wealth creation which can be designed to benefit more than a privileged few” (Brock, *et al.*; “New Currency Frontiers”).

Keith Hart, a professor of anthropology, also sees currency creation moving towards this state of decentralization and beyond the bounds of government (Hart, 2001). Greco claims that as part of the necessary steps towards localized and decentralized currency creation we need to, “define and utilize a nonpolitical, concrete standard of value and unit of account that cannot be manipulated to the advantage of any particular bank, cartel, government, or individual” (Greco, 2009: 108). The implicit assumption is that the current financial system has been manipulated to the advantage of certain groups. As has been argued throughout this work, this is exactly what has occurred; the manipulation of the currency creation system, including the scarcity of money, to the benefit of the certain class interests is something that the Federalists never shied away from admitting. All of the solutions that have been implemented by the federal government have focused on making the financial system as compatible with the dominant commercial economy

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<sup>32</sup> I will return to the role of gold and scarce commodities later in this chapter. However, it is important to point out that Brock *et al.* differ from many of the other CC advocates in that they do not see a role for a valuable commodity, and have a different notion of value from that which many of the other advocates adhere to.

as possible, therefore guaranteeing not to disrupt class relations. So CC advocates are completely correct when they claim that the current financial system has been manipulated to benefit certain interests (or classes of society). And their proposed solution can be seen as a direct challenge to the power of this history with the emphasis that the state no longer represents the interests of all classes of society.

Here again, Greco is informative, “since the people do not control their government, we believe that separation can only be achieved as the people assert their money power” (Greco, 2009: 111). CC advocates do not see government as representative of their interests, and therefore they are looking for ways of solving the scarcity of money via new means. This perceived failure of not just the government but also of the banks, signals a key shift in the history of the financial debates. The advocates of CC are not looking for solutions that fit within the historical understandings of class inequality and representative government. In essence the system of representative government, built to enable capitalism, is failing to meet the demands of at least the CC advocates, if not a large swath of society. The potential disruption is huge, and figuring out how to design a system of currency creation that returns a sense that the federal government actually is representing and mediating the needs of all classes, may be of critical importance.

The idea that money can be created in abundance, by anyone without any centralized authority, inevitably leads to the question: How would they retain value? Geoffrey Ingham, an academic and sociologist who has written extensively on the history and social aspects of money, states at the end of his book, “The Nature of Money,” that any answer to the question of scarcity and value of money is the result of a series of class struggles “for economic existence between different interests” and that “without such a struggle money cannot have value” (Ingham, 2004: 204). Ingham claims that the value of money is realized through the struggle over controlling the quantity in circulation. Ingham is claiming that money (and currencies) value is a social construct and not a naturally occurring phenomenon. The call for creating abundant, free, and sufficient quantities of currencies by CC advocates implies that there is no struggle over the

quantity in circulation. How then, in light of Ingham's work, do the CC advocates account for the creation of a currency's value?

In an attempt to answer this question many CC advocates turn to another historical theme in the financial debates - the role of gold or other scarce 'real' commodities in forming the valuable base for a currency system. These ideas of course, echo a long line of bullionist arguments, arguments that are still heard in many of the twenty-first century finance debates. There is a critical difference between the historical bullionist arguments and those of the CC movement. The bullionist arguments were aimed at limiting the supply of money and credit, while the CC advocates see the role of gold (or other commodities) as enabling an expansion of the total supply of money. This strange mixture of arguments marks another unique element to many of the modern financial debates.

Thomas Greco, in his book titled, "The End of Money," argues that, "the official unit of account be declared on the basis of a specific value standard that is defined in concrete physical terms" (Greco, 2009: 207). The belief that the currency's value needs to be anchored in something concrete returns the overall debate to one that mirrors those of the nineteenth and early twentieth centuries. When describing his theory of multiple currencies Lietaer states that he will, "propose a unit of account... which aims at firmly anchoring that currency to the material/physical world... In this role, the Terra would be akin to the gold standard in the nineteenth century" (Lietaer, 1999: 144).<sup>33</sup>

This argument for a natural source of value is in direct contrast to the earlier arguments made by the Greenbacks. Historically the argument for gold or 'real' value has been made by those claiming the natural scarcity of money, not by those who are attempting to argue for the possibility of abundant supplies of money and credit. The Greenbacks unique addition to the historical arguments had been their recognition of the social construction of money's value (Babb and Carruthers, 1996). They did this by putting government front and center making

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<sup>33</sup> The Terra is what Lietaer calls a Global Reference Currency, which forms the basis of his entire currency system (Lietaer, 1999: 140-150). "The Terra is defined as a standard basket of commodities and services particularly important for international trade" (Lietaer, 1999: 144).

