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Democracy in Crisis

The Dynamics of Civil Protest
and Civil Resistance

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DEMOCRATIC ACCOUNTABILITY OF BUSINESS AND MONETARY REFORM

MARK JOÓB

Introduction

Today's financial crisis reveals not only malfunctions of the financial system itself but also the failure of the present political framework for the whole economy. There is a considerable discrepancy between moral responsibility and accountability of business, since the liability of people acting by means of a company is limited. This leads to moral hazard and consequently to the privatization of profits and the socialization of costs arising from economic action. Democratic control over finance – and in particular over the monetary system – has largely been lost and has been usurped by commercial banks and unregulated hedge funds. Hence, the 'one man, one vote' fundamental principle of political justice that guarantees equal political participation for every citizen is losing its social relevance. It is being replaced by plutocracy meaning that the political power of an actor is proportional to their economic assets. The fact that governments recognize private financial actors as too big to fail clearly shows that society is to a great extent being ruled by these financial actors and not by the elected representatives of the people. Thus, the current financial crisis indicates a serious crisis of democracy.

Political justice demands a better harmonization of legal accountability with moral responsibility, which requires fundamental reforms, including a significant extension of liability in company laws. Especially important is a thorough reform of the monetary system, since it dominates finance and the whole economy. We need a new monetary architecture that restores democratic control over the money supply and makes the monetary system better serve the common good. A system of *sovereign money* could be a stable ground for the new monetary architecture.

The lack of democratic accountability

A momentous characteristic of today's society is the lack of accountability of major private economic actors, even though these actors profoundly shape society and people's lives. This observation holds true virtually throughout the world.

In the last four decades, the economic, political and social power of big business continuously increased due to globalization and the political implementation of the neoliberal ideology, which prescribes the deregulation of markets, the removal of trade barriers, and privatization of state-owned enterprises. Guided by the neoliberal dogma that unrestricted competition of private actors in self-regulating markets will benefit all members of society in the long run – as claimed by Friedrich Hayek for example (cf. Hayek 1982) – governments actually limited their scope of policy-making and handed over political power to dominant private economic actors. This way, democratic control over political power has been severely narrowed down, since those economic actors to whom political power has been transferred are not accountable to the public.

Supporters of neoliberalism usually deny the fact of this transfer of *political* power and even the possibility to assign *economic* power to single economic actors. So does also Hayek by considering the market to be a “spontaneous order” (Hayek 1966: 611), the outcomes of which nobody is responsible for. On this basis, it would obviously be wrong to hold any actor on the market accountable for negative market effects on society. The neoliberal concept of the free market working efficiently without any regulative interference from outside is based on a wrong assumption already made by classical liberalism. Accordingly, the market can exist as a natural, spontaneous order, as an impersonal, functional system guided solely by the rational price setting mechanism, thus as a system unaffected by social relations such as power and responsibility. Since market transactions are always conducted by humans within their specific social context, the current neoliberal attempt to put a socially completely disembedded market into practice is as much a utopia and deemed to fail as the communist central planning of the entire economy (cf. Gray 2004: 23 et seq.). Despite its emphasis on economic freedom, the neoliberal Utopia, similarly to communist Utopia, could only be reached by totalitarian means even though the neoliberal way of enforcement is quite subtle and opaque. At the end of the day, both utopias are an outrage upon human liberty.

To be sure, economic liberalization is not a phenomenon of the recent decades. “The Neoliberal Project” (Jackson 2012: 76) that was adopted in the early 1980s by Ronald Reagan in the United States (US) and Margaret

Thatcher in the United Kingdom (UK) and has been globally pursued since then is the revival of the first wave of liberalization that already started in the beginning of the 19th century in England and led to the gradual emergence of the market economy in the Western world, as impressively described by Karl Polanyi. On the transition from regulated markets to the self-regulating ones of the *laissez-faire* era of market economy, Polanyi comments:

“A self-regulating market demands nothing less than the institutional separation of society into an economic and a political sphere. [...] Such an institutional pattern could not have functioned unless society was somehow subordinated to its requirements. A market economy can exist only in a market society.” (Polanyi 2001: 74).

In other words, self-regulating markets require the detachment of the economic sphere from the political realm and thus from the institutions and processes of democratic accountability. Despite this theoretical and institutional separation of economy and politics, market economy is not neutral towards society, but necessarily implies society’s submission to the market system. Once enforced by policy, market economy imposes a powerful structural constraint on individuals and on governmental policy-making to adapt to the rules of the “market struggle” (Weber 2010: 563). In order not to become a loser in the “market struggle”, that is to lose their jobs and their livelihoods, individuals must behave in conformity with the market’s requirements to a great degree, as must governments in order to attract business.

