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Di Muzio on 'Sabotage'

In a series of essays published in 2013 and 2014 on capitaspower.com, political economist Tim Di Muzio explored the concept of 'sabotage' as it applies to capitalist power. I recently rediscovered these essays and was so impressed by them that I have reposted them here as a single piece.

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Di Muzio on 'Sabotage'

Tim Di Muzio

1. The meaning of 'sabotage'

Welcome to a weekly investigation into the fascinating world of corporate sabotage where human creativity, cooperation, mutual aid and well-being are all held ransom for the profit and power of dominant owners.

Every week this column will explore various aspects of what Veblen called 'strategic sabotage.' But first, a bit of context.

It appears that the English word 'sabotage' was at first associated with an emerging working class in the throes of being transformed into docile bodies for capitalists. The origins of the term are a bit fuzzy but it seems like it stems from the French — *sabot* — meaning wooden shoe or clog.

Popular history has it that workers would use their 'sabots' to 'sabotage' production in order to safeguard their livelihoods from machine replacing labor or win better working conditions from their masters. Eventually 'sabotage' could also mean workers deliberately performing poorly at their respective employments or willfully destroying tools or machinery. According to the Oxford English Dictionary (OED) 'sabotage' enters the English language in 1910 and can be defined as:

> The malicious damaging or destruction of an *employer's property* by workmen during a strike or the like; hence *gen.* any disabling damage deliberately inflicted, esp. that carried out clandestinely in order to disrupt the economic or military resources of an enemy (my emphasis).

Clearly, sabotage was both a working class phenomenon and a tactic used in elite European geopolitics in their Darwinist conceived nationalist 'war of all against all.' However, sabotage seemed to apply more to the activity of disempowered workers struggling for rights and better working conditions than it did the powerful and 'productive' capitalists.

It seems a bit strange then, that the term came to be applied to the modern business enterprise by the American born Norwegian political economist Thorstein Veblen. Veblen argued that in its quest for profit, business had to strategically sabotage industry. A free run of production — allowing workers to cooperate to meet the needs and maybe even demands of their communities — would be ruinous for business profit. In *Absentee Ownership*, Veblen argued that the practice of sabotage had more or less been normalized by modern business ownership:

> This line of least resistance and greatest present gain runs in the main by way of a vigilant sabotage on production. So true is this and so impassively binding is this duty of businesslike sabotage, that even in a crisis of unexampled privation, such as these years since the War [World War I], the captains of Big Business have been unable to break away and let the forces of production take their course; and this in spite of their being notably humane persons …
>
> (Veblen, 1923: 217)

Put simply, sabotage knows no mercy in pursuit of profit. But the idea that business could sabotage industry was hardly new. Marx understood this back in the nineteenth century:

> It is enough to mention the commercial crises that, by their periodical return, put the existence of the entire bourgeois society on its trial, each time more threateningly. In these crises, a great part not only of the existing products, but also of the previously created productive forces, are periodically destroyed. In these crises, there breaks out an epidemic that, in all earlier epochs, would have seemed an absurdity — the epidemic of over-production. Society suddenly finds itself put

> back into a state of momentary barbarism; it appears as if a famine, a universal war of devastation, had cut off the supply of every means of subsistence; industry and commerce seem to be destroyed. And why? Because there is too much civilization, too much means of subsistence, too much industry, too much commerce.
>
> (Karl Marx & Engels, 1848: 7)

And Marx was right. In a world where the majority just struggled to meet their daily caloric intake, no one would have complained about the 'overproduction' of food or material comforts. But the difference between Marx and Veblen is that where Marx saw acts of sabotage as periodic responses to economic crises, Veblen argued that it was a permanent feature of capitalist controlled industry. Business has to sabotage human creativity for profit. In fact, he argued that sabotage would be difficult for a small firm to carry out and much easier for large corporations to perfect.

Some have it that the modern corporation was born to minimize transaction costs. This is a charitable view unconcerned with organized power. Others building on Veblen's more critical stance have demonstrated that the birth of the corporation was all about subjecting human creativity to the pursuit of power measured in money (Nitzan & Bichler, 2009). The corporation is not born to minimize costs, it is born to exert power.

Veblen's analysis of the political economy of capitalism was a radical divergence from neoclassical economics — a pseudo-science that would steamroll over all independent, critical and creative thought in the twentieth century. As James Cornehls put it:

> [Veblen's analysis of the business corporation] stood in sharp contrast to the genial, socially productive behaviour of the capitalist envisioned by neoclassical economic theory. Neoclassical economics depicted business people, under the guidance of a benign market, producing as much as they could and striving to lower costs and bring the most cost-effective products to consumers. In Veblen's system this same group of business people would as soon sabotage production as enhance it, in order to obtain a financial gain.
>
> (Cornehls, 2004: 34)

So from working class origins, sabotage comes to be associated with organized business in Veblen's political economy. Next week, we'll take a closer look at how the capital as power approach conceptualizes sabotage with a view to a weekly investigation into corporate sabotage around the world.

2. The poverty of liberal history

Last week we looked briefly at the origin of the term 'sabotage' and found that it was more associated with the working class than it was with elite power — those who largely shape and reshape the terrain of social reproduction. In this formulation, workers sabotage while businessmen build useful industry for the community. In this view, there is no question of how 'workers' appear on the scene of word history intent on working for other people rather than themselves and their families. This is the poverty of liberal history.

In some sense, the old term 'sabotage' is similar to the modern term 'terror.' Originally associated with the murderous policies of the French revolutionary state, in the 20th century, terror no longer applies to the state in mainstream 'common sense' political analysis. Now, terror is always the work of the weak — or the politically deranged — no historical explanation of grievances necessary. Sub-state actors commit terror, states go to war for the 'national interest.' Business is now read in the same way. It's in the national interest.

Yet last week we saw how the recalcitrant Thorstein Veblen applied the concept of sabotage primarily to business rather than workers. This week, we want to consider how the capital as power approach builds on Veblen's application of sabotage to business. To do so, we have to briefly consider Veblen's conceptual split between business and industry.

For Veblen, the industrial system represents a matrix of interdependent points, each reliant to a greater or lesser degree on other points or branches in the industrial system. As the industrial process matures (becomes more complex or networked in contemporary language), Veblen claimed, there results a tendency towards standardization, itself a concomitant of the fact that mass industry requires planning and co-ordination. Without this uniformity of co-ordination and planned synchronization of industrial activity, the industrial system could not develop with any degree of sophistication. In other words, a break or major factor difference in any one branch of the industrial process threatens the entire system, or a great part of it, with collapse.

Left to its own devices, however, the industrial system, Veblen argued, would be extremely productive and has the capacity to flood the world market with a diversity of goods and services. The livelihood of the community then, is best served by an uninterrupted and balanced functioning of the industrial process. But when we think of industry we shouldn't just have in mind industrial machine production. Industry can be simply conceptualized as human potential or capacity — what is possible to achieve in any given age.

This creativity and potential is the necessary base upon which the business enterprise is erected. While the industrial process is materially and structurally prior, it is not in the ascendancy. Business enterprise, with its motives, methods and aims has come to drive the industrial or creative process in pursuit of ever-expanding pecuniary gains — gains determined primarily by the expected or future earning capacity of each individual firm (adjusted for 'risk' for sure). The businessmen in control of each individual firm have this goal in common, though they find themselves in competition to redistribute a limited yearly income to their business empire or corporation.

The competition for market share and profits combined with the growing complexity and interconnectedness of the industrial system and compound human knowledge forces each business enterprise to seek out differential advantages. For Veblen, this process manifests itself chiefly through the strategic control of industry and this involves sabotage as a going business concern. In other words, profit cannot exist without sabotage.

From this perspective, it is not that firms produce for the sake of production, which would be in the interests of the community, but rather, for the sake of profit. The production of material goods and services will be supplied to the community only insofar as the businessman can calculate the vendibility of his product and realize a reasonable rate of profit. This power is rooted in ownership — the legal right to exclude others from use of certain ideas and material artefacts. As Veblen put it:

> By virtue of this legal right of sabotage which inheres as a natural right in the ownership of industrially useful things, the owners are able to dictate satisfactory terms; so that they come in for the usufruct of the community's industrial knowledge and practice, with such deductions as are necessary to enforce their terms and such concessions as will induce the underlying population to go on with the work.
>
> (Veblen, 1923: 67)

The relationship between the two can be stated thus: business needs industry, industry does not need business. Business profit, rooted in ownership, requires sabotage. With these two conceptualizations in mind we can now start to consider how the capital as power framework thinks about sabotage (the relevant reference here is Chapter 12 of *Capital as Power*).

Veblen never had a detailed theory of sabotage, but the capital as power approach tries to make a conceptual distinction between two different forms of sabotage. The first is what could be called 'universal' or 'general sabotage' — the idea that all business firms must actively direct, control and limit human creativity and potential. It does so not for human betterment but for business gain, two opposed metrics.

We will consider copious examples in the weeks to come. But to provide one here, consider two very different firms: a telecommunications company and a home construction firm. Both companies have the capacity to do many things. The telecommunications firm likely has the ability to provide open internet access to the communities where it operates. The home construction firm certainly has the ability to build homes for the community. But neither company will unleash their full capacity to do so because to do so would be too ruinous to their profit margins. They both must, as a strategic necessity, restrict the capacity of the workers they control.

