

Democratic Money: The Case for a Decentralized Monetary System
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Chapter Five: The Case for Multiple Currencies

The pinnacle of power today is the power to issue money. If that power can be democratized and focused in a direction which gives social and ecological concerns top priority, then there may yet be hope for saving the world.

— Thomas H. Greco

My goal for monetary reform is to construct an interest-free exchange system that can complement the ideal conditions of a decentralized market economy by:

- 1) Supporting small local and regional businesses;
- 2) Maintaining the medium's integrity by ensuring it is administered within the context of its use;
- 3) Providing a means of democratic participation in local money matters, giving a community some measure of economic self-determination;
- 4) Protecting future productive capacity by keeping investment capital local or regional;
- 5) Ensuring that community savings are invested in the creation of productive capital.

I do not believe that a centralized currency, federally administered, would be able to meet these five conditions, throughout our diverse national economy. The Federal Reserve, by virtue of its size and structure, does not have the administrative flexibility to achieve optimal performance. For an exchange technology to provide accurate feedback, its creation and management should be tied to the context in which it will be used.

I contend that it is impossible to achieve optimal performance from a single centrally controlled currency. Instead, an interest-free monetary system designed to include multiple, complementary exchange media could ensure the administrative flexibility that would enable this technology to respond to the diverse and changing needs of our population. In such a system each medium would be 1) tailored to facilitate a certain level of economic activity, be it international, national, regional, or local; 2) designed to complement the specific needs of its designated economy; and 3) administered at a level that enables it to respond appropriately to changing conditions within its economy.

The idea of using alternative exchange systems to complement a national currency is not new. From the stamp scrip experiments initiated in Germany during the Great Depression, to the growing local currency movement in the U.S. and Canada, there is a wealth of empirical models to learn from. This chapter is dedicated to looking at the strengths and weaknesses of the more successful models, and how they might be modified and used in a decentralized, interest-free monetary system.

Ideal Money Circuit: Mutual Credit Systems

As money circulates through the economy it flows in a circular fashion; it is created, circulated, and then extinguished. In the conventional system, money is issued by a bank in the form of a loan, and then injected into the economy when the borrower uses it to make a purchase. The money then circulates, passing from hand to hand, until the initial borrower is able to earn enough money to pay back the loan. Once the loan is paid, the amount of money issued by the principle is extinguished.

Unfortunately, the conventional approach to money creation carries two previously noted problems 1) money is issued as highly disruptive, interest-bearing debt, and 2) the authority to create money is vested in the for-profit banking sector. These problems inhibit the technology from operating as a pure information medium. In an ideal money circuit, the medium should function simply as an *acknowledgment of value received* (AVR) (Greco, 1990). As such there is no reason why a buyer should need bank authorization to acknowledge the value of the goods and services they wish to obtain, nor should they need to pay for this right with interest. Hence, in an ideal system each individual would have the power to issue money at the point of transaction. The circuit would begin when a buyer creates money and issues it to a seller as an AVR. This AVR can be thought of as an I.O.U. the buyer uses to purchase goods and services. The AVR will then pass from hand-to-hand as each recipient uses it to make his or her own purchases. The AVR is extinguished when its initial issuer accepts it from a buyer in payment for goods or services. This means that, in an ideal money circuit, the right to issue carries with it an obligation to redeem the money created by providing the market with goods or services of equal value. Hence, an individual's right to create money should only be limited by their ability to redeem it in the market place.

In the ideal circuit, money is always created interest-free, and in the exact amount needed to meet demand. A mutual credit system – also referred to as a barter network – is the generic term used to describe any organization in which the members have agreed to trade among themselves using trade credits as opposed to the conventional exchange medium.¹ These credits circulate among members in a manner essentially identical to that of the ideal money circuit. Each member is empowered to issue trade credits as an AVR when they purchase goods and services offered by other members. The difference in a mutual credit system is that trade credits act as a standardized AVR, which all members have agreed to accept. These credits may take the form of paper scrip, metal coins, or simply as numbers in an account ledger. Whatever form the credits take, they provide system members with an interest-free alternative to their conventional exchange medium. In the following section I will look at two of the more successful mutual credit models currently in use.

¹ In the United States mutual credit systems have enjoyed relatively little success. This is due mainly to the complex federal tax laws and reporting requirements applied to a “barter” exchange as well as its members. Organizers of the exchange must file an information return which includes among other things: “the name, address, and identification number of each member providing property or services in the exchange; the property or services provided; the amount received for such property or services; the date on which the exchange occurred; and any other information required by IRS Form 1096” (Solomon, 1996). In addition each member must include with their income tax an accounting of their annual income earned from barter. These tax laws tend to deter most would-be LETS groups. As volunteer-run, nonprofit, community organizations, they are unlikely to have the time, resources, or expertise needed to fulfill their reporting requirement. And many potential members are turned-off by the prospect of filling out more tax forms.

Local Employment Trading Systems (LETS)

Although it has received little mainstream media attention, there is a growing international interest in mutual credit exchange systems. Of the various alternatives, the Local Employment and Trading System (or LETS) – previously known as Local Exchange Trading System – has enjoyed the widest popularity. There are an estimated 1,500 LETS programs in operation around the world, with 450 in the United Kingdom, 380 in France, 225 in Germany, and 150 in Australia and New Zealand.² The system was created by Michael Linton in 1983, and was first established in the Comox Valley of British Columbia. As an out-of-work computer programmer, Linton observed that many others were in a similar predicament. They possessed marketable skills but had no market in which to exchange them. The problem was not that his community lacked wealth, but merely the *money* to exchange it. Without an adequate supply of money to facilitate exchange, people will often turn to barter to supplement their needs. Linton, however, understood the limitations of whole barter. LET systems provide a way to overcome this limitation by opening barter exchange to a whole community of workers (Meeker-Lowry, 1996).

Here's how the system works: Matthew, a mechanic, agrees to provide his services to his neighbor Sam, a cook. They negotiate a suitable price for the transaction (say \$100). Sam is now in debt to the system for \$100, which is recorded in his LETS account. Matthew, in turn, has his account credited for the amount of the transaction. Next week, Matthew obtains the services of Carol, a web-site designer, for \$75. His account credit is reduced by \$75, while Carol's account is credited for the amount. The next day, Carol hires Sam to cater a party, and so the system continues.