government critical to the recognition of the social foundations of money's value. The Greenbacks had claimed that, "Money is a creature of law, it is created and upheld by law" (Wolcott qtd. in Babb and Carruthers, 1996: 1572). And, for the Greenbacks, this law is created by the people via their representation in the government, "We, the people, make the government. We give the government power to make, provide and issue money under proper rules and regulations...We make our money, we issue it, we control it. We regulate it" (Wolcott qtd. in Babb and Carruthers, 1996: 1572). The critical part of the Greenbacks argument is that they were attempting to socialize and politicize the source of value in direct opposition to the intrinsic and natural value that bullionists argued for. For Greenbacks the role of gold was what was reinforcing scarcity, and the best way was to end the role of gold (and by logical extension the scarcity of currencies) was to recognize the central role of government. Their solution was to tie the issue of currency scarcity and value to the political economic decisions of the federal government.

The reliance of the CC movement on bullionist type arguments results in them placing the source of their currency's value outside of government. However, this causes a fair degree of logical inconsistency to enter into many of the CC advocates arguments. On the one hand, the CC advocates are trying to theorize value as being natural by tying it to a commodity, while on the other hand they see the value of a currency being realized (and essentially embedded) in a set of social relations. In his book, "The Ecology of Money," Richard Douthwaite explains his theory of CCs, saying that a key step is to establish a currency, "that represents absolute amounts of something important to the whole world's population, present and future, rather than current transitory price levels determined by a temporary minority" (1999: Chapter One).

Here Douthwaite has naturalized money's value, removing its source from government or society. Yet, in the same chapter he asks, "What gives the money its value?" and answering his own question he states that, "This hasn't been mentioned yet, but the answer is purely its acceptability to other people. The value is not guaranteed" (1999: Chapter One). On the Ithaca Hours website they claim that, "Whoever first accepts an HOUR for goods or services is the person who gives it proven value" (Ithaca Hours).

In these examples, we can see how, in an attempt to combine three elements that appear in many ways as mutually exclusive, the CC advocates land up with a muddled concept of value that is neither natural nor social. If it is to be based off a scarce commodity it is hard to imagine how that would not land up looking something like a gold-standard system, one based on the issuance of credit. Except in this case the credit (understood as ‘community currencies’) can be created by any number of local communities or individuals. All of which seems to mirror nineteenth century banking system, one that showed itself to fail repeatedly within the context of the American capitalist democracy.

Why this focus on trying to create a “natural” or “real” value base represented by a commodity? The concern that the CC advocates seem to be trying to address is the fear that a rapidly increasing supply of money would lead to inflation. Greco believes that, “Paper money that is *properly issued* on the basis of sound collateral can be perfectly sound and legitimate medium of exchange” (Greco, 2009: 94). And Lietaer claims that, “this currency, by definition, could not become inflationary (given that its value was tied to the value of coal)” (Lietaer, 1999: 43).<sup>34</sup> Lietaer is associating the existence of inflation, at least implicitly, with money that lacks a real commodity base. There is an implicit claim that inflation was not a problem when money was tied to a commodity such as gold or in his example, coal.

Historically, advocates of increasing the supply of money have seen inflation as a positive force, though for different reasons. Paper money advocates in the eighteenth century saw the inflationary impact as part of their attempt to level society and create a more democratic and equal society. While Greenback Party members argued that this had been a positive force for the commercial economy by stimulating business and creating employment opportunities. The CC advocates are linking inflation not only to the lack of a scarce commodity but also to the actions of the government. Part of the underlying assumption is that by giving the currency a commodity base you will rid the financial system of dishonesty and the negative consequences of the politicization of currency creation, “We just need an honest measure, and the freedom to

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<sup>34</sup> The currency that Lietaer is referencing here is the issuance of ‘scrip’ issued by local governments during the Great Depression (1999).

judge for ourselves the value of not just goods and services, but also anything we might use as a medium of exchange” (Greco, 2009: 122).

However, many of these conclusions challenge the historical record and seem to be mythologizing an era that, upon a close reading of the historical documents, was one marked by multiple and repeating financial crises – bank collapses, inflation/deflation, and insufficient quantities of currency. Despite this history, many CC advocates want to create abundant supplies of money, while at the same time they want to tie the currency’s value to a scarce resource. Historically any attempt to peg a currency to a scarce resource has caused massive political economic problems.<sup>35</sup> What is new is that those that are arguing for an increased supply of money are also arguing for the return of a real commodity base to the currency creation process. This alignment is unique, but also in many ways fails to engage the history of our financial system and the evidence that this commodity base causes major problems and can result in real economic crises.<sup>36</sup>

All of these attempts at reconfiguring and redesigning, or conceptualizing the currency creation process are aimed at one goal for the CC advocates and that is the creation of what they argue will be a more democratic economy and system of currency creation. Jean-Francois Noubel, an advocate of CCs, claims that, “By deactivating the artificial scarcity embedded in conventional money, by giving the power to citizens to manage the real economy, free currencies take away the hidden competition and fear that poisons most human relationships” (Noubel). The historical trajectory of currency creation since the eighteenth century has been to give greater and greater currency creation powers to the government. The government in turn has developed a symbiotic relationship with the banking and the wealthy property owning classes of society. The way in which our financial system currently operates is designed to guarantee that the commercial

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<sup>35</sup> Much of this has been written about in great detail, including the social and political economic consequences. See Polanyi: 2001; Eichengreen: 1996.