In the last decades the neoliberal ideology dominated not only the political realm, but also the science of economics. While the neoliberal dogma of deregulation and privatization in politics was propagated and perceived as a factual constraint leaving no room for alternatives, critical perspectives on “market determinism” (Ulrich 2008:153) were banned from mainstream economics, which therefore has been called “TINA economics” (Hutchinson et al. 2002: 208). The acronym “TINA” stands for “There Is No Alternative”. If there were really no alternatives and economic policy was fully determined, it would of course be absurd to hold anybody accountable for it, since without alternatives to choose from, there is no freedom to act according to one’s choice, and this is a prerequisite of moral responsibility and legal accountability (cf. Joób 2012).

The main beneficiaries of the neoliberal monopoly of economic policy are clearly the large multinational corporations. The first wave of liberalization at the end of the 19th century established limited liability for share-

holders and awarded artificial personhood to corporations granting them rights similar to those of citizens, for example the right to property and liberty of contract. These two legal innovations are the basis of the present power of corporations. In his excellent analysis of corporate power, Florian Wettstein says that due to the second wave of liberalization in the last decades, the multinational corporation has become a “quasi-governmental institution” (Wettstein 2009: 169). Wettstein concludes:

“Today multinational corporations have entered the transformation from citizens into governments. They are increasingly acting not as mere persons but as rule makers; as such, they determine our private and social lives, as well as our public affairs, to an unprecedented and ever-increasing extent.” (Wettstein 2009: 187)

The problem with multinational corporations is not that they exert some influence on individuals and societies; the problem is that they have taken over control. Multinational corporations exercise their quasi-governmental power in several ways (cf. Wettstein 2009: 213 et seq.). They govern people by weakening the countervailing power of civil society; they govern markets by taking advantage of monopolistic or oligopolistic competition; they govern governments by lobbying and economic pressure and they govern themselves by filling the global regulatory vacuum with their own rules.

The depoliticization of economy as demanded by the (neo-)liberal ideology necessarily leads to the economization of politics, since the loss of publicly exercised political power that arises from deregulation is immediately compensated for by an increase of privately exercised political power. Hence, deregulation is nothing else but a transfer of power from the public to private economic actors such as multinational corporations, which is even more apparent in the case of privatization of publicly owned assets. This transfer is critical, because corporations are not organized according to the principle of democracy and thus do not meet the requirements of public scrutiny, accountability and equal weight of votes in decision-making, not to speak about the even more demanding prerequisites for deliberative discourse (cf. Ulrich 2008: 330 et seq.). Corporate decisions are not democratically legitimate since not all individuals affected by these decisions have an equal say in them. The large majority of affected individuals actually have no direct influence at all on corporate decisions. Even within the group of a company’s shareholders who have the power to appoint and dismiss the management, the weight of their votes is not equal but is in proportion to the amount of their investment. In other words, in-

vestors with the most capital rule those corporations, which to a great extent rule the lives of people, especially by controlling their access to livelihood. However, a society where disposal over capital is the decisive requirement for gaining power is not a democracy anymore but a *plutocracy*.

At this point, it is worth considering how the first wave of liberalization came to a close and why it took several decades until the present wave of liberalization started. The most important finding of Polanyi's profound analysis of societal transformation induced by the establishment of the *laissez-faire* market economy in the 19th century is that the “conflict between the market and the elementary requirements of an organized social life [...] produced the typical strains and stresses which ultimately destroyed that society.” (Polanyi 2001: 257) The measures adopted by society to counteract the negative social effects of the free market, such as unemployment and insecurity, unleashed dynamics, which fostered imperialism and finally led to the First World War (cf. Block 2001: xxxii). Then this tragic scenario was repeated when the Great Depression of the 1930s caused by market failure prepared the social conditions leading to the Second World War.

This short historical flashback clearly shows that the lack of democratic accountability of business, which results from deregulation, is not only a matter of legitimacy but also constitutes a serious threat to stability and peace within and between societies. Freed from governmental interference, today's global market works “to set sovereign states against one another in geopolitical struggles for dwindling natural resources” and impairs governments' ability “to protect citizens from insecurity” (Grey 2004: 27). Hence, it is an urgent task for humanity and each citizen to restore public control over the economy. Democratic accountability of business is a necessary prerequisite for both economic and political justice, since without justice, social peace cannot endure.

The failure of the monetary system

The absence of public control of the monetary system is most serious since the monetary system is the heart of the economy guaranteeing the circulation of money that is indispensable for economic transactions to take place. According to traditional money theory, money plays a threefold role in the economy as a medium of exchange, a store of value and a unit of account (cf. Issing 2007: 1et seq.). Money, however, is more than just a neutral means for business; money actually governs business. The monetary system rules finance, which today essentially determines the economy.