Internet access will only be provided to paying customers despite the fact that it can be provided at cost for all who want to get connected. Homes will be built for paying customers, not for the homeless, the jobless or those in need of shelter or a dwelling. This does not mean that the home construction firm somehow loses the ability to make homes when there are no customers to sell to. It merely means that there are no profitable paying customers — who are likely creditworthy enough to get a capitalized loan from a bank. Both have to restrict capacity pure and simple in order to make a profit.

A free run of production or in our case, allowing workers to provide internet services to the people or builders homes for the homeless would be antithetical to businesses concerns. 'Free is not a business model' (a rep of eBay China quoted in Nitzan & Bichler, 2009: 233). This, Veblen, argued, was the true meaning behind private property:

> Without the power of discretionary idleness, without the right to keep the work out of the hands of the workmen and the product out of the market, investment and business enterprise would cease. This is the larger meaning of the Security of Property.
>
> (Veblen, 1923: 67)

So to be clear, the first form of sabotage is one that all businesses have to engage in to remain profitable — the ability to restrict, limit and exclude. This closely follows Marx's observation that demand must be backed by the ability to pay under capitalism or simply put, capitalists are concerned with profit, not the community. The second form of sabotage, if not general or universal, is 'particular' or 'differential sabotage' (Nitzan & Bichler 2009: first mentioned on 246).

What this means is that individual firms engage in different types of sabotage to gain an advantage over their rivals. Again, examples abound, but to provide one here, consider the new Microsoft Surface tablet introduced to compete with Apple's iPad. Microsoft was late to the cloud storage game but later developed SkyDrive — its own version of iCloud or perhaps the more popular Dropbox. Dropbox has about 200 million users worldwide and their service allows users to store their data on a cloud server so that they can access their files from any device (tablet, computer, phone) they own.

With Surface, Microsoft has sabotaged their new competitor Dropbox — among a host of other software and app providers. While Surface users can download Dropbox as an application, it cannot sync files with the user's Dropbox account rendering it near useless for Surface users. This is differential sabotage in broad daylight.

There is little secret that Microsoft would prefer everyone to move from Dropbox to SkyDrive and force users to shop at its company store — a move it largely copied from Apple's own company store model. There is no technological reason why the Surface tablet cannot support Dropbox on its hard drive. The only reason for this sabotage is Microsoft's profit margin. So one of the greatest saboteurs in human history — Bill Gates — will enrich himself further by creating a noose-like monopoly over newly minted Surface users (provided customers do not become exceedingly irate at the control Microsoft exerts over how they use their newly purchased devices).

The company store is always open and it's the only store.

So in the capital as power framework, there are two forms of sabotage: universal and differential. Next week we'll take a deeper look at the historical relationship between ownership and sabotage with a view to examining business sabotage in more depths as the weeks go by. As we shall come to see, ownership, capitalism and sabotage are born together: the triplets of modernity. But there will be a fourth born: racism.

3. Sabotage and ownership

Last week we considered how the capital as power framework seeks to conceptualize two different forms of sabotage:

1. a general sabotage that limits the potential of humanity in which all business participates and;
2. a particular or differential form of sabotage that is relatively unique to each individual firm.

It should also be noted here that we are primarily concerned with what Nitzan and Bichler call 'dominant capital' or those firms with the highest levels of capitalization and the government organs that facilitate their profitability in one manner or another (for example, protecting patents). In other words, while certain small business owners may have some power to sabotage the potential of human creativity, this power is likely minimal in comparison to the giant saboteurs like Microsoft, Apple, Exxon Mobil and other highly capitalized companies.

This week we take a closer look at the relationship between sabotage and ownership and to do so we must briefly address the transition to capitalism debates. Mainstream theorists or liberals typically read capitalism back into history and argue that capitalist tendencies are more or less hard-wired into the human species. Capitalism is in our genes so to speak. In this way, capitalism is read as a transhistorical phenomenon. It was always with us, but its true flourishing only occurred once barriers to private property and individual ownership were removed through the struggle against kingly and religious authority.

More radical scholars of a Marxian or institutionalist variety argue that this view is ahistorical; that capitalism was a radical break with past practices of human economy and social reproduction and that its origins can be found in one of two places:

1. the changing social property relations of the English agrarian country-side or
2. in merchant trade which allowed commercial agents to accumulate a stock of wealth. They could then plough this additional capital or stock into new production facilities, risking their profit from one trade by investing it in industrial manufacture — the 'real' capitalism for Marx and his followers.

Oddly, rather than form somewhat of a synthesis of the two views, most scholars have tended to keep these two approaches conceptually distinct: it's either one or the other. Moreover, these approaches tend to offer interior explanations that focus on England in particular and Europe more widely, forgetting or ignoring how far broader international relations impacted upon the development of capitalism in Europe. But since these are mainly Marxist accounts, there is a focus on social property relations and the development of industrial production — which, not to put too fine a point on it, Marx identified as the one 'true' capitalism.

But in the capital as power approach, capital is understood as the commodification of differential power rooted in ownership. So instead of looking for a 'true' capitalism in the industrial revolution, we should be more concerned with social property relations in general and the creation of private property or ownership in particular. Where does ownership come from and how did it develop historically? Here both Marx and Veblen are helpful and we will consult them both below. But before we do, let me stress that the main point this week is that we can conceive of private property ownership as the first sabotage that laid the basis for the emergence of the capitalist mode of power.

To be sure, a mode of power that has produced tremendous goods and services and made many advances since the time of organic economies tied the rhythms of photosynthesis. But to only recognize its many achievements is to miss how capitalists are in fact capitalizing the sabotage of human potential — what we could do and be versus what we have become and where we are headed. And if present trends are any indication, we ought to be very worried about which path we are being lead down. From a certain perspective, industrial civilization may be assessed as a giant human catastrophe.

There are no definitive historical records on the origins of ownership. Its origins remain obscure. However, in the capital as power framework, our most promising hypothesis is that ownership must have something to do with the exercise of power. Veblen suggested as much in his essay on the beginnings of ownership. Veblen argued that the mere possession of goods by our ancient human ancestors is an unsatisfactory response to the origins of ownership. Why? The primary reason given is that whatever meagre possessions primitive people may have had, they considered them to be part of their persons — not alienable possessions.

This might seem an odd claim to make but it makes much more sense when contrasted against modern absentee ownership. Modern capitalists do not physically own what they have — for example Bill Gates does not have Microsoft software packages hanging in his home office, the railway cars of the Canadian National Railway in his garage (his second largest public asset) or Deere tractors and engines parked on the lawn of his Seattle mansion (his third largest public asset).

What Bill Gates owns is legal claims on the expected future profit of these firms — not their physical goods. So, Veblen says, the origins of ownership cannot be found in the mere possession of certain artefacts — particularly in a time of dearth when hoarding goods may have been more likely than trading them or giving them as gifts. To quote him directly:

> … in an earlier, non-commercial phase of culture there is less occasion for and greater difficulty in applying the concept of ownership to anything but obviously durable articles.
>
> (Veblen, 1998: 46)

Where then, does he locate ownership? Veblen argues that it first originates with the turn from a relatively peaceful community to one with a predatory habit of life — of which there is considerable historical evidence from crusades to conquests. But even in the predatory mode where one community may invade another, the seizure of their goods, asserts Veblen, is not enough to explain ownership. However, the seizure of persons, argues Veblen, does offer a more convincing explanation for the institution of ownership.

In particular, he argues that the taking of women as trophies by early barbarian tribes are the roots of ownership. First in that these persons are seized as possessions who must obey their master's command; second in that the fruits of their labor go to comfort their owner-master and; third in that possession of one or many women is evidence to others of superior force. For Veblen this relationship of force is eventually institutionalized in the ownership-marriage — the origins, for him, of patriarchy and private property. And indeed, where the institution of marriage did take hold, the wife was typically regarded as the property of the husband. So for Veblen, the birth of ownership results mainly in the sabotage of women or put another way, half the species.

There is some considerable evidence for Veblen's claims but thinking deep back into a primitive human past also relies on a considerable amount of conjecture and logical reasoning based on present knowledge. It also largely fails to appreciate historical changes in patterns of ownership and tenure.

What of Marx?

Marx also had some words to say about ancient primitive societies — also largely conjectural. For Marx, the real historical break comes with the establishment of a simplified class society between workers and capitalists as the means of production are developed and the demographic shift to cities starts to emerge as a key trend. He is less concerned to trace the idea of ownership as a general category stemming from some primitive human past and wants to explain the origins of capitalist private property in England — his major test case.

So the birth of capitalist private property is one of Marx's central concerns in both his early and mature political economy. Consider some representative quotes from as early as 1844 in what has become known as his *Economic and Philosophical Manuscripts*:

> Capital is thus the *governing power* over labor and its products. The capitalist possesses this power, not on account of his personal or human qualities, **but inasmuch as he is an *owner* of capital**. His power is the *purchasing* power of his capital, which nothing can withstand.

> The domination of the land as an alien power over men is already inherent in feudal landed property. The serf is the adjunct of the land. Likewise, the lord of an entailed estate, the first-born son, belongs to the land. It inherits him. Indeed, **the dominion of private property begins with property in land** — that is its basis.