In this system the unit of exchange, *green dollars*, is issued in a transaction of real wealth. Sam creates green dollars when he contracts to purchase Matthew's skills. The dollars will continue to circulate until Sam provides \$100 worth in services, at which point the credit in his LETS account returns to zero and the green dollars he created are extinguished. In this manner LETS credits conform to the ideal money circuit. A LETS member spends green dollars into circulation (i.e., acknowledges the value of another's service). The green dollars are backed by a member's agreement to provide his/her services at a later date. Green dollars exist only as records in an account book or computer database. All transactions are reported to a central coordinator, and each LETS member receives a monthly account statement along with a directory listing members and the services they provide (Greco, 1994). When Linton started the first LETS in Comox Valley, the program had only six members. Four years later the program could boast of 500 members, including several participating businesses (Meeker-Lowry, 1996).

A case study of Australia presents a major LETS success story. After Great Britain joined the European Union's Common Market, Australia lost its primary export market. Perishable goods bound for Britain had to be destroyed, and the decline in trade had a devastating effect on employment. LETS had already sprung up independently in Australia, and the government had observed the relief they provided to their

² These are the most recent estimates available. There is currently no official worldwide registry for LETS programs, so organizers are never quite sure how many are in operation. I compiled these estimates by comparing the various LETS web-site directories for each country, as well as a number of multi-national regional directories.

communities. In 1992 the Australian government invited Linton to establish a series of LETS throughout the country, and covered the expenses for education, publicity, computer equipment, etc. In their first year of operation, government-sponsored LETS pumped an estimated A\$3 million into Western Australia's economy, with approximately 1500 participating businesses.

The beauty of LETS is that they create a relatively self-adjusting, local exchange system. Because money is created at the point of purchase the amount of money in the system will always equal the value of goods and services exchanged. The value of the green dollar will not decline due to "too many dollars chasing too few goods." Furthermore, because LETS are closed systems, any money they create will remain local to help facilitate future transactions. This makes LETS an ideal economic tool to complement the conventional monetary system. During an economic recession, when federal dollars are scarce, green dollars can mitigate the effects by helping to maintain effective demand. Experience lends credence to this claim: LETS organizers have noted their membership expands during economic recessions.

From an administrative standpoint, a LETS system is entirely local and community oriented. LETS systems are usually run by a community-based nonprofit organization or a member-owned cooperative. Administrative authority is vested in a board of directors, possibly member elected, with clearly defined and limited powers. LETS organizers, who may also be board members, should have the following responsibilities:

- 1) Establish a central record-keeping office where members can report their transactions. This office maintains a record of reported transactions and updates members' accounts accordingly. Periodically these records will be disseminated in a summary report listing each members' transactions over a given period, as well as each account's beginning and ending balance.
- 2) Recruit new members from the community, and process the applications of prospective members. In so doing, maintain a regularly updated membership list.
- 3) Host regularly scheduled membership meetings in order to update members on the organization's status, and enable them to participate in decision-making. These meetings also give members an opportunity to get to know one another, thereby promoting the mutual trust upon which the system is based.
- 4) Ensure members know what goods and services are available within the system. This is accomplished by periodically publishing a LETS newsletter or directory listing the goods and services offered by each member. Such a directory should include a classified section where members can display ads, and post both offers and requests for goods and services.
- 5) Generate enough revenue to cover the program's start-up and operating costs. Some of these will be cash costs, such as phone bills, overhead, and equipment, and will require payment in conventional dollars. These cost are covered by charging an annual membership fee, and/or initiation fee, a portion of which must be paid in conventional money. Other costs, such as record-keeping services, publication costs, and management, are typically covered by LETS credits (Solomon, 1996).

Though requiring considerable oversight, a local LETS is an excellent way for a community of people to supplement its buying power. And given its flexible structure, a

LETS can be tailored to meet the particular needs of its community.

The greatest concern with the LETS model is the risk of members running up an excessive debt balance. A LETS is founded on the basis of mutual trust with each member expected to repay their obligations in good faith. A LET system is not a bank; hence its members have no legal obligation to repay their debts. In the event a member acquires more debt than he can repay, it will fall upon the other LETS members to fulfill his obligations. If a large number of accounts are permitted to remain perpetually negative, it will cause members to lose faith in each other's ability to repay, in which case the system will likely fail. An even more troubling aspect of the debt repayment problem is that it is more likely to occur in a LETS as its membership expands. Many observers attribute this to the changing conditions brought by expansion. Initially LETS begin with a small community of like-minded and idealistic members, with a personal commitment to making the program work. As membership expands the program tends to become less personal and less idealistic, and it's more likely that potential defaulters will join.

Organizers of LETS programs have experimented with a number of methods to prevent this problem. The simplest and most obvious solution is to reduce the risk of abuse by limiting the amount of debt each member may incur and carry. Unfortunately, the application of this solution presents a number of new administrative problems. The LETS organizers are now stuck with the unenviable task of deciding how large a debt balance each member can incur, and how long it can remain unpaid. One option is to set a fixed ceiling per member, say \$500 to \$1000. However, a fixed ceiling may not be appropriate for every member and could limit participation. Some businesses, for example, can legitimately carry larger debt burdens and would hardly find it in their interests to participate (Solomon, 1996). Another option is to limit each member's credit limit to what they can reasonably repay within a two- or three-month period. Another is scheduling a time for the periodic resettlement of outstanding debts. Unfortunately, no matter how a program chooses to enact its credit limit, the restriction reduces the primary benefit of the LETS credit system, that of providing a community with an unlimited means to transact wealth.

An alternative to setting an arbitrary ceiling is to adjust each member's credit limit based on his or her credit history. The central LETS office could perform a credit check on each prospective member before applying an appropriate credit limit. As members develop their LETS credit history, their debt limit can increase. The primary drawbacks of this option are the added expense of performing a background check on each prospective member, plus the additional staff oversight needed to perform the subsequent credit adjustments (Solomon, 1996).