In the last decades this fact has been widely neglected when discussing the negative social and ecological effects of business activity. Even current debates on the 2008 financial crisis that evolved to the biggest economic crisis since the Great Depression and is still persisting show no awareness of the significance of the monetary system for finance and the real economy. How is the present monetary system affecting the economy and thereby society and nature, and why is it failing? I will outline the interconnected malfunctions of the globally prevailing monetary system in ten points.¹

1. Money is debt. Today, money comes into existence exclusively by debt creation when commercial banks borrow from central banks and governments, or producers and consumers borrow from commercial banks. Thus, the money supply of the economy can only be maintained if the private or public economic actors get into debt. Economic growth requires a proportionate increase in the money supply in order to avoid deflation that would paralyze business, but an increase in the quantity of money involves a simultaneous increase in debt. This way, economic actors run into danger of excessive indebtedness and bankruptcy. It is not necessary to say that overindebtedness causes serious problems to societies and individuals in the face of the ongoing debt crisis, which began as a debt crisis of private homeowners in the United States and then transformed into a debt crisis of commercial banks and insurance companies before being absorbed by national treasuries and so turned into a sovereign debt crisis. Reductions in national expenditure required to pay off public debt often lead to social unrest and are inequitable, because they impose burdens on citizens who did not profit equally from debt creation.

2. The money supply is under private control. Only a small fraction of the money circulating in public has been created by central banks. Central banks issue coins and banknotes which in most countries account for just between 5 % and 15 % of the money supply. Most of the rest is created by commercial banks in an electronic form as account money when granting loans to customers. But all money, whether cash or account money, is brought into circulation by commercial banks. Therefore, commercial banks *de facto* control the money supply. On the one hand, commercial banks principally bear the credit risk for the loans they grant, which should induce them to carefully examine the creditworthiness of their customers. On the other hand, however, commercial banks decide which customers are granted a loan and which investments are made according to their interest

¹ The following outline is inspired mainly by Huber 2010, Binswanger 2009, Robertson 2012 and Lietaer et al. 2012.

in maximizing their own profits. Whether an investment is socially desirable is definitively not the decisive criterion for commercial banks. This way, investments serving the common good without being profitable enough are not supported by the banking system and have to be financed by government spending that depends on tax revenues and public debt creation. Instead of financing long-term investments in the interest of society as a whole, commercial banks with their credit business nourish short-term financial speculation and over the last two decades actually have established a gigantic global casino beyond any public control.

3. Bank deposits are not secure. Bank deposits refer to account money, which in contrast to cash is not legal tender although it is handled as if it were legal tender. Account money is a substitute for money, just a promise from the bank to disburse the corresponding amount of money in legal tender if requested by the customer. In the present fractional reserve banking system, usually only a very small proportion of account money is backed by legal tender. Banks hold only a few percent of their deposits as cash and reserves at the central bank. That is the reason why banks are reliant on the trust of their customers. In the case of a bank run, when too many customers demand cash at the same time, they would run out of cash and face sudden bankruptcy. Hence deposit insurance systems have been established to avoid the loss of bank deposits. In the case of chain reactions and large-scale bankruptcy as in 2008, however, government bailouts of commercial banks may be necessary, eventually with the assistance of the central bank as lender of last resort.

4. The money supply is pro-cyclical. Commercial banks grant loans by creating account money in order to maximize their interest revenues. The more money they issue the higher their profits – as long as the debtors are able to pay. In times of economic growth banks most willingly grant loans so as to profit from the boom, whereas in times of economic decline their granting of credit is very restrictive in order to reduce their risks. This is how commercial banks induce an oversupply of money in booms and an undersupply of money in recessions, thus amplifying business cycles as well as financial market fluctuations and creating asset bubbles in real estate and commodities. Such asset bubbles may cause heavy damages to society and to the banking system itself when they burst. Again, the 2008 mortgage-triggered banking crisis after the burst of the US real estate bubble is the most illustrative example.

5. The money supply fosters inflation. Besides its pro-cyclical character in the short term, the money creation of commercial banks in the long term

induces an oversupply of money that leads to consumer price inflation as well as asset price inflation. Principally, an oversupply of money arises if the increase in the quantity of the money in circulation exceeds the growth of the production of goods and services. The long-term oversupply of money results not only from traditional granting of credit to governments, corporations and individuals but also from credit-leveraged financial speculation of hedge funds and investment banks. Due to inflation consumers usually face an annual loss of purchasing power, which means that they have to increase their nominal income in order to maintain their level of consumption. Since the ability to gain compensation for the loss of purchasing power by increasing one's nominal income varies from individual to individual, inflation causes a redistribution of purchasing power to the disadvantage of unprivileged social groups, which are not in the situation to effectively advocate for their own interests.