> **Political economy starts with the fact of private property**; it does not explain it to us. It expresses in general, abstract formulas the *material* process through which private property actually passes, and these formulas it then takes for *laws*. It does not *comprehend* these laws — i.e., it does not demonstrate how they arise from the very nature of private property.

> Wages are a direct consequence of estranged labor, and **estranged labor is the direct cause of private property**. The downfall of the one must therefore involve the downfall of the other.
>
> (Karl Marx, 1844)

And from Capital, Volume 1:

> Political economy confuses on principle two very different kinds of private property, of which one rests on the producers' own labor, **the other on the employment of the labor of others**. It forgets that the latter not only is the direct antithesis of the former, but absolutely grows on its tomb only.
>
> (K. Marx, 1867)

These quotes all point in one direction: expropriation. In order for some to become the owners of capital — first in land — others have to be completely dispossessed of any access, tenure or relationship they may have had with the land outside of monetary relationships. And indeed, Marx called this process of expropriation primitive accumulation.

Unlike early liberals who viewed primitive accumulation as the accumulation of money for investment, Marx understood it as the forcible movement in late feudal Europe to dispossess peasants of their commons and customary rights to land. Commonly referred to the enclosure movement or the agricultural revolution, the expropriations contributed to growing pauperism and poverty. The enclosure movement did not create wage-workers. It created paupers who could then be employed as wage workers.

Thanks to David Harvey and others, there has been a bit of a revival of the concept of primitive accumulation. It turns out that expropriation did not end with the enclosures of land. But from the capital as power framework, there is no 'primitive accumulation.' There is simply accumulation — the attempt by the few to accumulate monetary wealth regardless of the means employed. But whether we want to keep or jettison 'primitive accumulation,' Marx's focus on social property relations (and their transformations) is important.

For Marx, modern capitalist private property is founded upon the sabotage of the commons and customary right. In order for the great English landlords to become obscenely wealthy, the majority of peasant workers not only had to be made non-owners but far worse, non-tenured paupers. As Polanyi (1964) suggested in his major work, political economy and pauperism are born together. But capitalism would require one more thing. To safeguard private property, royal authority itself would have to be sabotaged.

Next week we'll take a closer look at how exclusive ownership to private property was born in a struggle against princely power.

4. Royal authority and private property

Last week we considered the concept of ownership though the work of Veblen and Marx. We noted that the establishment and protection of private property involved the dispossession of the many by the few and that this tendency begins with the appropriation of humans (slavery) and land for private profit.

Keeping with Marx's recognition that we ought to be concerned with a transformation in property relations when considering the emergence and development of capitalist private property, this week we consider how royal authority in England was challenged and largely incapacitated by an emerging ruling class of capitalists. The old feudal strictures could not hold under the weight of newly organized capitalist power.

We are concerned with England primarily because it is on this tiny island where we first see the most systematic transformation of social property relations towards exclusive private property for the few (at least in practice). Moreover, it is an interesting case to look at because a body of political theory will develop to not only justify private property but to challenge the idea of a monarchy altogether. Many writers, such as Algernon Sidney, would lose their heads for advancing such ideas.

But where to begin?

The Norman Conquest of England in the Battle of Hastings of 1066 is a key point of departure for two reasons. First, because the conquest established that all the land of England was now the private title of William the Conqueror or William I. After having won England through a violent invasion that dispossessed Saxon leadership, William and his soldiers pacified rebellious populations and created many castles to fortify his newly won kingdom. In return for military service William granted large tracts of land to his soldiers. These men became barons or lords of manors but they did not own their lands. They held them as grants or privileges extended by the monarch. Indeed, even in Hobbes' Leviathan we find that whatever liberty and property a subject of the kingdom may have, he enjoys it at the pleasure of the monarch (Hobbes, 1980).

In other words, the lords of manors did not have absolute private ownership over the lands they were granted. They used this land at the pleasure of the William I and successive kings. Of course in practice the lords of manors did have 'possession' of their granted lands as did others who were granted diverse forms of feudal tenure. However, in theory, since all of England was the King's land by allodial right gained through conquest, the land or the proceeds of it could be confiscated by the King though direct seizure or through the introduction of new taxes. One of the major reasons why royal authority might engage in such practices was to fund wars waged to advance the power and riches of the monarch and his merchant and landowning supporters.

The second reason why we begin with the Norman Conquest is because it is the primary reference point for virtually all contending parties during the English Civil War (1642-1651). To summarize a complex historical debate, there were largely three contending forces that all used the memory of the Norman Conquest in their attempts to advance their desired political positions. All of their discourses were steeped in religious language that we will largely ignore here.

The first were the social forces of royal authority — the King (Charles I 1600-1649), his court and his supporters in Parliament and elsewhere. One line of argumentation ignored the Norman Conquest altogether and contended that Charles I ruled by divine right. Legitimacy or rule, as it were, was conferred by God's will and therefore the King was not subject to any other earthly authority.

This line of reasoning, however, did not go down well with Charles' wealthy subjects who were challenging a royal prerogative free from Parliamentary consent. The forces of royal authority will not totally abandon this line of reasoning but they will also advance a further claim: the right to rule is rooted in the original Norman Conquest. Why does Charles I have absolute authority? The answer: by right of conquest, just as the King's sovereignty was extended to newly conquered lands in North America. Since elite social forces would be familiar with this justification, those who opposed the royal prerogative would have to tread very carefully indeed.

The answer of the second group of social forces — in short hand called here the Parliamentarians — was that the Norman Conquest never took place. Instead, William I was no conqueror but heir to the throne of England. In this way, the conquest was disavowed. If William I was heir to the throne of England, and not its conqueror, then a new position opens up: William I ruled by respecting the rights and privileges granted to Englishmen by the ancient Saxon constitution. Such a constitution did not allow for arbitrary rule since the King had always — since time out of mind — ruled with Parliament. Whether convincing or not from a legal point of view, this was the line of argumentation that would ultimately be victorious, if only because the argument was backed up by the decisive force of arms required to win the Civil War. The Royalists were defeated and King Charles I lost his head.

The monarchy would be restored about ten years later and by 1688 when William of Orange was invited to the throne, the monarch was made subordinate to Parliament. With the royal prerogative now in a shambles, the men of property were now in control of the English state or as Polanyi put it, 'the government of the Crown gave way to the government of a class' (1964). It is not that these men lacked possession of land or wealth when monarchs reigned. They did. But possession was not enough. With the threat of royal prerogative their property could be confiscated by the decision of the monarch. This is what was ultimately at stake for those wealthy Parliamentarians that fought and financed the war against royal power: a say in their own governance and the protection of their fortunes.

And this is where liberal historiography ends: with the triumph of Parliament over an arbitrary monarchy. But the struggle to sabotage princely power and subject it to the will of a newly propertied class was not just a struggle that looked upwards towards the King. It was also a struggle directed at the social forces from below — those without significant property or power.

In the tumultuous times of the Civil War, more radical social forces emerged that not only questioned royal authority but the entire structure of society. They can roughly be divided into two camps: the Levellers and the Diggers. Both will argue, like the Royalists, that a conquest did indeed take place in 1066. From this point, the rights and privileges of Englishmen were increasingly usurped not only by the monarch but by the lords of estates. Great wealth in the hands of the few is the result of the conquest and government is little more than a war waged against the poor. Politics is the extension of war by other means.

The Levellers wanted an extension of the franchise but in the Putney Debates, Cromwell's son-in-law argued that the unequal distribution of property would be challenged if all men in England could vote. They would vote, it was imagined, for a more just distribution of property. Whether or not this be true, the threat was real enough. The debate was not solved by reason. It was settled by murdering the Leveller's leadership.

The Diggers were even more radical. They did not believe in laboring to enrich a master and abhorred wage-labor. Instead, they were concerned to work the land in common for the benefit of the community. Private property, their leader reasoned, was the chief reason for political faction and violence in support of the powerful. Common property and working collectively could solve these problems. This was heresy to the powerful and the Diggers were chased from the land they had so carefully tended during those years where 'everything was turned upside down.'

So arbitrary royal authority was a threat to the men of property just as much as democracy. Or, if we want to put it in a slightly different way: popular democracy would (not could – *would*) sabotage the privilege of a small minority of property owners by calling the unequal distribution of property into question. The so-called founding fathers of the United States would fear much the same.

Could the constitution of the United States be considered a form of sabotage? We'll discuss this next week.

5. The constitution of the United States of America

It is by now fairly clear that the Congress of the United States is a 'do-nothing' Congress populated by 268 millionaires (out of 534 lawmakers). The job approval rating, depending on which poll we consider, hovers around 9-14%. This is perhaps hardly surprising given that the Republican Party vowed to sabotage Democratic and presidential initiatives as soon as Obama became President of the United States. But are there deeper structural roots to this inertia? Why does Congress seem so incapacitated? How far and in what ways could we consider the Constitution of the United States an act of sabotage by its promoters?