Some LETS programs have opted to avoid setting credit limits and to rely instead on a form of group regulation. Periodically the central office will publish and distribute a list of each member's account balance, trusting on peer pressure to discourage excessive debt balances. It also gives members the opportunity to avoid transactions with perpetual debtors. Debt disclosure seems most effective in the smaller trading communities. However, many are put off by the perceived violation to privacy (Solomon, 1996).

The WIR Network

This mutual credit model is designed to facilitate transactions on a national level. Located in Switzerland, the WIR-Bank is a nationwide, cooperative exchange network,

founded in Zurich in 1934 by supporters of Silvio Gesell's free money theory. The WIR (pronounced *vir* and short for *Wirtschaft*, which means "economy" in German) operates in much the same manner as a LETS program. However, there are a number of notable differences, mainly in size, intent, and membership. LETS are tailored to local economies, catering primarily to a community of individual traders, although local businesses are also welcome. The WIR is designed as a support system for middle-sized businesses competing with stronger and larger corporations. It is primarily an intra-regional or intra-national economic tool. As stated in the network's articles of intent:

The WIR-cooperative is a self-help organization of trade-, industry- and service businesses of the middle class. Its goal is to advance the participants, and through the WIR system to make their purchasing power usable to each other and to keep it in their own ranks, in order to create additional turnover for the participants... (Defila, 1994)

The network is structured like a bank. Its main office is located in Basel and has seven regional offices throughout Switzerland. Like LETS, the WIR is a cashless accounting system administered through a central office. The network's unit of exchange, the WIR, has the same value as the Swiss Franc. Members record their transactions using forms similar to conventional bank checks and credit cards.

In the WIR network "money" is created in the same manner as in the LETS system, when a transaction takes place. The difference is that trading occurs only between businesses, not between individuals. In accordance with free money theory, WIR savings do not accrue interest and debt is charged only a minimal service fee. Cash withdrawals are prohibited, ensuring credits created by the system will remain in the system. In order to connect buyers and sellers, the network publishes a monthly magazine, *WirPlus*, and a tri-annual catalogue displaying the goods and services provided by WIR members. The network's operation costs are covered by a small quarterly fee (8 Swiss Francs in 1990) plus a small service charge, 0.6-0.8% on every transaction (Kennedy, 1995). As of 1999, the network catered to 82,487 firms, facilitating approximately 1.8 billion WIR worth of transactions (Stodder, 2000).

Mutual credit systems are designed to supplement the conventional monetary system, not replace it. Given its almost 60-year history, the WIR Bank provides a wealth of empirical data indicating how the network functions in relation to the general economy. This data was used in a recent study analyzing the potential economic effects of "barter" exchanges, conducted by Dr. James P. Stodder, Clinical Assistant Professor in the Lally School of Management & Technology at Rensselaer Polytechnic Institute. Stodder concluded that the WIR exchange has played a "stabilizing role" in the Swiss economy (Stodder, 2000). After comparing the post-WWII performance of the Swiss economy to that of the WIR Bank, Stodder found that the network functions counter-cyclical to the national economy. During periods of economic boom, the growth of WIR activity has tended to slow. During periods of recession, the growth in network activity accelerated. The same counter-cyclical correlation can be found between WIR activity and general employment levels: as the number of unemployed grows, WIR activity tends to increase.

The implications on this study are quite promising for the future of mutual credit systems. However, Stodder remains noncommittal as to why these systems tend to

complement the general economy. “There remains the vital question, however, as to why this counter-cyclicality occurs. A basic difference of opinion exists within macroeconomic theory as to whether instability is more due to price rigidity, or to inappropriate levels of money and credit” (Stodder, 2000). Do mutual credit systems complement the general economy because they provide greater price flexibility when its needed, or through their ability to create supplementary credit? Given that prices levels in the WIR network tend to mirror those in the general economy, it would seem that the network benefits its members most by providing them with additional credit interest-free.

The Potential of Mutual Credit Systems

The goal of a mutual credit system is to provide its members with an alternative to monopolized bank money by empowering its members to create their own exchange medium in the form of trade credit. The members of a mutual credit system agree to respect each other’s right to issue credit based on their ability to redeem it by providing the system with the equivalent value in goods and/or services. In such a system, a positive credit balance indicates the amount of value a member has delivered to his or her trading community. A negative balance indicates the value a person is obliged to deliver. Models of mutual credit systems, such as the WIR network and LETS programs, have already proven their usefulness as supplementary exchange systems. In their current forms, however, these systems will continue to hold only a supplementary position for two reasons. First, mutual credit programs are designed as cashless exchange systems in which only members can enjoy the benefits of additional credit, and membership is limited to direct providers of goods and services.

Second, and potentially more problematic, a system’s trade units, such as green dollars or WIR, are intended to operate only as a transaction medium, designed to supplement but not replace, the conventional exchange medium. Members must still rely on conventional money to perform the other functions required of money as a communication technology. Furthermore, like any other exchange medium, a mutual credit program is vulnerable to credit stagnation in the form of idle balances. We’ve already noted the problems that can occur in a LETS program that carries a large number of perpetually negative accounts. For a mutual credit system, permitting members to carry a perpetually positive balance, can be equally problematic by reducing the circulation of credits. Trade credits are purely a medium for current transactions; they are designed for spending not saving. When a member attempts to save his or her credits for future consumption, it has the same effect on a mutual credit system as the hoarding of money has on the general economy. It slows the circulation of trade credits, and to an extent, hinders those with debt from fulfilling their obligations to the system.

One solution to this problem is to design a mutual credit program that is a truly complementary system, in that its trade credits are able to function as both a medium of exchange and a store of value. Thomas Greco suggests that a mutual credit system could accomplish this by; 1) limiting the amount of trade credits a member can carry in their general account from one quarter to the next, and 2) providing a means to store any excess credits such as a savings coop (Greco, 1994). This could be implemented by assigning each member both a *current account* and a limited-access *capital account*. The current account would function like the normal mutual credit account, providing a record of each member’s quarterly transactions. Any limits on the amount of debt or credit each

member was allowed to carry would be applied to this account. If at the end of the quarter, a member's credit balance exceeded the limit, the excess credits would be transferred to their capital storage account. Their access to these capital account credits would be limited. For example, the savings coop could require a mandatory savings period of six months to a year before a member could access their capital account, and/or set a time-lag between a withdrawal request and the release of funds. Limited access would compel members to rely mainly on the money-creation power of their current account to fund their current consumption, which would help maintain steady credit circulation (Greco, 1994).