6. Interest on money is a subsidy to the banking sector. Since money is debt, it carries interest. Therefore, interest has to be paid on all the money in circulation and virtually nobody can escape these payments. Primarily, of course, the customers who take up loans from commercial banks and thereby ensure the money supply are obliged to pay interest. Secondly, everybody who pays taxes and buys goods and services makes a contribution to the interest payment of the original borrower, because taxes have to be raised partly in order to finance the interest payments on sovereign debt and corporations, and individuals providing goods and services must include the costs of their loans in their prices. This way, by using money society pays an enormous subsidy to the commercial banks, a part of which they pass on to their customers as interest payments on deposits. Interest is a subsidy to the banks because the account money they create is handled as legal tender; and it is a hidden subsidy because it is not subject to public discussion. The magnitude of the subsidy society pays to the banks is reflected in bankers' disproportionately high salaries and premiums as well as in the disproportionately big banking sector, which is dominated by a few giant banks. These giant banks hold assets that exceed the size of large national economies, so they really are too big to fail since their collapse would have disastrous social effects on a global scale.

7. Interest on money forces economic growth. Interest forces monetary growth and consequently the growth of the real economy. When customers repay their loans to the commercial banks, the banks write off the returned amount of money and the quantity of money in circulation decreases correspondingly. However, the money that over time has been paid as interest on the loans does not disappear; it becomes the property of the banks. Debtors

need more money than they have borrowed in order to not only pay back their loans but also to pay interest on them. The additional amount of money needed for interest payments, however, can only be available in the economy if additional loans are granted by the banks. Otherwise the money supply would not be sufficient for the real economy to work properly and be profitable. It follows that the money supply must continuously increase to avoid economic crises. A financial system that cannot function unless it grows is nothing else but a Ponzi scheme.² Yet, an even more detrimental effect of forced monetary growth is that it exerts a heavy pressure on the real economy to grow incessantly in order to back the additional money supply by additional economic production. The forced perpetual growth of the real economy involves an increasing exploitation and destruction of nature and thus impedes the sustainable development of humanity. This way, growing financial indebtedness caused by the monetary system leads to growing ‘ecological indebtedness’. Furthermore, the quantitative growth of the real economy will sooner or later inevitably end since the Earth’s resources are limited.

8. Interest fosters wealth concentration. Interest is commonly seen as a lending charge for using the money of someone else. Not only the customers who borrow money from banks but also the banks, which hold customer deposits pay interest. When commercial banks create money by granting loans, they credit customer accounts and thereby expand the total of bank deposits. Since accounts usually carry interest, the banks spend a part of their interest revenues for interest payments to the account holders. Now, bank deposits and loans are not equally distributed among the customers. Some have mainly loans they pay interest on whereas others mainly have deposits they earn interest on. Because in general poorer people have more loans than deposits and richer people have more deposits than loans, interest payments are in toto a transfer of money from the poorer to the richer people, especially to the few super-rich. Interest thus fosters wealth concentration. This concentration of wealth to a great extent favours the commercial banks, which on the one hand make investments themselves and on the other hand earn the amount resulting from the considerable interest

² Named after the peculator Charles Ponzi, a *Ponzi scheme* is a fraudulent investment operation that pays returns to existing investors from funds contributed by new investors. With little or no legitimate earnings, the schemes require a consistent flow of money from new investors to continue. Ponzi schemes usually entice new investors by offering higher returns than other investments. Ponzi schemes tend to collapse when it becomes difficult to recruit new investors or when a large number of investors ask to cash out. (According to the description of the US Securities and Exchange Commission: <http://www.sec.gov/answers/ponzi.htm> [accessed January 4th 2013].)

spread between borrowing and lending rates. Moreover, interest is added regularly, for the most annually, to the initial investment and thus carries interest itself turning into compound interest and generating an exponential growth of monetary assets. However, monetary assets do not grow in value by themselves since they are *per se* not productive. Value-increasing interest on monetary assets can only be generated through human labour; and human labour is permanently under a monetary pressure to increase its productivity and lower its costs so as to satisfy the demands of exponentially growing compound interest. Interest is therefore a value transfer that favours capital investments to the disadvantage of labour income.