At first this may seem like a strange question, but if we return to the context in which the document was written we may gain some greater clarity and find out why the federal system of government is hardly responsive to the needs and desires of the majority of American people. In fact, the Princeton political scientist Martin Gilens found that 'influence over actual policy outcomes' in the United States 'appears to be reserved almost exclusively for those at the top of the income distribution' (Gilens, 2007). This was not always so, but since the 1980s the United States has, for all intents and purposes, become a plutocracy.

The first thing to remember is that the so-called 'founding fathers' were not debating the establishment of a democracy. Rather, their primary concern was how to found a *republic*, or a state without a monarch. According to Ellen Meiksins Wood's *Democracy against Capitalism*, the very concept of 'representative democracy' that the American constitution eventually guaranteed was historically new and contrary to earlier forms of direct democracy that did not alienate political power. As she reminds us:

> We have become so accustomed to the formula, 'representative democracy' that we tend to forget the novelty of the American idea. In its Federalist form, at any rate, 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*.
>
> (Wood, 1995: 216)

So our question must be why direct forms of democracy were incapacitated and representative democracy on a federal scale implemented?

The answer to this question can be gleaned by considering the social forces at play when the Federalists took up their pens to advocate for federal government. They were opposed by the anti-federalists who argued that the new constitution would centralize power and jeopardize the rights and liberties of individuals, localities and states. We also have to recall that there were really two American revolutions — the first was directed at power from above — that is to say, against King George III and his parliament of propertied men. The list of grievances against the King can be found in the American Declaration of Independence.

Yet according to Benjamin Franklin, one reason stood out (Greene & Jellison, 1961: 492). The main reason for the revolutionary war was not so much taxation without representation but the fact that George III and the Bank of England largely forbade the use of Colonial script — paper currencies popular in the colonies. The Currency Act of 1764 sabotaged the domestic currencies and apparently caused recessionary conditions in the colonies because it restricted the money supply. Just over a decade later, leading colonists would form the Continental Congress. With borrowed money from France and the Netherlands, the rebellious colonists waged war against imperial Britain and by 1783 declared victory.

That was the first American Revolution.

The second American Revolution followed soon after. It was a counter-revolution directed at the people themselves by the ruling social forces of slavery and capital. From the perspective of the ruling class, the decades of resistance and revolution generated new threats to the social order from below — threats that made Federalists realize that the Articles of Confederation were inadequate for the task of encoding their power in institutions after the revolution.

The major fear here was that the people had become too involved in their own governance, and often initiated legislation that harmed the minority of affluent property owners. Debt and tax relief, as well as emissions of paper money threatened the accumulation strategies of wealthy citizens. And where state legislatures were not responsive to popular demands for relief, aggrieved citizens often took up arms in open rebellion, regularly justifying their resistance by appealing to the language of liberation spawned by the revolution. What made matters worse, however, was the realization, articulated most forcefully by Madison, that an impending class war was perhaps inevitable.

In devising the national government of the United States, James Madison was careful to inform the delegates at the Constitutional Convention that they were not only deciding the design of republican government, but also its fate. Whilst Madison identified a number of threats to republican government, he identified and stressed one ultimate danger: 'the violence of faction.' For Madison, factions were inevitable if liberty was to be preserved. He feared, however, that 'the superior force of an interested and overbearing majority' might ultimately threaten the rights of the minority (Madison, 1787a).

Whilst he identified a number of sources of faction, he argued that 'the most common and durable source of factions has been the *various* and *unequal* distribution of property.' Here, Madison was certainly concerned with the diversity of property ownership and the possibility that there would be conflicts between men of property in regards to policy. What Madison was more concerned about, however, was the *unequal* distribution of property and the fact that 'those who hold and those who are without property have ever formed distinct interests in society.'

In this context, we do well to recall that Madison and others not only had access to political theory, but also the historical experiences of other class divided societies. In designing the constitution, Madison realized that whilst the present distribution of property in the United States bore directly on the design of the national government, the future was perhaps more important. He remarked that whilst 'the United States have not reached the stage of Society in which conflicting feelings of the Class with, and the Class without property, have the operation natural to them in Countries fully peopled,' the future would be different:

> In future times a great majority of the people will not only be without landed, but any other sort of, property. These will either combine under the influence of their common situation; in which case, the rights of property and the public liberty, will not be secure in their hands: or which is more probable, they will become the tools of opulence and ambition, in which case there will be equal danger on another side.
>
> (Madison, 1787b)

Thus, whilst the special circumstances in the thirteen newly independent states served to suppress 'conflicting feelings' that were 'natural' to the propertied and propertyless, Madison certainly anticipated a future were these conflicts would inevitably surface. However, in perhaps one of the most telling passages in the records of the Federal Convention — records that were not released for public scrutiny until 1840 — Madison admitted that the germs of class conflict were already blossoming in post-revolutionary America:

> It ought finally to occur to a people deliberating on a Government for themselves that as different interests necessarily result from the liberty meant to be secured, the major interest might under sudden impulses be tempted to commit injustice on the minority. In all civilized Countries the people fall into different classes having a real or supposed difference of interests. There will be creditors and debtors, farmers, merchants and manufacturers. There will be particularly the distinction of rich and poor. It was true as had been observed, by Mister Pinkney, we had not among us those hereditary distinctions, of rank which were a great source of the contests in the ancient Governments as well as the modern States of Europe, nor those extremes of wealth or poverty which characterize the latter.
>
> We cannot however be regarded even at this time, as one homogeneous mass, in which everything that affects a part will affect in the same manner the whole. In framing a system which we wish to last for ages, we should not lose sight of the changes which ages will produce. *An increase of population will of necessity increase the proportion of those who will labour under all the hardships of life, and secretly sigh for a more equal distribution of its blessings*. These may in time outnumber those who are placed above the feelings of indigence.
>
> According to the equal laws of suffrage, the power will slide into the hands of the former. No agrarian attempts have yet been made in this Country, but symptoms, of a leveling spirit, as we have understood, have sufficiently appeared in a certain quarters to give notice of the future danger. How is this danger to be guarded against on republican principles? How is the danger in all cases of interested coalitions to oppress the minority to be guarded against?
>
> (Madison, 1787c, emphasis added)

What this passage reveals is not only a concern to secure the minority against the majority in the present, but also in the future. In other words, the politico-strategic rationality that informed the constitution was not a provisional consideration of the present but a going concern to be operationalized in the very design of the national government.

Given the likelihood of a protracted class war and the possibility that more propertyless people would be enfranchised over time, answering the question of how to guard the minority of property owners against the majority of propertyless became the ultimate security problematic. Indeed, as one student of the Constitution has noted:

> … the original focus on property placed inequality at the center of American constitutionalism. For the Framers, the protection of property meant the protection of *unequal* property and thus the insulation of both property and inequality from democratic transformation … Effective insulation, in their view, required wealth-based inequality of access to political power … The inherent vulnerability of all individual rights became transformed into a fear of 'the people' as a threatening propertyless mass whose power must be contained.
>
> (Nedelsky, 1990: 2)

Building on his theory of inevitable class conflict, Madison argued that only a larger political union could suppress majority rule and protect what he called the 'public liberty.' As many Anti-Federalists recognized, this was a complete reversal of republican political theory which argued that only small governmental units could protect the liberty of the people. With the experience of some of the state legislatures in mind, Madison, however, reasoned that small governmental units were vulnerable to majority rule and factious combination.

As Holton (2005) has suggested, Madison's strategy was to divide the population by extending the scale of government so that the minority, who could more effectively organize around issues and candidates, could rule it. In this way, Madison argued, 'a rage for paper money, for an abolition of debts, for an equal division of property, or for any other improper or wicked project' would be frustrated by the electoral system spanning the entire voting population (Madison, 1787a). However, the attempt to drown out popular voices was only one way of answering the question of how 'interested coalitions to oppress the minority' could be guarded against by a national government.

Another mechanism which proved to be of crucial importance was the creation of a national army to suppress rebellious activity domestically. For the early liberals that informed the American political debate, standing armies were always identified with despotism. But a standing army is exactly what the men of property wanted. Today, they have the largest military force on the planet.

In this light we can assess the constitution of the United States — particularly given that there were more democratic options. We can suggest that the constitution was not designed to facilitate democracy. It was designed to incapacitate it. It is not that democracy was a threat to property *per se*. It was more the case that democracy was a threat to radically unequal property and therefore radically unequal political power.

Today, 1% of citizens in the United States own 35.4% of all net worth. The next 19% own 53.5%. The remaining 80% collectively own 11%. In other words, about 45.6 million adults own 89% of all the wealth in the United States. The remaining 182,545,600 adults have 11% to split between them.

With this in mind, we might conclude with the progressive historian Vernon Parrington's apt observation:

> … the drift toward plutocracy was not a drift away from the spirit of the Constitution, *but an inevitable unfolding from its premises*; that instead of having been conceived by the fathers as a democratic instrument, it had been conceived in a spirit designedly hostile to democracy; that it was, in fact, a carefully formulated expression of eighteenth century property consciousness, erected as a defense against the democratic spirit that had got out of hand during the Revolution, and that the much-praised system of checks and balances was designed and intended for no other end than a check on the political power of the majority — a power acutely feared by the property consciousness of the times.
>
> (Parrington, 1930)

(Some of this post is excerpted from my 'Empire of Liberty and Domination' now published in Gill and Cutler's (eds) *New Constitutionalism and World Order*.)