In addition to creating a more functional money system, this method would provide a vital source of capital for investment. One of the basic principles of market theory is that long-term assets or projects should not be funded by the issuance of new money, but instead, should be financed out of savings. The establishment of capital accounts would provide a mutual credit system with its own capital market, from which members could obtain interest-free loans to finance such things as the construction of factories, improvement of land, the purchase of production equipment, or any other long-term asset that should be financed out of savings. In this manner a mutual credit system could observe the market theory condition, that savings be used in the creation of productive capital. Money creation, on the other hand, would be based on the exchange of existing supplies of goods and services, as transacted through current accounts. This would result in a relatively self-regulating money supply, as it is created in tandem with the transaction of current wealth.

Another benefit of this theoretical model is that it manages to reconcile the two conflicting functions of money: first as a medium of exchange, and second as a store of value. By separating credits into current accounts and capital accounts, the system is able to designate which function the credit is intended to perform. In either case, a credit represents a "claim" upon the market. In a current account, a credit is a short-term claim, which the market is obliged to redeem at any time. In a capital account, the credit represents a claim against long-term productive assets (e.g., factories, buildings, machinery, etc.), which will benefit the market in the long run. These claims are satisfied over time, as the asset's value is recovered by its use in the production of future goods and services.

The possible benefits of this model are quite encouraging. However, the challenge remains to design a way to administer a fully complementary mutual credit system. Two very basic problems need to be solved; 1) how the system can be expanded to include an entire community of people, and not just direct providers of goods and services, and 2) what type of organization should be entrusted with the management of the mutual credit capital market.

Local Currencies

Given the legal deterrents to LETS (see footnote 11), communities interested in alternative exchange systems have turned to local currency programs. This is also understandable given U.S. history. In the United States, paper currency wasn't standardized until after the Civil War. Before that, banks would issue their own scrip, which would circulate like paper money. It wasn't until 1935 that the last of the post-

Civil War bank notes were retired from circulation (Solomon, 1996). During the Great Depression there were literally hundreds of alternative currencies issued by a variety of authorities, including state governments, municipalities, barter associations, school districts, chambers of commerce, manufacturers, business associations, even individuals (Greco, 1994). For example in Springfield, Massachusetts, the publisher of the *Springfield Union News*, Samuel Bowles, issued his own scrip, which circulated widely during the 1930s. Bowles began his program by first striking a bargain with local merchants: those who agreed to redeem his scrip in goods and services could use it to pay for advertisements in the *Union*. He then used the scrip to pay employees, who in turn used it to buy goods from participating stores (Block, 1998).

By the end of the 1930s, employment was on the rise due to President Franklin Roosevelt's work programs and arms production for WWII. Local currencies were quickly displaced by the newly resuscitated economy. However, in recent years, the U.S. has seen a resurgence in local currencies. I have been able to identify 26 local currency programs, active in the United States and Canada.³ This may seem insignificant when compared to the number of LETS in existence, but these groups have experimented with a variety of noteworthy innovations.

There are a number of models for local currency programs, but the defining characteristic is the issuance of locally designed scrip, which can only be used to transact business in a designated geographic region (e.g. town, city, county, etc.). The stated goal of these programs is to strengthen local economies by keeping money in the community and under local authority. As stated by community activist, Paul Glover, "When decisions are made by people far away with different priorities, many local economies become vulnerable. Farmers in this economy, for example, have long understood that money moves from rural areas to major money centers – with deadly effect. Local and regional money can revive deflated discarded economies, both rural and urban" (Block, 1998).

Ithaca HOURS

Paul Glover is the originator of the HOURS local currency model, and founder of the original hour-based currency, Ithaca HOURS, located in Ithaca, New York. Ithaca HOURS is based on the labor-hour standard, founded on the premise that human labor is the source of all real wealth. Wealth is created when human skills are applied to raw materials in order to create something with real use value. By this standard, human labor is our most valuable economic asset and as such should be used to back any currency. In a labor-standard system, value is measured in units of labor-hours which, simply translated, means that one unit of value is the equivalent of one hour of labor. The HOURS model is by far the most widely used of the various local currency programs operating in North America. To the best of my knowledge, there are only seven non-HOUR-based programs active.

³ See Appendix A for a directory of active local currency programs in the United States and Canada. Each listing includes the program's contact information, background, and basic stats on currency circulation and participation levels. Information was obtained through personal communication with directors from each program. This local-currency directory can also be found on the E. F. Schumacher Society's web site at <http://www.smallisbeautiful.org>.

When Paul Glover started the program in October 1991, only 90 people and a handful of local businesses had agreed to accept HOURS. Since then Ithaca HOURS has grown into the most successful local currency program in the United States. More than \$95,000 worth in local scrip has been issued to over 2000 participants, facilitating several million dollars worth in transactions. HOURS are accepted by over 480 businesses, and can be used to pay for such various things as rent, groceries, car repair, legal services, childcare, even medical expenses and health insurance. Ithaca HOURS is a freely circulating scrip available for use by members and nonmembers alike. In 1998 the HOUR Advisory Board incorporated as Ithaca HOURS, Inc., and held elections for a new Board of Directors.

One of the program's basic principles is that each person's time is just as valuable as another's, and thus, all labor should be treated with the same dignity. The currency is issued in 4 denominations, all measured in units of time: 1, 1/2, 1/4, 1/8 HOUR (see figure 2). The basic unit, one Ithaca HOUR, is equal to \$10, the approximate average hourly wage (excluding benefits) for workers in Tompkins County. In this manner, the program attempts to act as an economic leveling force, raising the minimum wage and providing low-wage workers with additional spending power. This is not to say that the principle of one Ithaca Hour for one hour of work is not flexible, the program leaves room for negotiation. As Paul Glover explains:

With Ithaca Hours, everyone's honest hour of labor has the same dignity. Still, there are situations where an Hour for an hour doesn't work. For example, a dentist must collect several Hours for each work hour because the dentist and receptionist and assistant are working together, using equipment and materials that they must pay for with dollars. So, a lot of negotiating must take place (Meeker-Lowry, 1996).