9. The monetary system is unstable. There is clear empirical evidence showing that the monetary system suffers from structural instability arising from the mechanisms described above. The financial crisis that started in 2008 and is still lasting, if not even worsening, is not a unique phenomenon. In the last decades, numerous crises related to the monetary system occurred around the world. Between 1970 and 2010 a total of 425 financial crises affecting member states of the International Monetary Fund (IMF) was officially recorded: 145 banking crises, 208 monetary crashes and 72 sovereign-debt crises (cf. Lietaer et al. 2012:51). The multitude of financial crises and their contagion effect on separate national economies plainly demonstrate their structural-systemic character. The present monetary system inevitably evokes crises in finance and consequently in the real economy, which in turn is the basis for the monetary system. Briefly, the instability of the monetary system is largely due to the fact that the monetary system is not compatible with a finite world.

10. The monetary system counteracts crucial moral values. A moral value is something that is seen as valuable from a general perspective after careful consideration. Moral values hence embody the most rational and most important values of society. Moral values and monetary values do not fully overlap; monetary values represent only a limited number of moral values. Money as a means to satisfy basic human needs, for example, is morally valuable, whereas money harming the needy by speculative investments is certainly not. Since money, respectively the monetary system, rules the economy and dominates society, moral values not contributing directly to the profitability of business are systematically suppressed in policy-making. This way, the current monetary system counteracts crucial moral values, such as solidarity, amicable relationships and a fulfilling life.

Reforming the monetary system

My analysis above clearly demonstrates the failure of the globally prevailing monetary system. The monetary system undeniably fails to ensure stability and security in finance, to enable a consistent and sustainable development of the real economy and thus to serve society as a whole. My analysis also shows that the apparent deficiencies of finance and the real economy cannot be remedied without radically reforming the monetary system. Hence, it is about time to fundamentally redesign our monetary architecture. As Joseph Stiglitz and other experts, realizing the prime importance of monetary reform, note in their recent UN-report: “The current crisis provides, in turn, an ideal opportunity to overcome the political resistance to a new global monetary system.” (Stiglitz et al. 2010: 166)

Though monetary reform has not yet been put on the political agenda, the public and academic discourse on this subject has in the last years indeed become more intense. Two concepts of monetary reform are particularly popular in the present discourse – the concept of sovereign money and the concept of complementary currencies. I will now, in a short overview, depict the main features of these two concepts and address some of their strengths and weaknesses.

The sovereign money system

With regard to recent history, the sovereign money concept traces back to the so-called Chicago Plan that was proposed by leading U.S. economists in the 1930s in order to end the Great Depression and to avoid the occurrence of similar crises (cf. Yamaguchi 2011: 4 et seq.). The monetary reform envisioned by the Chicago Plan was splendidly elaborated by the prominent macroeconomist Irving Fisher, who predicated this plan being “incomparably the best proposal” to remove “the chief cause of both booms and depressions, namely, the instability of demand deposits, tied, as they now are, to bank loans” (Fisher 1936: 9). Accordingly, the core intention of the Chicago Plan was to take the control over the money supply out of the hands of the commercial banks and to restore actual governmental control over money creation by requiring 100 % reserve backing for bank deposits.

As a result of 100 % reserve backing of all current accounts, commercial banks would no longer be in the situation to almost unlimitedly create money by granting credit, but they would be obliged to fully finance their credits by central bank reserves. These reserves, which embody legal ten-

der, are given as loans to the commercial banks if they deposit appropriate assets as collateral at the central bank. In the case of 100 % reserve backing, thus, the total of the money in circulation – cash and current account holdings – would be equal to the amount of legal tender issued by the central bank. And since the central bank works under the mandate of the government, the government would ultimately control the money supply and let the central bank enlarge the quantity of money to a degree, which allows for a steady economic development.

In a recent IMF working paper, two experts rigorously evaluate the impacts of 100 % reserve backing by applying the recommendations of the Chicago Plan to a precise model of the current U.S. financial system. Their results fully validate the benefits of this plan as claimed by Fisher (cf. Fisher 1936: 19 et seq.):

“The Chicago Plan could significantly reduce business cycle volatility caused by rapid changes in banks’ attitudes towards credit risk, it would eliminate bank runs, and it would lead to an instantaneous and large reduction in the levels of both government and private debt. [...] One additional advantage is large steady state output gains due to the removal or reduction of multiple distortions, including interest rate risk spreads [...] Another advantage is the ability to drive steady state inflation to zero [...]” (Benes and Kumhof 2012: 55 et seq.)