6. The capitalization of money creation: The greatest sabotage in human history?

Every year in my course on Political Economy in the New Millennium I ask my students to do an exercise. The task is for them to ask three members of their friends or family how money is created. As you can imagine, the answers diverge widely from 'the government prints it' to the 'central bank makes it.' Some just throw their hands up in the air and say they don't really know. And the vast majority of us do not.

But I'm also guilty. My entire post-secondary degree I could not have really answered the question with any accuracy. I might have been able to rattle on something like this: someone who wants to save money goes to a bank and deposits it. Since the depositor will not likely take out all of their money at once, the bank can then lend a portion of the deposit to customers who want to borrow. For this service, the bank makes a profit by paying less in interest to the depositor than it receives from the debtor taking out the loan. I would also have been able to tell you that the money supply can expand in this way thanks to fractional reserve banking.

How does this work?

The key to understanding it is to consider the idea of a reserve ratio. The story goes like this: the central bank tells commercial banks that they must hold a certain percentage of cash on hand. Supposedly this is to ensure that there is some cash in the bank and that it isn't all loaned out. After all, if everything was being lent out, there would be no cash for depositors to withdrawal! And here's where the expansion bit comes in. Let's take a look at it in stages.

First, I go to the bank and deposit $100 dollars.

Let's suppose the central bank has asked my bank to keep a reserve ratio of 10%. In other words, the bank only holds a fraction of the deposit as a reserve: hence, fractional reserve.

That means the bank has to keep $10 on deposit but can use the other $90 for loans.

Sam comes to the bank and takes a loan out for $90 and deposits this into an account.

The bank must hold back 10% of $90 or $9 but can loan out a further $81.

Let's now check in and see how much money has been created:

So far, out of my initial $100: $90 + $81 = $171 has been created.

This process can continue until the initial $100 dollars is worn out by reserve requirements as banks make more loans.

That much I could have told you. And I would have been completely wrong! In fact, most students of economics would repeat something like the above because this is pretty much what modern neoclassical economics teaches. It is incredibly misleading.

So why is it that most of us are so bad at being able to explain how money is created let alone what it is? The first reason might be because the fractional reserve thesis has managed to convince the ones who care to ask the question in the first place. But since the vast majority of us would not be able to answer the question, a second hypothesis should be considered: that finance is the language of the minority in power and that those who profit from the current monetary system have a keen interest in making sure the population remains confused on the issue. This would help to explain all the secrecy surrounding the banking industry, the second largest capitalized industry on the planet after oil and gas (if we include the estimated market value of state run oil and gas firms — see DiMuzio, 2012 for further clarification).

One of the chief edicts of many of the Slave Codes was that slaves should not be allowed to read or write. It was thought that if they gained this capacity it would be easier for them to communicate, organize and overthrow the slave mode of power. And we all know what literacy and the printing press did for the unity of the Catholic Church! In the same way, so long as we remain financially illiterate we will have little chance to communicate, organize and overthrow the capitalist mode of power let alone offer a workable and sane alternative.

So how is money actually created?

In the majority of the world — and particularly the OECD – about 97% of all money is created through digital loans by commercial banks. They do this by entering numbers into a computer when someone takes out a loan. So for example, if I go take a personal loan for $1000 from a commercial bank, the bank records the $1000 as a liability for me and as an asset for the bank. This means that our money is created as debt bearing interest.

The other 3% is created in physical notes and bills by the government — typically by what is called a Mint. The government sells these notes and bills to banks at face value. So for example if the government prints $1000 worth of $100 dollar notes, a commercial bank will by those notes for $1000. But, since it typically costs the government less money to print money and forge coins, the government can turn a profit on the difference between the face value of the notes and the actual cost of producing the notes. So for our $1000 face value example, consider it only costs the government $1 dollar to make. Profit would be $999 and this would go into the government treasury to fund operations and help service the so-called 'national' debt.

To many, this revelation is rather shocking but it has more or less been the way our capitalist societies have been creating money since the increasing use of computers and abandoning the gold standard in the early 1970s. (For those who want to learn more by using the UK as an example there are a series of videos at Positive Money that explain the process in a relatively straightforward way.)

Our concern in the capital as power framework, however, is not simply with how money is created, but its very capitalization. Since commercial banks produce most of the world's money as interest bearing debt and the banks are owned by a small minority of people worldwide, how, we might ask, did this relationship come to be? Creditors with the power to create money out of thin air and a world filled with debtors drowning in interest payments.

We'll consider this history next week and perhaps strangely, the story actually begins with a dearth of money in England, before the Glorious Revolution of 1688. What transpired could be considered the largest sabotage in human history.

7. The privatization of money: The greatest sabotage in human history? Part II

Last time we found out that modern money is created when commercial banks make loans to people and businesses. They are not loaning out other people's money at all, but effectively creating it by entering numbers into a computer. Between Part II and the last article I wrote, a further revelatory article was published in the Guardian by David Graeber of *Debt: The First 5000 Years* fame. The article (Graeber, 2014) is worth considerable thought for anyone who wants to understand modern capitalism. As I hinted at last week, even the capital as power framework has been silent on the issue of money and its creation as interest bearing debt.

This week, I want to share some of my new research with you on the history of money, how the creation of it was privatized and why this act can be considered the greatest sabotage in human history. As this is a blog post and not an academic paper, my history will be somewhat stylized.

One of the key questions the capital as power approach asks is: what are investors capitalizing when they invest in or come to own income-generating assets? Since we are concerned with money created as debt, in this article we ask what are bank owners capitalizing? The simple answer to this question is that they are capitalizing the bank's power to create money as debt by extending loans to businesses and people in need of money. This requires exclusion and therefore sabotage to function: counterfeiting must be made illegal and punishment swift if banks are to have this exclusive power. For example, the maximum sentence for counterfeiting in Australia (where I write from) is 14 years in jail. In the United States it's 15 years in the slammer.

Since everyone needs money to transact in a market economy — including governments — this gives the owners of banks and their directors tremendous power over human life and patterns of investment, development and differential accumulation we experience. The creation of money by banking corporations is also a wonderful system for ensuring that a tiny minority (the owners of the banks) continue to grow ever wealthier from interest payments, dividends and rising stock prices. There's a reason why most bankers at the top of the food chain are wealthy and their banks are the second most heavily capitalized industry on the planet: the demand for money is both high and constant.

How did this happen?

It has been well documented by numismatists (people who study money) that diverse historical political communities used a variety of materials as early forms of money. For example, the Aztecs used the cocoa bean as a form of currency. But since we are concerned with the creation of modern money we can skip a deeper history of money and move to our major turning point: the establishment of the Bank of England in 1694.

The first thing we have to recognize is that in Europe, the most coveted form of money came to be silver or gold coins. This was largely a legacy of the Roman Empire in Britain but the history stretches all the way back to Lydia (a part of Turkey) and King Croesus's creation of coins (560 to 547 BC). Gold and silver coin were also highly coveted because they appeared to be universally admired and the only main currency in international trade. An absence of gold and silver coins effectively meant you could not participate in trade — and for Europe, which coveted the riches and luxuries of Asia, this meant a race to find more gold and silver to pay for imports. Since gold and silver were the only things that could technically act as money, the only way the money supply could increase was by producing more gold and silver, trading goods with other nations, or stealing/confiscating/pirating it from others.

In England, the dominant form of money was silver coin and its production was the purview of the sovereign or monarch. Gold was also used and in circulation but England in the 1600s did not have a considerable amount of gold and did not move to a gold standard until the next century. Lacking any significant gold mines, the English relied on trade to bring gold into the country. Much later, it would extract considerable amounts of gold from its colonial possessions such as Australia. However, the key problem in England in the 1600s was the scarcity of money.

A bevy of pamphlets on the money situation of the country clearly identify this problem. It was a major problem because leading thinkers of the time understood that England was becoming more productive and the dearth of money would not allow for the full circulation of goods. Like today, people complained for a want of money. Part of the reason (we won't go in depth about this here) England was becoming more productive was its use of coal energy — the result of Britain denuding its forests rather rapidly. Since energy means the capacity to do work, with more energy coming online, England could become more productive. Over time, Britain became the first country to achieve sustained economic growth (Wrigley, 2013).

So in modern parlance, England's economy was running far below its capacity for want of money. Recognizing the situation a number of interested parties set forth to find a solution. The most decisive was the Hartlib Circle (a network of friends interested in improvement and science) who operated from 1630-1660. This group arrived at the conclusion that money did not have to be metallic coins. For many, this was hearsay, but necessity forced the idea that money was not necessarily a material thing but a medium of some kind founded on trust. This idea made it possible to conceive of money as credit — as something beyond gold and silver coins. Of course credit in the form of paper notes had long been in existence but it was highly personal, largely untransferable and as such, could not expand the money supply, which was the identifiable problem.

So the key problem was how to expand the money supply. There were many banking precursors Hartlibians and other thinkers could rely on — particularly Italian and Dutch banking practices — but neither would suffice to solve the problem of expanding the money supply. As Wennerlind notes of the Dutch experience:

> In fact, England was largely self-sufficient when it came to ideas about credit. While political economists sought inspiration from the Dutch on all matters commercial, their financial innovations were considered inadequate to answer

> England's needs and were thus rarely given serious consideration in the English debates. More precisely, because the Dutch did not develop a national debt backed by the nation-state, did not enjoy a liquid secondary market in public debt instruments to complement its stock market, and, most importantly, did not issue a generally circulating credit currency, Dutch finance did not constitute a model that the English sought to emulate directly.