The cornerstone of Ithaca HOURS is the annual publication of an HOURS directory listing the individuals and businesses which have agreed to accept HOURS as a portion of the purchase price for their goods or services. Some members accept 25% or 50% payment in HOURS, others will accept HOURS for the entire purchase. To help fund publishing costs, the program charges a listing fee, \$5 for the first 1 or 2 offers, and \$2.50 for each additional offer. A member may post as many listings as they choose, and fees can be paid in dollars, HOURS or some combination of the two. Directory updates



1 HOUR = \$10

½ HOUR = \$5

¼ HOUR = \$2.5

Figure 2: Examples of Ithaca HOUR Scrip⁴

are posted on the Ithaca HOURS web site, and also published in the program's periodic newspaper *HOUR Town*. The newspaper also gives members a chance to run display advertisements, and list offers or requests for goods and services in the paper's classified section.

The issuance of Ithaca Hours is unique among alternative exchange systems. The majority of HOURS are issued on the same basic principle governing LETS issue – credit is created only for members, those able to redeem its value by providing goods and services. However, in the Ithaca HOURS program the issuance of scrip is controlled by fiat through the organization's Circulation Committee, and based uniformly on membership. Here's how the system works. When a member signs on they agree to list an offer in the annual Ithaca HOURS directory, indicating what goods and/or services they will provide in exchange for HOURS. Each new member of Ithaca Hours, Inc. is issued 2 HOURS by mail and becomes eligible to vote in elections, and to apply for HOURS business loans. Membership is renewed yearly, at which point every member

⁴ Bills are shown at approximately ½ size. During the program's 10 years of operation there have been fifteen different series issued. Currency examples can be found online at <http://www.ithacahours.com>. Information includes the issue date for each series, and total volume of bills issued.

who agrees to remain in the program is issued an annual renewal bonus of 2 HOURS. In this way the committee controls the issue of HOURS so that the currency grows gradually as membership increases. They can manipulate the growth rate as needed by increasing or decreasing the amount issued to new members, and/or the size of the annual renewal bonus.

The second major method of issuance is through HOURS loans, ranging from \$100 up to \$30,000 in value. In 2000, the largest HOURS loan ever made (\$30,000) was given to the Alternatives Federal Credit Union/CUSO, to cover 5% of contract work on construction of the union's new headquarters. The loan is interest-free and scheduled to be repaid over 10 years. According to Bill Myers, manager of the credit union, the HOURS were spent for plumbing, carpentry, electric work, and a wide range of other services provided by local contractors (Glover, 2000).

And finally, a significant percentage of Ithaca HOURS are issued through the organization's granting policy; at least 10% of the total volume of HOURS issued are given as grants to local non-profit organizations. To date, 62 local groups have received HOURS grants, totaling over \$10,000.

Ithaca HOURS have supplied a substantial economic benefit to commerce within the area. The program has issued \$95,000 in debt-free scrip directly into the local supply of transaction money. The majority of this money (that not issued through HOURS loans) will continue to circulate in the local economy, with an endless multiplier. Since HOURS can only be used locally, they also create a guaranteed demand for local products. But, of all the program's benefits, the one I find most promising is the potential for local economic planning and organization. Not only does Ithaca HOURS provide a source for interest-free local financing, but it also creates an organization whose membership is comprised of local businesses, non-profit groups, professionals, and community members. People with the skills and incentive needed to plan and carry out projects designed to meet community needs.

A good example of this is the recent creation of the Ithaca Health Fund, a nonprofit, locally-controlled health financing fund. After conducting a random survey of 125 Ithacans, organizers found that 36% were uninsured, and 98% did not have dental insurance. Many of the insured respondents indicated that their preferred providers and therapies were not covered under their existing plan. The Fund's stated goal is twofold, "to make preventive and innovative health care more affordable, and to recapture health insurance premiums for local health purposes (Glover, 2001)." The Fund is managed by a member-elected board of directors, representing a variety of health sectors.

The Fund provides compensation through two forms. First, members are entitled to discounts on services and goods emphasizing preventive care, offered by 115 participating health providers. The providers are required to offer Fund members a minimum discount of 10%, and all accept Ithaca HOURS. Fund providers include conventional physicians, dentists, psychiatrists, herbalists, chiropractors, nutritionalists, etc. Second, members are entitled to payments from the Fund for stipulated health problems, including diagnostic exams, preventative and emergency care. Payments are made worldwide with any credentialed health provider, and there is no deductible. Membership fees are annual and applied as follows; \$100/year for adults, \$75/year for a spouse/partner, and \$50/year for a child. In just its first year the Fund has accumulated over \$95,000 in reserves (Glover, 2001).

The Ithaca HOURS model has a number of advantages over mutual credit systems. For one, use of an hour-based local currency is not limited to members, but can be utilized by everyone in the community. Instead of serving only direct providers of goods and services, a local currency will benefit wage labor as well. However, there is a drawback to this openness. Without a closed system, it is impossible to institute an ideal money circuit because there is no way to prohibit money from being either hoarded, or flowing outside of the system to be used by non-members. If this happened in a mutual credit system, it would become increasingly difficult for debtors to regain the credits required to balance their accounts. Consequently, in the Ithaca HOURS model the power to create money is vested in the Circulation Committee, not members. Instead of being issued tandem to the exchange of real wealth, an hour-base currency is issued by fiat, making it a step removed from its actual use in transactions. This also means the system has no self-regulating way of controlling the money supply. Currently there is no reason to believe the Circulation Committee lacks the responsiveness or flexibility to manage a local currency. However, the issuance of a perpetually circulating, fiat currency could prove much more difficult to manage on a larger scale.

Toronto Dollar

The Toronto Dollar project is one of the few non-hour-based local currency programs in operation. The program is run by the Toronto Dollar Community Projects Inc., a non-profit organization established in Toronto, Ontario by St. Lawrence Works, a coalition of local businesses and cultural groups interested in sponsoring community initiatives. The organization's stated goal is to "improve the social and economic health of communities in the City of Toronto by undertaking projects that benefit these communities, including the sponsoring of barter networks and local currencies." (Toronto Dollar web site) After more than a year of preparation, the currency was launched on December 5, 1998 in the St. Lawrence Market, by the mayor of Toronto, Mel Lastman.