It is important to note that this conclusion refers to a version of the Chicago Plan which, gives the government the exclusive right of money issuance. This result can be achieved in the following way: when commercial banks are obliged to back their outstanding credits to 100 % by central bank reserves – instead of, for example, the 1 %, which is required in the euro zone at present – then they suddenly have to deposit very large assets as collateral at the central bank. If the central bank accepts only domestic government bonds as collateral for reserves, the commercial banks must fund their non-government loans with money that originates from government loans and comes into circulation by public spending or lending. Consequently, the commercial banks are bound in the first round, when creating money, to grant all their credits to the government and deposit all the government bonds that they receive as equivalent from the government at the central bank as collateral.

Then, in a second round, they must collect existing money through income and borrowing in order to be able to grant credits and to facilitate productive investments. This way, money creation by commercial banks would be limited to the amount of loans, which is requested by the gov-

ernment. Simultaneously, money would not come into circulation in the economy except through the treasury by public spending or lending according to government policy.³

This government version of the Chicago Plan would solve the problem of how to guarantee complete congruency between the credits granted by the commercial banks and their holdings of central bank issued reserves, but money would still represent debt and carry interest. Though the government could exercise a monopoly over money issuance, money creation would still depend in part on the willingness of commercial banks to give loans to the government and therefore these banks would have some bargaining power with regard to the interest rate of the government loans. Less rigorous versions of the Chicago Plan that allow the central bank to accept not only government bonds but also non-government securities as collateral for reserves, are even more problematic, since they face difficulties in controlling the money supply by monetary policy. The reason for this is that the commercial banks could take an active role in granting credits to the private sector according to their own interests leaving to the central bank just the reactive role of providing reserves for already existing current account holdings.

Joseph Huber draws the logical conclusions from the government version of the Chicago Plan, when he in the present debate on monetary reform formulates the convincing idea of replacing the unnecessarily complicated two-level banking system by a single-level system, in which money is no longer backed by reserves, but money itself is the reserve (cf. Huber 2010 and 2012). Partially together with James Robertson (cf. Huber and Robertson 2000), Huber has developed further the 100 % reserve concept of Fisher by specifying and adapting it to the conditions of electronic data processing. The work of Huber is the most important theoretical basis for the monetary reform movement that has come into life in Europe in the last years and aims at a fundamental modernization of the current dysfunctional fractional reserve banking system. This monetary reform movement includes the German *Monetative* initiative, the Swiss *Vollgeld* initiative (cf. Joób 2013) and the *Positive Money* initiative in the UK. In the following, I will refer to the monetary concept of this reform movement as “sovereign money”.

³ The government version of the 100 % reserve system that I shortly describe in this paragraph contains core elements of, but is not identical with the version of the IMF working paper. The version of the IMF experts is more complex and makes further assumptions regarding the envisaged monetary reform; cf. Benes and Kumhof 2012: 18 et seq.

In the sovereign money system, both cash and current account holdings are fully valid legal tender and do not need to be backed by reserves because they themselves embody the reserves and are completely safe from a legal point of view. Hence, money on current accounts would not disappear in the case of a bank's bankruptcy and governments would not have to bail out large banks since a core element of the sovereign money reform is

“[...] to take bank customers’ current accounts off bank balance sheets, and recognise formally what they now actually are: accounts containing non-cash money which belongs to customers, just as customers’ wallets and purses contain cash money that belongs to them. In other words, customers’ current accounts will cease to be accounts belonging to the banks. They will be containers of money belonging exclusively to bank customers.” (Huber and Robertson 2000: 23 et seq.)

This simple but very effective innovation would lead to a strict separation of money and credit and would end the money creation by commercial banks, which would merely hold customers’ current accounts in trust. In the sovereign money system, commercial banks would be nothing more than financial intermediaries and could therefore only grant credits from money, which they have previously borrowed from their customers or owners (cf. Huber 2010: 92 et seq.).

Similarly to Fisher who intended to put a governmental “currency commission” in charge of exclusively issuing reserves in the form of cash (Fisher 1936: 17 et seq.), the sovereign money concept aims to establish a sovereign public authority with total control over the money supply, both cash and current account holdings. This monetary authority would represent a fourth separate and largely independent section of the state besides the legislature, the executive and the judiciary. It would serve the common good as “the trustee of a nation’s currency, defending its exchange value and its domestic purchasing power, creating, if necessary, additional money in accordance with real economic potential, and ensuring full seigniorage from the creation of money.” (Huber 2012: 9) The money created by the monetary authority would be transferred to the treasury and would come into circulation by public spending; thus, it would benefit the public purse and contribute to the reduction of national debt. Public revenue would be especially high in the moment of transition to the sovereign money system when the money owed to commercial banks becomes owed to the monetary authority, which would significantly reduce public indebtedness. In other words, instead of bringing the commercial banks an extra profit, money creation would serve the whole community. This result is clearly proven by

Yamaguchi's macroeconomic modelling, who concludes that in the sovereign money system "looming debt crises to be caused by the accumulation of government debt can be thoroughly subdued without causing recessions, unemployment, inflation, and contagious recessions in a foreign economy." (Yamaguchi 2011: 26)

Compared with the 100 % reserve system, a great advantage of the sovereign money system is that money would be issued debt-free by the monetary authority and would therefore not carry interest – unless, in a following step after being created, it is lent by its owner as an investment, for example to a commercial bank. Debt-free money issuance would considerably alleviate the current social and ecological problems arising from interest, such as forced economic growth and redistribution in favour of capital.

