What is Money?

Money and where it comes from are not as mysterious as most people think. To understand how money is created, however, we first have to ask, "What is money?"

Most simply put, money is anything that can used to measure, and to represent, the value of something being offered to satisfy a debt, or being exchanged in the marketplace. Money can take many forms (including financial contracts), depending on how people exchange things they own or reasonably expect to acquire. Money is therefore a means for securing the fundamental human right to acquire private property (the right to the fruits of and control over what a person owns).

Money is a "social tool," an artifact of civilization invented to facilitate economic transactions. Like any tool, money can be used justly or unjustly. It can be used by those who control it to suppress the independence and human potential of the many, or to achieve economic liberation and universal prosperity by financing capital ownership for every citizen.

Most economists will explain that money is: (1) a medium of exchange, (2) a store of value, (3) a standard of value, and (4) a common measure of value. "Currency" or "current money" involves a "commonly recognized determination of value, often regulated, but need not be created, by government."

Delving deeper, lawyer-economist Louis Kelso illuminated the nature of money. He understood the impact of contracts, private property, and credit arrangements on the economic system — recognizing that money is, ultimately, a social tool for measuring values used for the exchange of property rights:

> Money is not a part of the visible sector of the economy; people do not consume money. Money is not a physical factor of production, but rather a yardstick for measuring economic input, economic outtake and the relative values of the real goods and services of the economic world. Money provides a method of measuring obligations, rights, powers and privileges. It provides a means whereby certain individuals can accumulate claims against others, or against the economy as a whole, or against many economies. It is a system of symbols that many economists substitute for the visible sector and its productive enterprises, goods and services, thereby losing sight of the fact that a monetary system is a part only of the invisible sector of the economy, and that its adequacy can only be measured by its effect upon the visible sector. (Louis O. Kelso and Patricia Hetter, *Two-Factor Theory: The Economics of Reality*. New York: Random House, 1967, 54.)

Creating money using commercial banks and a central banking system (such as the U.S. Federal Reserve System) is not supposed to be a secret guarded by high priests. The system was designed to benefit everyone by allowing money to be created or cancelled as needed by the economy. That way there would never be too little money (resulting in deflation) or too much (causing inflation).

The House Banking and Currency Committee, in its widely circulated publication, *A Primer on Money* (August 5, 1964), noted:

> When the Federal Reserve Act was passed, Congress intended [the purchase of "eligible paper" by issuing promissory notes] to be the main way that the Federal Reserve System would create bank reserves. . . . When this practice was followed, the banks in a particular area could obtain loanable funds in direct proportion to the community's needs for money. But in recent years [i.e., from 1933 to 1964], the Federal Reserve has purchased almost no eligible paper (p. 42).
>
> When the Federal Reserve System was set up in 1914 . . . the money supply was expected to grow with the needs of the economy. . . . It was hoped that by monetizing "eligible" short-term commercial paper, by providing liquidity to sound banks in periods of stress, and by restraining excessive credit expansion, the banking system could be guided automatically toward the provision of an adequate and stable money supply to meet the needs of industry and commerce. . . . To safeguard their liquidity and provide a base for expansion, the member banks . . . could obtain credit from the nearest Federal Reserve bank, usually by rediscounting their "eligible paper" at the bank — *i.e.* . . . selling to the Reserve Bank certain loan paper representing loans which the member bank had made to its own customers (the requirements for eligibility being defined by law). If necessary, the member banks might also obtain reserves by getting "advances" from the Federal Reserve bank (p. 69).

In other words, under a central banking system as originally designed, businesses or other productive enterprises would obtain loans at their local commercial bank, a process called "discounting." The commercial bank, in a process known as "rediscounting," would then sell the qualified loan paper of the business enterprises to the central bank. This would create an "elastic," asset-backed reserve currency to stabilize the economy and facilitate commerce.

As a social tool, however, the money creation powers of the central bank are like the vote. They can be used to keep an *élite* in power, or they can spread power around by financing capital formation and acquisition

by every person by creating money to purchase assets that pay for themselves out of their own future profits. Once the assets are paid for, the stream of profits provides the owners an ongoing source of income to help meet consumption needs such as food, clothing, shelter, healthcare, and education.

The Center for Economic and Social Justice (CESJ) has proposed a new system of political economy that CESJ calls "the Just Third Way," an advance over both capitalism and socialism. This system offers a program ("the Economic Democracy Act") for financing the future of the U.S. economy so that it can empower economically every person, not just a few or the State. Financed with a more just system of money and credit, the world, as R. Buckminster Fuller suggested, *can* work for "100% of humanity in the shortest possible time with spontaneous cooperation without ecological offense or the disadvantage of anyone."

Under this program every citizen — each child, woman and man — would have an equal right and access to the financial system to purchase on credit each year newly issued full dividend, full voting equity shares. Projecting the growth needs of the economy, the financial system would extend to every citizen, rich or poor, an equal allotment of no-interest credit (loans) repayable with the full stream of future profits generated by the new shares.

It is important to note, however, that no new money would be created until the shares a citizen wants to buy have been approved by the lender and deemed a good risk by a capital credit insurer.

How would it work? A local commercial bank would accept a contract for a loan — "paper" — from a citizen. The bank would "buy" the contract from the citizen by issuing a promissory note. The bank would then immediately sell its paper to one of the twelve regional Federal Reserve banks.

Although no actual teller's window exists where commercial banks stand in line to sell loan paper to the Federal Reserve, the transaction is described as taking place at "the discount window." (While it is called the "discount window," the process is actually *re*discounting.) When the discount window is "open," commercial banks can sell their "qualified industrial, commercial and agricultural paper" to the central bank. When the "discount window" is "closed," commercial banks must go elsewhere to obtain excess reserves to lend, or cease making loans.

The Federal Reserve would issue its own promissory notes to the local bank to back newly printed currency or new demand deposits that would be handed over to the citizen to purchase the shares he or she wants to buy. When the shares pay dividends, the citizen would use the dividends first to repay the loan used to acquire the shares. After the loan is repaid the citizen would continue to receive dividend income to use for his or her consumption needs.

As the loan is repaid, the Federal Reserve would cancel the money it created for that loan. As all such loans were repaid, the currency would be taken out of circulation, or the demand deposits "erased" from the books. This would remove money from the economy that was not linked directly to productive assets. In this way the Federal Reserve System would create an"elastic" asset-backed currency that increased or decreased as the need for money increased or decreased, avoiding deflation or inflation.

At the same time, without harming the property rights of existing owners, it would rapidly increase the number of capital owners in the country, while decreasing the wealth and income gap. It would also reduce the role of the State in taking care of people as they become able to take care of themselves.

Thus, the establishment of the Federal Reserve really did have the potential to become an "Economic Fourth of July" . . . assuming the economy grows faster in ways that every citizen can earn more wages and profits to purchase what the economy can produce. Without that, the social good of money and credit will keep being used to make the rich richer and keep the non-rich property-less and powerless.

(Find out how to change the money system: https://www.cesj.org/learn/economic-democracy-act/overview/) 101924