The Toronto Dollar program is unique in its method of issuance. Here's how it works: the currency is issued when consumers exchange their Canadian dollars for an equal amount of Toronto Dollars. For each Toronto Dollar purchased, Toronto Dollar Inc deposits 90 cents into the program's reserve fund, and 10 cents into the Toronto Dollar Community Projects Fund. Approximately 250 businesses have agreed to accept Toronto Dollars on par with Canadian dollars. A business can either continue to spend their Toronto Dollars at other participating stores, or redeem them for Canadian currency at 90 cents on the dollar. Money for these redemptions is drawn from the reserve fund.

Toronto Dollars help the local economy by keeping money working and circulating locally. But its most distinguishing feature is the Community Projects Fund and its "10% solution". The Fund receives 10% of the proceeds obtained when consumers exchange Canadian Dollars for Toronto Dollars. This money is then used to support the work of community-based non-profit organizations. In its first two years of operation the Toronto Dollar Community Projects Fund was able to donate \$25,000 to 22 local agencies and community groups.

What makes the Toronto Dollar design so promising is that it provides a community with the means of financing the good works of community non-profits, while maintaining local spending power. The program ensures that 10% of the value on all transactions made in Toronto Dollars will be funneled into community building projects.

In essence, the program has created a local exchange medium specifically designed to further community goals which are under funded by the conventional economy.



Dollar

\$1 Toronto



Dollars

\$5 Toronto

Dollars

\$10 Toronto



Dollars

\$20 Toronto

Figure 3: Examples of Toronto Dollar Scrip⁵

Investment and Banking with an Interest-Free Medium

In my research on local currencies, I've discovered that one of the greatest advantages a program can have is the support of the local banking industry. Not only does bank support provide its sponsors with helpful input and expertise, but it also increases a program's legitimacy within the community. Hence, I believe any attempt to introduce an interest-free currency – be it local, regional, or national – should also include the development of new banking techniques that will complement and legitimize the new medium.

In the next section we will look at one particular model for interest-free banking that has already proven successful; the JAK Medlemsbank in Sweden. Its banking methods can provide an outline for future experiments.

J.A.K. Cooperative Banks

JAK Medlemsbank ("Members' Bank" in English) in Sweden is a non-religious, politically neutral (i.e. no party affiliations), interest-free, savings-and-loan co-operative bank. Savings deposits receive no interest and loans are charged only a small administrative fee, which corresponds to an interest rate of 1.7% to 4.4%, depending on the loan. Established in 1965 as a co-operative savings-and-loans association, JAK was granted official bank status by the Swedish government in December 1997. With that status, members' savings are insured under the Swedish banking system's deposit guarantees. Currently, JAK boasts over 21,000 members nationwide, served through 24 regional offices located throughout Sweden (JAK Medlemsbank, 2001).

The initials J.A.K. stand for Jord, Arbete, and Kapital (Land, Labor, and Capital), a farm movement which started in Denmark during the 1930s (Kennedy, 1995). At that time, most Danish farmers suffered heavily from debt. Even though their farms were productive they lived under the constant threat of foreclosure. The farmers (influenced

⁵ Bills are shown at approximately ½ size. Examples of scrip can be found on the Toronto Dollar web site, <http://www.web.net/~tordoll> (See also Appendix on Local Currencies).

by Silvio Gesell's Free Economy movement) realized that an interest-free money system could make their farms profitable again. Working in co-operation with sympathizers in the trading and manufacturing sectors, the JAK movement established its own interest-free currency and banking system. Fearful that its authority was being threatened, the Danish government prohibited the use of JAK currency in 1933, and forced its initial savings-and-loans system to liquidate in 1938 (Hofford, 1998).

Today, the design of JAK Medlemsbank in Sweden is basically similar to its 1930s predecessor.⁶ It operates on the principle that interest is inimical to a healthy economy. JAK's ultimate goal is the elimination of interest as an economic instrument, and it works on two fronts to obtain this end. The first is ideological, the bank endeavors to disseminate information on the harmful effects interest has on economic and social stability, and environmental health, while presenting possible alternatives. The second is the practical example provided by JAK itself, which demonstrates the feasibility of interest-free banking.

JAK is a co-operative bank, each member is also a joint-owner and required by law to contribute to the bank's equity. Each member must pay a non-refundable contribution of 200 Swedish Crowns (SEK), as a basic stake in the enterprise. This, along with an annual membership fee, entitles a member to use JAK's unique savings-and-loans system.

In JAK, one's savings do not earn interest, but instead accrue *savings points*, required in order to obtain a JAK loan. The size of a loan is dependent on three factors: 1) how soon the loan can be repaid (i.e. the size of monthly payments), 2) how much money is available in the savings pool, and 3) the member's savings performance, determined by their savings points. A member's savings points are calculated by multiplying their average balance by the number of savings months. This number is then multiplied by the *Savings Factor* (S), which reflects the quotient of loans divided by deposits and is set each month by the JAK board (Hofford, 1998). For example, assume a member saves 1,000 SEK over 6 months with an S of 0.9. At the end of the saving period they would have 5,400 savings points ($1,000 \times 6 \times 0.9 = 5,400$) (Hofford, 1998).

A member is required to save for a minimum of six months before they are eligible for a JAK loan. Most members save for at least 1 to 2 years before seeking a loan. The JAK bank offers two types of loans, the Basic Loan and the Basic Loan plus the Add-On loan. The Basic Loan is determined by the applicant's number of savings points, and how quickly they are able to pay off the loan. Larger payments will entitle one to a larger loan, and vice versa.

A Basic Loan is usually relatively small, so many members opt for the Basic Loan plus the additional Add-On loan. The size of the Add-on loan is determined by the *distribution number* (D), which the board sets monthly in relation to how much money is currently in the common pool. D can vary between 0 and 19, but usually falls between 3 and 6. The Add-On loan is calculated by multiplying the amount of the Basic Loan by D. To illustrate, assume an applicant is entitled to a Basic Loan of 20,000 SEK and D is 4. The applicant would be eligible for an additional 80,000 SEK, for a total loan of 100,000.