The proponents of the Chicago Plan were aware that their goal of establishing public control over money creation could be thwarted by the emergence of new financial instruments, specially bank-created securities, taking over the function of money (cf. Benes and Kumhof 2012: 18). This is a serious danger also to a sovereign money system, in particular with regard to the interbank market. Financial regulations would be needed to prevent the emergence of near monies which would impair the monetary authority's control over the money supply, for instance by prescribing a minimal holding period for financial instruments.

Another problem that needs to be resolved in a sovereign money system is how to secure the independence of the monetary authority. Since governments generally seek to increase public revenue in order to enlarge their scope of action, they would be tempted to put pressure on the monetary authority to issue more money than the potential of the real economy and the principle of sustainable development in a given situation allow. In the same way as the independence of the judiciary is guaranteed today, the monetary authority's independence from short-sighted political interests could be secured by an adequate institutional arrangement, which simultaneously warranted complete transparency in monetary decision-making and full democratic accountability of those who rule the monetary system. A central aim of the sovereign money concept, after all, is to restore democratic control over the monetary system as the heart of the economy and to make it serve the common good by promoting welfare, justice and social peace.

Complementary currencies

The complementary currencies concept, similarly to that of sovereign money, is rooted in certain efforts of the 1930s to counteract the Great Depression. In this case, the efforts aimed at putting into practice the theoretical work of Silvio Gesell and included the successful monetary experiment that was conducted in the Austrian town of Wörgl in 1932 and 1933 (cf. Schwarz 2008), as well as the Swiss WIR cooperative that was founded in 1934, then soon became a bank and today still maintains a large national complementary currency system for small and medium enterprises (cf. Kennedy and Lietaer 2004: 113 et seq.).

The concept of complementary currencies intends to establish a monetary system with several currencies working in parallel in different economic contexts and so complementing one another. The aim is not to abandon the present malfunctioning monetary system and to replace it by a completely new one, but to introduce new currencies in addition to the prevailing national or supranational currencies, which today represent the single legal tender in a given country. The current monetary and banking structures would, thus, remain unchanged. The negative effects of these structures, however, would be countered by the benefits of well-functioning complementary currencies, which, for the most on a regional level, serve a specific socially desirable goal. Accordingly, the recent report of the Club of Rome on the link between money and sustainability concludes:

“To systemically improve the resilience of our economies and the health of our societies, we must shift our monetary paradigm from a monoculture of debt-based, interest-driven money to a *monetary ecosystem* [...] Our monetary monoculture needs to make room for sufficient diversity in both the types of exchange media and in the types of agents creating and managing them.” (Lietaer et al. 2012: 181)

Actually, remarkable progress on the way to the envisaged monetary diversity has been made up to now, as there are a considerable number of complementary currencies working around the world, many of which have proven to be prosperous. Owing to civil society initiatives, a great variety of complementary currencies has emerged since the 1980s, especially in peripheral regions and in previously neglected realms of economy. The cause for introducing a complementary currency is typically some kind of economic exclusion of the people concerned, such as unemployment, no access to functioning markets or missing funds for important services.

Thus, complementary currencies are a way of self-help when the usual economic structures are absent or fail.

Regions that are not attractive enough for national and multinational business often face problems in generating sufficient tax income needed for the provision of important social services, such as education and health care. This can lead to a decreasing standard of living and even to depopulation in such regions. According to the proponents of complementary currencies, the problem in such regions is not a lack of money in general but, more precisely, a lack of monies since “the local financing equation cannot be solved *in official national currency alone.*” (Arnsperger 2011: 8) From this view, the solution is to establish a complementary currency, the use of which is limited to the region in order to bind productive capital to the region by preventing its outflow.