<sup>36</sup> This is not to say that all CC advocates call for the return of a commodity base. Several advocates, including Arthur Brock and Michael Linton, don’t advocate this at all. In fact, in many ways they don’t engage the question of value directly, except to say that there are already multiple currencies in circulation that have value – they highlight college degrees or airlines miles as examples of currencies representing value and enabling exchanges. Their approach is founded on the idea that currencies are about the flow or circuits of information. Michael Linton frames currencies as, “just information, a way we measure what we trade, nothing of value in itself. And we can make it ourselves, to work as a complement to conventional money. Just a matter of design” (Linton).

economy operates smoothly to the benefit of specific class interests. The CC advocates are attempting to shift this historical trajectory by theorizing the creation of currencies in a way that reinforces new types of social relations leading to new types of economic exchanges emerging and being reinforced. It is hard to imagine how this would not create problems for the currently dominant capitalist democracy. In that case, it is perhaps unlikely that the federal government will sit idly by while these new currencies proliferate, especially if they appear to be successful at enabling new, but potentially destabilizing, class relations.

The type of political economy that CC advocates promote is one in which the localized currencies enable the valuation (measurement) of currently unvalued exchanges and the retention of local economic wealth. On the website of a California-based CC they state that, “Because the currency must be used locally, and because it has local community backing, it promotes the exchange of goods and services and increases local purchasing power while avoiding the danger of government currency depreciation” (Humboldt Exchange). The CC advocates define their local communities along either geographic boundaries (a town, a neighborhood, a city) or by affiliation or membership in a currency association.<sup>37</sup> Both of these constraints are designed to perform the same purpose – to retain the wealth realized through the exchanges within the local community and its shared economy. The same CC’s website states that the, “Community Currency is a means of exchange that has a localized value. This value is limited to a specific community, usually restricted within a geographical region. This structure keeps the wealth created by the exchange of goods and services within the local community” (Humboldt Exchange).

The underlying belief is that the politicization of currency creation has led to money losing its value, resulting in a loss of wealth for local communities. This politicization has also resulted in the centralization that is behind the scarcity of currencies and the erratic character of supplies. Michael Linton writes that, “where conventional money flows erratically in and out of our communities, creating dependencies that are harmful to the economy, society and nature, the new

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<sup>37</sup> Essentially this is a group of people, fellow self selected members, willing to accept the CC in payment of debts.

complementary money re-circulates, enabling business and trade” (Linton). This argument mirrors many of the historical arguments and reasoning used by the federal government for the creation of the Federal Reserve System. It also mirrors many of the complaints heard throughout the nineteenth century by everyone from Greenback Party members to the efforts at creating a national bank in the late eighteenth century. But all of these efforts had historically turned to the government or banks to solve this problem. CC advocates are not looking to government representatives; they are looking to their local communities. The people they live next door to, and engage with on a daily basis!

The CC advocates make a direct link between this localization of currency creation and ideas of democracy. In this way they are picking up on some of the original threads of democratic theory and linking it to their theories of currency creation. Mirroring the efforts of many of the colonial state legislatures of the eighteenth century, CC advocates recognize that the way in which currencies are created has direct implications for the type of political economy allowed to operate and that it has direct implications for the type of class relations and level of class inequality. Many of the colonial state legislatures created paper money with the intention of reducing class inequality.

Today’s CC advocates take the side of the colonialists in making similar claims to want to reduce class inequality:

“Open money is flat money. It confers no power of one **over** another, only one **with** another. Exploitation is no problem; when you have your own money, you can't be bought and sold so easily. You can choose what you do to earn your money. And there's no monopoly, all systems coexist in the same space. Flatter than flat - open money is superflat.” (Linton, “Open Money Manifesto”)

This flattening of power and ending of class inequality is, according to Michael Linton achieved through the individualized, localized and decentralized creation of currencies. Other CC advocates see the same result; “People will be able to consensually participate in currencies



rather than being held hostage by an authoritative them. P2P architecture will at long last bring democracy to the domain of money” (Brock, “P2P Currency”). Paul Glover claims that, “Ithaca Hours is a local currency system that promotes local economic strength and community self-reliance in ways which will support economic and social justice, ecology, community participation and human aspirations in and around Ithaca, New York” (Glover).