⁶ Denmark is also host to a JAK banking system. The modern JAK in Denmark takes the form of small independent local savings-and-loan associations, rather than JAK in Sweden's centralized banking model. Both systems operate using the national currency. To my knowledge the neither program has made an attempt to reintroduce the issuance of interest-free money.

However, if a member obtains an Add-On Loan, they must continue to save regularly during the repayment period in order to maintain the bank's balance between savings and loans. So in addition to quarterly loan payments, a borrower is required to deposit a fixed amount in a blocked, post-savings account. The borrower is obliged to continue with post-savings up to the total amount of the Add-On Loan. As a result by the time the loan is paid off, the member will not only be debt free, but will have an extra 80,000 SEK in post-savings, which become available for withdrawal 3 months after the last installment.

JAK offers its members three different types of accounts. The first and most convenient is the Open or Current Account. Under normal conditions, there are no restrictions placed on deposits or withdrawals from a Current Account. However, the Savings Factor applied to them is much lower. The next two are both long-term savings accounts: 1) The Goal Account, and 2) the M-24 Account. The Goal Account is designed for regular savings and requires monthly deposits of a predetermined amount. The maturity period is at least two years, and withdrawals require a minimum of six months advanced notice before the release of funds. The M-24 Account, on the other hand, is designed for one-time deposits. The maturity period is also two years, but withdrawals require two years advanced notice. To counter the inconvenience of long advanced notice requirements, both long-term accounts are accessed with a higher Savings Factor.

In accordance with their ideological work, one of the services JAK readily provides is loan refinancing. Members burdened with high interests loans are able to pay them off with a low-cost JAK loan. Dana Hofford, a former member of JAK's board of directors, illustrates the benefits in this real life example:

In 1989, a man had taken a second loan of 22,000 SEK at variable interest on his cottage with a repayment time of 30 years. It was supposed to be an annuity loan with an amortization of 705 SEK quarterly. In the four years he had the loan, however, he paid 13,476 SEK (~800 SEK per quarter) yet the debt had reduced by only 300 SEK: 98% of the payments had gone to interest! Due to high interest rate, he was often paying only interest with no amortization at all (Hofford, 1998).

By 1993, having already paid 13,176 SEK in interest on a 22,000 SEK loan, the gentleman was still 21,700 SEK in debt, and the debt was compounding rapidly. He approached JAK for a refinancing loan. At that time he'd been a member for around 18 months and maintained an average balance of 5,030 SEK in his account. He was able to obtain a 12-year loan of 24,636 SEK on the collateral of two personal guarantors. The principal of the loan was 22,000 SEK and assessed with a 2,636 SEK loan fee. With the JAK loan he was able to repay the variable interest loan. Since then, each quarter he pays the bank 1001 SEK, of which 513 SEK goes to debt repayment, and 488 SEK is deposited in his post-savings account. By 2005 he will be debt free while having saved an additional 23,424 SEK (Hofford, 1998).

Despite the success of JAK, the model does carry some significant disadvantages. Perhaps one of the primary drawbacks is the bank's limited commercial appeal; 90% of its members apply for mortgage loans. For businesses, a major deterrent is the long savings requirement. Most entrepreneurs are unwilling or unable to wait 1-2 years before

receiving capital financing. JAK is currently looking into a number of ways to overcome this deficiency. Previously, the bank had facilitated cooperative lending schemes among members using its so-called *C-loan*. With the C-loan a member, or group of members, can sponsor a project financially without having to risk their own funds, or deal with the bother of oversight. The investors simply deposit their funds in a blocked account, from which the C-loan recipient may borrow. JAK takes care of all administrative details, and investors are given partial access to their funds after one-half of the repayment time has passed (Hofford, 1998).

Recently, this financing method was expanded through a new scheme, subsidiary Local Enterprise Banks. One of its primary aims is to counter the growing disinvestment in Sweden's rural communities. As in other Western nations, Sweden has felt the pressure to globalize. Membership in the European Union (EU) has required the country to liberalize its banking laws in line with EU standards. Following deregulation, established banks tend to channel the savings from rural regions into urban centers and abroad, where average returns on investments are higher. As a result local businesses are finding it harder to obtain affordable finance capital. Local Enterprise Banks are an attempt to fill in this gap (JAK Medlemsbank, 2001).

Here's how the program works: If a local investment group has been unable to obtain funds from an established bank, they can open a Local Enterprise Bank (LEB) account with JAK Medlemsbank. Investors deposit their savings into the LEB account, which then is used as a savings base to finance the local project. JAK takes care of all administrative oversight, and the funds are covered by national bank deposit insurance.

For the future, JAK is looking into other non-interest investment schemes, such as profit-loss sharing loans. Taking their cue from Silvio Gesell's theory, JAK argues that normal commercial loans are unfair because money does not deteriorate over time (Hofford, 1998). On the contrary, the use of compound interest makes it grow. By demanding a fixed profit on their investment, the lender will have a constant advantage over the entrepreneur, whose projects are never 100% predictable. Not only is this unfair, but it ensures finance will continue to dominate the productive sectors.

In a profit-loss sharing scheme, JAK and a prospective entrepreneur would contract to split any profits earned by the enterprise. If the business fails, both parties lose; the entrepreneur his labor and expertise, the bank its loan. This is a far more equitable solution, as it takes into account any unforeseen problems. The profit-loss model is widely used throughout the Muslim world, where interest is forbidden on religious grounds. JAK is currently still in the process of developing this loan instrument (Hofford, 1998).

In addition to its commercial shortcomings, JAK members have identified two other disadvantages in the system. First, the pre-savings requirement can exclude those who have no possibility of saving and are in need of credit the most. One possible solution is to introduce a new lending instrument, a type of refinancing loan that can be granted to those without pre-savings. One complication with this solution: JAK would need to require a higher total savings performance from the rest of its members in order to accumulate the additional funds needed to back such loans (Hofford, 1998).

Second, JAK's collateral requirements tend to exclude those with lower-incomes who have no assets and can't find personal guarantors. The proposed solution is to introduce a loan insurance program to be used in those cases where the proper collateral

is not available. In this program each borrower would pay an insurance premium which would build up funds as a buffer to any credit losses over time (Hofford, 1998).