The most widespread among the very different types of existing complementary currency systems is the Local Exchange Trading System, in short ‘LETS’. A LETS brings together supply and demand and makes possible the exchange of goods and services without using conventional money. The heart of a LETS is a central bookkeeping where the member accounts are managed in the following way: when an exchange transaction takes place, the seller gets a credit over the respective amount and the buyer gets a debit over the same amount; so the total of credits is always exactly counterbalanced by the equal amount of debits. The currency in circulation within a LETS is embodied by the credits listed in the central bookkeeping or, alternatively, by paper money representing these credits. A LETS is limited in its scope by the fact that it requires the members to substantially trust each other because their earnings generated through this system consist of credits to be paid off in the future with goods and services which they will purchase from other participants. Also conventional money is, of course, based on trust, but its acceptance – though not its purchasing power – is guaranteed by law since it is a legal tender. Complementary currencies, in contrast, are grounded rather on voluntary commitment and therefore must be able to provide extra benefits for their participants in order to be accepted, benefits like economic inclusion and additional income. Successful complementary currencies designed as LETS are for instance *Time Dollars* in the United States, *Hureai Kippu* in Japan and *Tlaloc* in Mexico (cf. Lietaer 2001: 312ff.).

However, complementary currencies are not always successful. Several have not gained enough support from the community addressed so their existence lacks significance or they have already been abandoned (cf. Hirota 2011 and Thiel 2011).

The complementary currencies concept promotes community currencies that are created and maintained in order to achieve benefits for society as a whole and in particular for marginalized groups. The ideal is a multilevel monetary architecture as a part of a new economic governance that allows “two types of economy to coexist peacefully”: the competitive economy, which is based on conventional money and “a cooperative economy”, which makes possible for communities “to develop the full potential of their projects without needing to depend on the supply of bank-debt currency” (Lietaer et al. 2012: 191). Hence, complementary currencies aim to foster the economic independence and self-determination of – for the most local and regional – communities.

At this point, an important clarification must be made. In contrast to the intention of the complementary currencies concept as it is pictured in the current debate on monetary reform, complementary currencies do not necessarily represent an alternative, ‘cooperative’ economy. Not all complementary currencies promote socially desirable non-profit projects. On the contrary, the large majority of complementary currencies in use today serve purely commercial goals since they are designed as loyalty systems and motivate customers to repeatedly buy goods and services from the same company or alliance of companies (cf. Kennedy and Lietaer 2004: 240 et seq.). The points or frequent-flyer miles which are allotted as rewards for purchases and typically stored on cards, represent money because they entitle customers to discounts and substitute a certain amount of money when cashed (cf. Arnsperger 2011: 5 et seq.).

Conclusion

The severe problems caused by our present monetary system prevail in spite of the multitude of existing commercial complementary currencies. This shows that the diversity of currencies alone is not a sufficient solution for these problems. The solution cannot be found in the quantity but only in the quality of currencies. What we need are well-constructed and properly functioning currencies, which serve the common good. That is the reason for the failure of the *free banking* concept, the core elements of which correspond to the complementary currencies concept. Free banking stands for the complete deregulation and privatization of money creation and for the competition of different currencies on a free market. Free banking was proposed by the neoliberal dogmatist Friedrich Hayek (cf. Hayek 1976) and is still promoted today by some economists (cf. Hülsmann 2007; Polleit and Prollius 2010). The key point about free banking is that many of

our present monetary problems come from our monetary system's close similarity to a free banking system, as described above. Therefore, we need rather the opposite of free banking and much more than just a diversity of currencies.

A serious weakness of the complementary currencies concept is that it has no answer to the decisive question of how currencies should be regulated in order to ensure that they are well-constructed and serve societal goals. Not only commercial currencies but also currencies promoting non-profit projects have a risk of fraud and the risk of bankruptcy of the currency issuer, both leading to losses of the customer's money. These risks must be minimized since the customer's trust is the most important prerequisite for successful currencies. Public supervision by a democratically legitimate authority is still the best way of guaranteeing a proper functioning of the monetary system. This lesson must be learned once again from the financial crisis of the last years, which have shed light on several malpractices and crimes of financial actors. The fact that the central problem of supervision and regulation is not solved in the complementary currencies concept is one aspect that clearly demonstrates the great advantage of the sovereign money concept. Another aspect showing this is that it is vastly improbable that even a great diversity of complementary currencies would be able to counterbalance the negative impacts of the mainstream monetary system.

To replace the current monetary system by a sovereign money system is an imperative not only of economic rationality but also of political justice. We cannot overcome the present crisis of democracy without restoring democratic accountability with regard to the creation of money. The implementation of the sovereign money system on a national or supranational level is one of the most important measures to be taken in order to combat the plutocratic tendencies that pervade our society today. Simultaneously, in combination with a sovereign money system, appropriately regulated non-profit complementary currencies could play a significant role in ensuring economic self-determination of communities on a local or regional level according to the principle of subsidiarity.

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