> … On the continent, banks had already transcended the disadvantages associated with the lack of quality coin. The Bank of Amsterdam, founded in 1609, provided traders in the Dutch Republic with a convenient and secure paper currency. However, because the paper currency was fully backed by coin in the vault, the Bank of Amsterdam did not augment the overall money stock, at least not in a significant way.
>
> (Wennerlind, 2011: 8 and 69)

But while the Hartlibians were concerned to stimulate the economy by introducing more money into the economy, the real innovation of credit money derived from the need of William III and his Parliament to fund a war with King Louis the XIV of France. Traditionally the monarch was responsible for funding all wars out of the royal estate and whatever customary taxes were owed to the sovereign. Hence, there were strict limits imposed upon the monarch in regards to finance, often forcing the Crown to borrow from private subjects to finance war-fighting exploits. This typically meant the accumulation of debt and the alienation of more of the royal estates by sale to private persons. An additional alternative was the leasing of royal lands for a fee or forcing loans — a practice disdained by merchants and moneylenders. Since ordinary people were largely outside of the money economy until the money supply grew and new taxes were issued, the tax burden fell most heavily on merchants and the propertied.

What this amounts to is the simple fact that finding a way to finance war was a key factor in England's monetary and financial revolution. The answer to the problem was twofold: the creation of the Bank of England and the long-term 'national' rather than sovereign debt. Both would arrive on the scene once the propertied of England made the Crown subordinate to Parliament in 1688.

A Scot, William Paterson introduced the scheme for the Bank of England which was chartered in 1694. The bank was given the exclusive right to extend credit to the government at interest. In turn, the government promised to finance the interest on its loans by providing creditors with a portion of its tax revenues. The creation of money was no longer the prerogative of the sovereign but of private social forces interested in the accumulation of evermore money. From the point of view of capital as power, investors in the Bank of England were capitalizing the state's power to wage war and tax its subjects.

After the creation of the Bank of England, taxation exploded in Britain to cover the interest on the so-called national debt — a debt owed to the 1% of bank owners. The British became the most taxed in history. An article appearing in 1820 captured the automatic progression in taxation:

> Taxes upon every article that enters the mouth, or covers the back, or is placed under the foot — taxes upon everything which is pleasant to see, hear, feel, smell or taste — taxes upon warmth, light, locomotion — taxes on everything on earth, and the waters under the earth — on everything that comes from abroad or is grown at home — taxes on the raw material — taxes on every fresh value that is added to it by the industry of man — taxes on the sauce which pampers a man's appetite, and the drug that restores him to health — on the ermine which decorates the judge, and the rope which hangs the criminal — on the poor man's salt and the rich man's spice — on the brass nails of the coffin, and the ribands of the bride — at bed or board, couchant or levant, we must pay. The school-boy whips his taxed top; the beardless youth manages his taxed horse with a taxed bridle, on a taxed road; and the dying Englishman pouring his medicine, which has paid seven per cent, into a spoon that has paid fifteen per cent, flings himself back upon his chinz (299) bed, which has paid twenty-two per cent, makes his will on an eight pound stamp, and expires in the arms of an apothecary,

> who has paid a licence of £100 for the privilege of putting him to death. His whole property is then immediately taxed from two to ten per cent. Besides the probate, large fees are demanded for burying him in the chancel. His virtues are handed down to posterity on taxed marble, and he will then be gathered to his fathers to be taxed no more.
>
> (Davies, 2002: 300)

Heavy taxes are the necessary corollary of a monetary system based on money as interest bearing debt owed to the few.

But how was the money supply eventually increased?

Paterson himself was a banker and there is little doubt that he understood precisely what merchant bankers were up to before the creation of the 'national' debt and the Bank of England. Like goldsmiths and other bankers, he understood that the gold and silver received on deposit would largely remain at the bank for reasons of security and the convenience of handling paper notes rather than heavy coins. The depositor would simply deposit gold, silver or both and receive a note of receipt. This receipt could then be used for making transactions without bothering with metallic money. As long as depositors were confident they could exchange their notes for their coins, all would be well.

Paterson suggested that the Bank of England could do the same but on a far larger scale. He ensured that the credit money issued was backed by reserves of good quality silver coin. He reasoned that the Bank would only have to keep 15-25% of silver in reserve and on this basis, start extending credit. The fact that the notes in circulation were not backed by an equivalent amount of silver coin, of course, was not broadcast to the public. But to shore up trust among the people that mattered to his scheme, Paterson also reasoned that investors/depositors in the Bank could feel secure in receiving payments since Parliament had the right to tax its subjects for payment of interest on the 'national' debt. This, in short, was the original means by which the money supply was extended through debt. As one historian of money noted:

> When the government established a royal commission to inquire into the activities and reserves of the bank, the bankers would only respond that the reserves were "very, very considerable." When asked to be a bit more specific, they said that they would be "very, very reluctant" to add to what they had already said.
>
> (Weatherford, 1997: 160)

But to make this sleight of hand system work, investors were capitalizing far more than the ability of the Bank to profit off the 'national' debt. As Wennerlind has demonstrated, the new system of debt money required the death penalty for counterfeiters. In other words, the exclusive right to create money demanded the violence of the state. Dozens were put to death at the hands of Sir Isaac Newton — who accepted the responsibility for catching counterfeiters as the Master of the Mint.

This was not necessarily a new practice. Historically, people found counterfeiting were subject to all kinds of gruesome torture and often death (true as well in China). But it was difficult to know the true source of counterfeiting and thus it was difficult to punish and thus create deterrence by providing a symbol to others. The creation of debt money reinforced the impetus to find and punish counterfeiters. In this sense, early investors in the Bank of England were capitalizing the state's power to command the death of its subjects.

But killing counterfeiters was not enough to ensure the monetary revolution and the security of the new organized creditors. Since excessive taxation was unpopular, the national debt could be funded in another way: the transatlantic slave trade, the trafficking of human beings from West Africa to Spanish America and ultimately the British colonies. Towards this end, the South Sea Company was established to help fund the national debt and service the interest owed to investors in the Bank of England. The company had the 'right' to transport and sell 4,800 slaves to the Spanish colonies per year. In effect then, investors in the

Bank of England capitalized one of the most reprehensible practices in all of human history.

Guarding the exclusive right to creating money as debt also meant sabotaging colonial currency in what we today call the United States. The British colonies also suffered from a dearth of silver and gold to facilitate their trade and repay their debts — many of which were owed to British merchants. The scarcity of money problem was solved — however imperfectly — by issuing debt-free paper currency in relatively controlled amounts. The debates are more complex than I can allow for here, but one thing is certain: the Bank of England wanted to extend its power to the colonies and could not permit the colonists to issue their own currency.

This was viewed as a key challenge to the bank's monopoly on money creation through debt. I do not want to oversimplify or suggest that the origin of the American Revolution is monocausal, but the Currency Act of 1764 goes a far way in explaining why colonists would take the massive risk of taking up arms against their perceived oppressors. Indeed, upon being interviewed by the House of Commons in 1766, Benjamin Franklin said the following when asked why colonists had lost respect for Parliament:

> To a concurrence of causes: the restraints lately laid on their trade, by which the bringing of foreign gold and silver into the Colonies was prevented; the prohibition of making paper money among themselves, and then demanding a new and heavy tax by stamps…
>
> (Franklin, 1766)

The tax was disliked because everyone was forced to pay it and Franklin reasoned that there was not enough gold and silver in the Colonies to pay the tax. He argued that to pay the tax, the colonists would have to be compelled by arms. In this way, investors in the Bank of England were also capitalizing the attempt of Britain to enforce its rule over the recalcitrant colonists once they finally rebelled. After the victory by the colonists, the money problem as well as the debt contracted by the war loomed large in the debates on how to establish a new republic. We cannot entertain these debates here, we only note their importance for the history of banking, state-formation and the creation of money in the United States.

Eventually, states started to adopt (or were forced to adopt) a silver or gold standard — for example Japan adopted a gold standard to participate in international trade. But as I mentioned last week, by the 1970s, this system had proved too restrictive (as it had done so before) and the monetary system known as Bretton Woods was effectively abolished by the United States when it no longer backed its paper currency with gold. Thanks to the massive demand for oil and the fact that other commodities were denominated in US dollars, the Nixon administration could be sure of continued demand for dollars.

In most of the world we now have fiat debt money backed only by the force of the government. As already stated, most of this money is lent into the economy when people take out mortgages, credit cards, car loans, student loans, personal loans etc… The more in debt we are, the more money there is and the more bank owners stand to make off interest and fees. This helps us explain why the richest countries on the planet are also the ones with the most 'national' and personal debt loads.

But the important thing to know is that the very few capitalize the power to create money as debt and so long as we continue with this system, we can expect many, many morbid symptoms.

It doesn't have to be this way.

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Notes

The cover image (from Wikimedia commons), is a CIA manual from 1944 that gave advice for how sympathetic citizens in occupied countries could sabotage their regimes. Details here.