The implicit claim is that the current financial system enables the destruction of social justice, the environment and local economic wealth while reproducing class inequality and exploitation. In this way the CC movement is claiming that currencies are not neutral, but can actively produce and reproduce different types of economic exchanges. While the colonialists still relied on the government to play the critical role of currency creation the local nature of these legislatures and the ability to participate directly meant that the idea of localization was, in many ways, as critical to their currency creation ideas as those of the CC advocates. In the eyes of CC advocates, the Federal Reserve certainly does not represent the “democratization of credit” as President Wilson claimed in 1913 (qtd. in Wickware, 1915: 51).

The title of a paper published by the founder of Ithaca Hours says it all, accurately summing up many of the beliefs of the CC movement, “Creating Economic Democracy with Local Currency: We Print Our Own Money in Ithaca!” (Glover). The idea that individuals have a right to create money has never been made before and the idea that this can happen without any government involvement while claiming it is a democratic solution is unique to the current debates over currency creation.

Just like those arguing for paper currency in the 1860’s, CC advocates are arguing that a greater volume of currency would enable an increase in exchange. However, what the CC claim is that these local currencies will actually result in new alternative economic exchanges – exchanges that had previously being ignored by the national currency. This differs from the efforts of the Greenbacks whose central goal was to enable the continued expansion of the capitalist economy. No previous effort had focused on exploring questions of sustainability, ecology, social justice or

community building. Those previous efforts had been most interested in the creation of more work and the way to do that was to expand the commercial economy. On the other hand the advocates of a CC called Berkshares claim that they are a “tool for community empowerment, enabling merchants and consumers to plant the seeds for an alternative economic future for their communities” (“What Are Berkshares?”). This localization is what creates empowerment, reducing the impact of inequality, and through this process, new alternative economies are able to emerge.

Bernard Lietaer makes a slightly more nuanced argument when he states that, “such currencies are called complementary because their intent is not to replace the conventional national currency but to perform social functions that the official currency was not designed to fulfill” (1999: 55). His argument is, in part, less about challenging the existing paradigm, and more about expanding it to include new arenas. In this way it may be more accurate to say that some CC advocates are trying to expand the spectrum of value encompassed within economic exchanges in an attempt to make previously invisible exchanges newly visible, valuable, measured and protected.

Carol Brouillet, who runs a website called Community Currency, claims that:

“Money can be created by banks or governments to serve their interests, or it can be created by people in a community to serve their needs. Local currencies help communities to recognize their inner strengths, the gifts of their members, and the value of cooperation. Local currencies inspire people to live in accordance with their values, to follow their inner passion rather than chase after an obsolete notion of "success." They enable people to make a contribution to their community and receive what they need or desire in return. They nurture relationships and demonstrate how local production for local needs benefits the community, as well as reducing the stress upon distant communities who have been forced into near slavery and starvation to provide resources and services to the world's wealthy.” (“Community Currency”)

Brouillet goes on to claim that these CCs encourage, “participatory democratic processes and shows how non hierarchical systems empower people, and nurture hope, creativity, respect, and compassion” (“Community Currency”). The conclusion that results is one that offers an image of a political economy in which inequality has disappeared and in which government is no longer central to the operation of the economy and currency creation. Greco claims that the enormous benefits of money can only be realized if it “is created democratically on a proper value basis by the people themselves” (Greco, 2009: 100).

Summing it up - the people are the ones that create the value, they create the currency, their economies are protected and new alternative democratic economies will emerge through this newly democratized process of currency creation. Margrit Kennedy, who has written and lectured extensively on CCs has argued that, “Money can be made to serve rather than to rule, to be use—rather than profit-oriented—and to create abundance, stability, and sustainability.” She said that while “money is one of the most ingenious inventions of mankind” it has “the potential to be the most destructive or most creative” (qtd. in Stonington, 2004). Money, credit and currencies in general, are the product of a long series of social decisions. These decisions have, historically focused on designing a system of currency creation that is both compatible and that reinforces the underlying class inequality necessary for the smooth operation of the American capitalist democracy. The rise, since the 1980’s, of a new set of financial debates, represents a unique challenge to a long running theory of currency creation. The CC advocates are pointing to the sense that the current financial system is failing; their solutions are not focused on saving the current system but on fundamentally reconfiguring the entire political economy. No theory of currency creation has attempted to articulate an alternative political economy since the failed efforts of the colonial state legislatures of the 1770’s. Democratic money, in the twenty-first century, is a type of money and credit that envisions a new political economy built on class equality.

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