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Uncategorized

CAPITAL AS POWER · ECONOMIC HISTORY · MONEY CREATION · OWNERSHIP · PROPERTY RIGHTS · SABOTAGE · TIM DI MUZIO · VEBLEN

Published by Blair Fix

Political economist. Blogger. Muckraker. Foe of neoclassical economics. *View all posts by Blair Fix*

Previous
Power Over Principles

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How Dominant are Big US Corporations?

21 comments

Clint Ballinger
SEPTEMBER 27, 2021 AT 4:33 PM

On the banking bit and "97%" or similar figures…you have to remember that warehoused £s /$s etc — that is, gilts, treasuries, etc — are still (government) "money". And it is on the same scale as bank-credit "money".
The key is to make sure banks are lending only for productive purposes. Make them hold the loans they originate until paid (forces good underwriting) and don't allow financial collateral (leverage).
Done correctly, the public unit of account, the tax-credit, organizes public goods; government licensed lending organizes private production. The problem w the latter arises when it is not regulated intelligently (the problem now); the lending function itself is important and beneficial if regulated correctly.

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REPLY

Steve Cameron
SEPTEMBER 27, 2021 AT 7:38 PM

"So how is money actually created?

In the majority of the world — and particularly the OECD – about 97% of all money is created through digital loans by commercial banks. They do this by entering numbers into a computer when someone takes out a loan. So for example, if I go take a personal loan for $1000 from a commercial bank, the bank records the $1000 as a liability for me and as an asset for the bank. This means that our money is created as debt bearing interest."

Isn't it the other way around? I have the asset (a credit 'loaned' to my account, that I can use to buy things with) and the bank has the liability (a debit to its account). I do have a 'legal liability' that I have signed a contract to repay the bank with interest over a specified time period. If I don't repay the loan, the bank makes less profit, as the liability it created for itself (to balance the asset it created for me) negates some of its shareholders assets. If I do repay the loan that cancels the debit is created for itself, and the profit is the interest I paid.

If this way of looking at it is correct, the bank goes broke if it has too many loans that aren't repaid. This is "creating money from thin air" but there is confusion (including mine) as to how that happens.

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REPLY

Blair Fix

SEPTEMBER 28, 2021 AT 12:47 PM

Hi Steve,

Thanks for the comment. First let me say that I am not an expert on accounting, so the 'proper' terminology for the various accounting entries eludes me.

But as I understand money creation it is very simple. Yes, money is created out of nothing by banks. But the trick is to use double-entry book-keeping to make it look like nothing happens. Forget about money for a second and just think pure numbers.

Here's a true statement.

5 – 5 = 0

Now I give you the '5' and keep the '-5'. The net is still 0, but you can 'spend' the 5 now and pay me back later. The catch is that I charge you interest, which is not covered by the 5 I gave you. That means you depend on someone else borrowing numbers to finance your interest.

Yes, the interest earned on loans is where banks make some of their profit. However, my understanding is that banks make most of their money from fees, not interest on loans. But I could be wrong.

At any rate, the fact that money seems 'real' is the main point of confusion. It's really just a pure number and so subject only to mathematics.

Hope that helps.

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REPLY

Steve Cameron

SEPTEMBER 30, 2021 AT 8:46 PM

Hi Blair, that makes it clearer, but the story is incomplete still; what happens to the -5? My understanding is that in double-entry book keeping entries are never deleted, so if I never repay the 5 loaned its balancing -5 'represents' a net loss to the bank. This could only work with government oversight obviously.

I have puzzled over this for years, surely money cannot be created out of thin air, but maybe it can within limits. The other explanation, of people loaning money from one bank to buy something and that payment being deposited in another bank to be loaned out, repeated over and over (but shrinking each time), still stands of course, but that is not ‘magical’.

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Blair Fix

OCTOBER 1, 2021 AT 8:05 AM

Hi Steve,

Have you read David Graeber’s *Debt: The first 5000 years*? It helped me work through these issues.

Basically, Graeber argues that debt (hence, money) is a ‘quantified obligation’. Like any obligation, it can be followed through (repayed). Or it can be ignored (not repayed).

When debt to a bank is not repayed (the -5 in my example), the liability gets moved around to various debt collectors. In the end, if the debtor doesn’t pay, the debt is simply wiped from the books. It’s as simple as erasing a number from a chalk board. The ‘quantified obligation’ disappears.

With debt, the bank doesn’t lose the principle, since it created that out of nothing. (Yes, really out of nothing.) When debtors default, the bank loses the interest it would have accrued.

I think James is right that other authors go into far more detail than me. I’m personally interested in the social relations that debt embodies, not the fine accounting structure that modern banks use.

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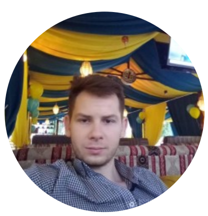

James Harris

OCTOBER 1, 2021 AT 7:21 AM

Steve is right to question this. If you want to learn more about it, I highly recommend Perry Merhling’s MOOC on Coursera called “Money and Banking”.

Its 3 months long and well worth it, but you can get the basics within the first 2 weeks. Teaches you how money is created on balance sheets, but also about the “hierarchy of money” which I plan to put a CASP spin on.

Anyway, so what happens is a swap of IOUs. The bank creates a deposit account on its liabilities side at 0 interest. That deposit account is your asset, you can withdraw cash at any time which the bank is liable for. The bank also creates a long-term loan at interest as an asset for itself and liability for you. so it looks like:

You Bank
Assets / Liabilities Assets / Liabilities
Deposit / Loan Loan / Deposit

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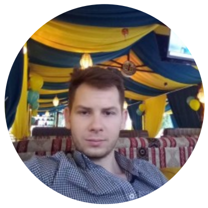

James Harris

OCTOBER 1, 2021 AT 7:36 AM

Last comment didn't format the balance sheets correctly. I'll do them sideways since I can't tab over.

You:
Assets = demand deposit
Liablities = loan

Bank
Assets = loan
Liabilities = demand deposit

While the two are bear an equal principal, its the interest rate difference that makes it profitable.

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Steve Cameron

OCTOBER 1, 2021 AT 9:19 PM

Blair, the thing that is still mysterious is that there appears to be no downside risk for the bank, they cannot loose money, just make less of it (interest) if they have loans that aren't repaid. If so this is truly money growing on trees.

James the balance sheet explanation is of course relevant but I find it hard to understand, I think of debits and credits to accounts held by different parties.

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Blair Fix

OCTOBER 2, 2021 AT 7:31 AM

Steve, I think you are correct that banks cannot lose money from loans … at least not directly. Where they can lose money (even go bankrupt) is when banks are the debtors. That happens with savings accounts, where the bank credits you with money and keeps the debt on its side. Since banks never keep the cash on hand, they can go bankrupt if too many people request their money.

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Stephen Cameron

SEPTEMBER 27, 2021 AT 8:23 PM

To clarify my last comment, in an electronic ledger the bank creates a matching debit and credit that cancel each other out, in its *own* account. It moves the credit across into my account, net effect is that my balance goes up, the banks balance goes down. I now have an asset that I can withdraw, as cash, but a liability to repay the loan.

The bank's account contains the shareholders funds as credits, so it starts out in positive balance, It gets added debits as loans are made, added credits as loans are repaid (with interest), and the bank makes a profit if the balance of this account increases over time.

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REPLY

Blair Fix

SEPTEMBER 29, 2021 AT 11:25 AM

That sounds accurate to me.

Loading...

REPLY

cactusneedle

OCTOBER 1, 2021 AT 9:00 AM

This article is really shocking about how the minority uses power and manipulation to control the people.
This article reminds me of the book "A Forest Journey" its basically about the history of deforestation since the formation of the very first city.
It talks about how almost all the wars in history have been about control and domination of forests for wood resources and how the USA was formed as well as England and the Roman Empire as well as their downfall trough abundannce and lack of wood.

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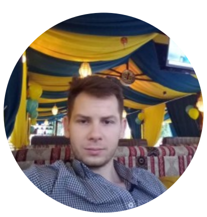
REPLY



James Harris

OCTOBER 1, 2021 AT 11:38 AM

I feel there may be an issue with the theory of sabotage the similar to the issues with anti-trust law you've covered.

To describe sabotage as a situation where "human creativity, cooperation, mutual aid and well-being are all held ransom for the profit and power of dominant owners." Implies a hypothetical alternative where human creativity, cooperation, and mutal aid magically flourish once profit is removed. This is a foundational concept to CASP but relies on comparisons to an imaginary society, just like how Anti-Trust cases rely on an imaginary situation of perfect competition to compare to Monopoly.

Do you know if anyone else has spelled out the concept more?

Its also quite old and focused on the potential of industrial production. Yes we could just have the factories running 24/7, but you'd be sabotaging the environment.

I can easily see the capitalist rebuttle discuss the amount of cooperation and creativity done for the sake of profit outweighs cooperation or creation done for its own sake.

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REPLY

Blair Fix

OCTOBER 1, 2021 AT 1:39 PM

I have an uneasy relation with 'sabotage'. On the one hand it is easy to point to corporate practices that are nefarious. On the other hand, it is difficult for me to conceive of something called 'industry' that is separate from 'business'.

What, for instance, would the 2 million Walmart employees be doing if Walmart did not exist? Clearly something very different. So the existence of business shapes societies such that we can't be sure what would exist in its stead. That's why you'll notice that in my writing, the distinction between industry and business never comes up. I don't find it particularly useful.

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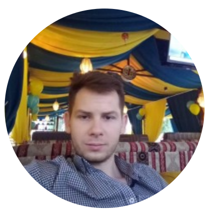
REPLY



James Harris

OCTOBER 3, 2021 AT 3:32 PM

I'm suprised, and really relieved to hear you say this. I've always found your writing to be more level headed and straight forward than the sometimes overly philosophical writing of Nitzan and Bichler.

Loading...

Steve Cameron

OCTOBER 1, 2021 AT 8:25 PM

Hi James, thank for your comments to this discussion. I believe there is an real "alternative where human creativity, cooperation, and mutual aid magically flourish once profit is removed" – it is the worker cooperative! This form of organisation can, it so chooses to, prioritise 'principles before profit'.

No need for magic, there are seven cooperative principles that the movement tries to follow: 1. Open and Voluntary Membership. 2. Democratic Member Control. 3. Members' Economic Participation. 4. Autonomy and Independence. 5. Education, Training, and Information. 6.Cooperation Among Cooperatives. 7. Concern for Community.

In terms of power relationships, most enterprises need 1. workers, 2. managers and 3. financial capital (to buy equipment etc). Power comes from owning the business, the owner makes the key decisions and gets the profits. The owner can be one (or a combination) of the workers, the managers or the capital providers (capitalists). By far the most dominant form is the third, shareholders owning public or private companies, employing managers to run them, and the managers employing workers to do the actual work. Small family businesses are often owned by managers and get capital from savings or banks. The form that is very uncommon is the workers owning the organisation, employing or delegating managers and getting capital from savings, banks or even silent shareholders (owning less than 50%).

Blair has looked at how managers gain a form of power other than ownership that they create through a management hierarchy [often with the promise of ownership through share options, or their alignment with the owners through bonuses dependent on profit].

As a rebuttal to the capitalists, take a look at the Mondragon Cooperatives in the Basque region of Spain, very successful and achieved, much so, via Principle 6 Cooperation Among Cooperatives. My question is why is this form of power relationship so rare?

The common explanation is that financial capital is a limited resource and capitalists take risks in investing their scarce capital into companies (so a 'healthy' 'growing' economy is created by low tax rates on profits). But if capital doesn't need to come from capitalists but instead from banks that can create it out of thin air, maybe there is more to the story than is commonly understood.

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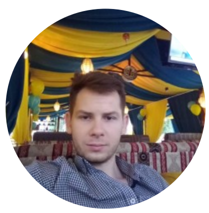
REPLY



James Harris

OCTOBER 3, 2021 AT 3:55 PM

I've very familiar with coops, having endorsed cooperativism for over a decade.

Various issues still arise though. According to the perspective borrowed from Veblen, even a cooperative needs to "sabotage" production in order to pay its workers. Even if OPEC was worker owned, it would still have caused an oil shortage and inflation in the west.

Why are cooperatives so rare you asked? I can give an answer, and its one that has shaken my faith in coops. Cooperativists like myself have often praised the system for being more egalitarian, democratic, better for employment rates, and stable, having a much smaller rate of failure compared to traditional enterprises. So if it fails less, why isnt it more common? Because when corporations succeed they succeed big. They are volatile, unstable, but the few that survive end up thriving (often at the expense of others).

I recived my answer while studying finance. You can have a nice stable, recession-proof portfolio of bonds, but you're going to make way less than the market average. 10% average return is going to beat out 3% stable ROI over time. Coops might make the average, but they rarely beat it.

Thats the "non-political" answer at least. There are definitely political and organizational reasons for them not being more common as well.

Also Mondragon, while large, hasn't been the most ideal coop since the 1980s. They have many non-owner workers, especially out in eastern europe.

Banks also don't create money out of "thin air". Credit comes from credibility, it depends quite a bit on the recipient. Balance sheets also have limited space which banks frequently try to economize. I know its a common phrase, but we really need to remove it from our mindset because its all too common in our individualistic society to treat social relations as not real, air, or “spooks”.

I get that your point is that society need not be profit-driven, but sabotage doesn’t have to be profit-driven either. Sabotage is a very broad concept, perhaps too broad which is why both Blair and I have had uneasy feelings about it.

I hope you found my hypothesis for why coops aren’t as common interesting.

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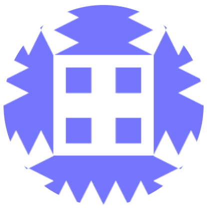

Steve Cameron

OCTOBER 3, 2021 AT 10:01 PM

James I think that the problems faced by cooperatives that seek to compete within a largely capitalist system are good subject for another blog post. I think its far more complicated than we can go over here. For example, with the cost of financial capital being historically very low, and the leverage of the capitalists low as a result, why aren’t more coops starting?

However, the bankruptcy of the largest Montragon cooperative ‘Fagor’ can be attributed to a need to compete with cheaper goods coming mainly from China, as well as the GFC. The promotion of free trade as an inherently good thing (and for the most part the consumers of cheap goods agreeing) is another form of sabotage – its sabotage by arbitrage.

I regards banks ‘making money from thin air’ see my other comment about the apparent lack of down-side risk faced by banks if a borrower doesn’t repay. If banks are lending out money that comes from depositors then there is definitely a downside risk if its not repayed, that they then have to repay from their own money. But if the money lent is just credit created electronically, as we have discussed, there seems no such downside risk.

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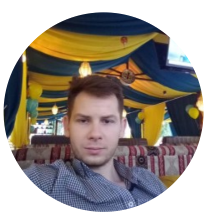

James Harris

OCTOBER 4, 2021 AT 4:47 AM

Hi again Steve, thanks for the reply. I’d like to clarify the stuff about banking.

“I regards banks ‘making money from thin air’ see my other comment about the apparent lack of down-side risk faced by banks if a borrower doesn’t repay. If banks are lending out money that comes from depositors then there is definitely a downside risk if its not repayed, that they then have to repay from their own money. But if the money lent is just credit created electronically, as we have discussed, there seems no such downside risk.”

I’m sorry I missed your earlier comment on risk. At first I wrote a reply detailing all the different kinds of risks that happen when a mortgage is made and rehypothecated but I’ll spare you that.

What is the downside risk of a mortgage defaulting? Well the bank has to devalue its asset which risks its own ability to gain loans from other banks. Thats one risk. Another is that your bank has likely already used it for leverage so not paying the bank means they might not be able to pay either. So if leverage has risk why do it at all? Well dying to leverage is risky, but dying to the competition is certain without it.

So you didn't pay and now your bank has to pay its own loans but doesnt have funding available for it. Your bank also can't get a short term loan either because it had to devalue its assets. Que the financial crisis.

Let me know if you want to answers to anything else about the mysteries of banking and money.

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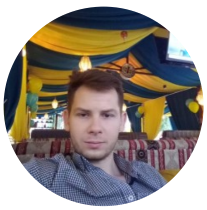

James Harris

OCTOBER 1, 2021 AT 11:55 AM

I've known about Tim's books for some time and I've seen his presentations but this is the first time reading him at length. I was really impressed on how he folded the US constitution into CASP theory. Very well done.

Veblen's theory on the origin of property in marriage was refused about 100 years ago in the League of Nations when they were debating a ban on dowry as a kind of slavery. Tim references Graeber's "Debt" which mentions how anthropologists difused the debate by showing you can buy and sell a cow, but you can't sell a wife. They aren't property.

I know money is supposed to be Tim's specialty within those working on CASP but I wasn't impressed with his work here. Bank's money creation may not be able to be considered a form of sabotage because there is nothing (yet) to exclude. There's no pile of money they are blocking you from. You co-create money when you get a loan from the bank.

Additionally everyone can create money, the trick is getting it accepted. Its very common for businesses these days to make various forms of near-money such as gift cards, loyalty programs, and coupons (I'm writing an article on how retailers are banks too). Early bank deposits weren't accepted by other banks the same way an amazon gift card isn't accepted for payment at walmart. 50 years ago, Ireland had a series of bank strikes lasting 6 months long and people wrote and cleared checks with eachother.

Banks aren't stopping you from making a list of favors your neighbors and friends owe you, its just that anyone outside of that small circle wont care for your funny money. Banks are a level up and offer money accepted by a broader circle containing you, your friends, and various businesses.

To elaborate a little more though, its very possible that if you run your own business and distribut product to retailers, retailers will also accept coupons that you put out. So its possible to get businesses to accept your funny money too. Banks don't stop any of this, at times they encourage it. The main source of Air Miles rewards come from credit card companies instead of airlines. Credit card companies are the major reason why and Air Mile isn't equal to a mile anymore.

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REPLY

In Search of Sabotage – Economics from the Top Down

MARCH 11, 2022 AT 9:40 AM

[…] more details about the evolution of the term 'sabotage', see Tim Di Muzio's discussion in 'Di Muzio on Sabotage', and in his book The Tragedy of Human […]

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REPLY

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