Refinements for Use in Further Experimentation

At the beginning of this chapter, I proposed five conditions for an ideal interest-free exchange system. I contend that these conditions are best met by exchange systems that operate on a local or regional level. In each of the local systems reviewed in this chapter, there are weaknesses relative to that ideal which leave opportunities for improvement. Successive models have eliminated some of the problems. Others remain.

In the next section I will outline my proposal for a hybrid system that incorporates characteristics from several different models in order to overcome the “internal” impediments, specific to each system. External issues such as government approval, taxation, enrolling wide-spread participation, etc., will require further consideration.

The proposed system would operate on a local or regional level, and be able to perform both as a medium of exchange and as a store of value, using the mutual credit current-versus-capital account scheme mentioned earlier. This proposal borrows heavily from the mutual credit model, with a few pertinent modifications: oversight of the system will be vested in an elected governing board (similar to the Ithaca HOURS Inc. Board of Directors), and administered through local or regional banks.

Exchange Function

Why the mutual credit model? Of the various systems reviewed in this chapter, the mutual credit model provides the most desirable exchange medium. In a mutual credit system, trade credits provide all the benefits of the ideal money circuit. First, trade credits are issued without interest, allowing the technology to operate as a pure information medium. When a transaction takes place, the credits exchanged simply acknowledge the amount of value a member provided to the system. Second, in an ideal money circuit, the power to issue money is completely decentralized, granted to each member in the system. Third, because trade credits are issued at the point of transaction, the amount in circulation will always equal demand.

A mutual credit systems result is a decentralized, interest-free, and relatively self-regulating money supply. However, mutual credit systems tend to suffer from a number of problems that reduce the effectiveness of the model. First, mutual credit programs must remain closed in order to protect the integrity of the system. If trade credits were allowed to leave the system, it would disrupt the balance between credit and debt. Hence, mutual credit systems tend to be “membership use only.” This problem is further compounded by restrictive membership requirements. Only direct providers of goods and services, those able to back trade credits with real wealth, are permitted to join. This excludes wage earners from participating in the program.

My solution is to open the system to wage earners by giving the employees of participating businesses automatic membership. Employers could then pay a portion of wages using trade credits. This would open the system up to broader community participation and would also overcome the limitations of a closed mutual credit system. By expanding and diversifying participation to include local businesses, professionals, and wage labor, the system will naturally offer a greater variety of goods and services.

Given its community context, the proposed mutual credit system would operate much like a LETS program, requiring a central record-keeping office to keep track of members' transactions. However, expanding participation as suggested would amplify the inherent problems of LETS account administration. The larger and more diverse membership became, the harder it will be to set flat limits on credit and debt.

My hybrid model attempts to solve this problem by incorporating the local banking industry into an expanded mutual credit program. A bank can provide the expertise and infrastructure needed to administer to a more diverse membership. This would allow a community to enjoy broad participation, as in a local currency program, without having to sacrifice the benefits of the self-regulating ideal money circuit. Initially, each member would open a current account with a participating mutual credit bank. The bank would then assign each member both a debt limit and a credit limit based on the member's financial status. For example, the account for a local retailer would need a higher debt limit than the account of a self-employed professional who worked at home. In the case of wage earners, their credit and debt limit would be accessed based on the amount of pay received in trade credits.

Incorporating a community's existing local banking sector with the traditional mutual credit model, can also streamline the method of payments. Instead of reporting transactions to a central record-keeping office, as in a LET system, members would make payments using normal bank checks and debit cards. Trade credits would also be convertible into local scrip for more convenience.

Savings Function

One of the primary limitations to both the mutual credit and local currency models is that neither provides a means of savings. Savings are necessary for the creation of investment capital. Furthermore, if the function can be provided by a community exchange system, it ensures the savings will be reinvested in the local economy. In my hybrid proposal the savings function would be performed through a mutual credit savings coop, which operates on the JAK banking model. These operations could be incorporated into one of the participating local banks, or cooperatively provided among them, as long as it permits the community to save collectively. If each bank were to offer its own savings options it would reduce the lending benefits of a large savings pool.

Upon becoming a member, each participant would be given an account with the savings coop. In accordance with the current/capital account scheme, each member's current account would be assigned a balance cap determining the maximum number of credits it is allowed to carry. If a member's current account has too many credits at the end of a quarter, the excess credits will be cleared to his or her capital account for storage (i.e. forced saving). This, along with planned savings, would create a capital pool from which members could obtain interest-free loans.

As a concession to forced saving, members will, for the most part, be able to choose between a variety of savings accounts, each with varying degrees of accessibility. However, there is one exception; each participant would be automatically assigned an Open, or basic capital account upon becoming a member. Excess credits cleared from a member's current account would be automatically transferred to their Open account. In keeping with the JAK model, the first and most accessible account would be the Open account. Under normal banking conditions there would be no restrictions on

withdrawals. However, because they are so easily accessed, it may prove useful to apply a balance cap on Open accounts to prevent hoarding and ensure that funds don't remain idle. Given their accessibility, these accounts would accrue very few savings points. Long-term savings accounts would accrue more savings points, but access would be limited by advanced notice requirements and/or long maturity periods.

Oversight and Administration of the System

Oversight of the hybrid model is designed to ensure that the system is managed within the appropriate local context, and that decision makers are democratically accountable to members. Although administration in this system is vested in participating banks, and the savings-and-loans coop, policy decisions will be made by a member-elected Board of Directors. The Board would have all the usual administrative responsibilities that accompany an hour-based local currency: i.e. overseeing the printing of local scrip, and publishing of a member directory/catalogue. However, its most important responsibility would be to set local monetary policy. To this end, the hybrid system, as opposed to earlier models, provides many more opportunities to influence local or regional economic conditions.

As we've seen in the general economy, when decision makers focus solely on economic issues, their effectiveness at furthering political and social goals is greatly hindered. Hence, decision-making within the proposed system would represent a broad community base, and its mission would be defined beyond issues on currency and capital. To this end, the Board would have two main policy roles. The first role is to set and pursue local economic and community development goals. Some possible examples include setting lending requirements with the savings coop (i.e. 10% of savings must be invested in sustainable local business), and/or collaborating with local economic development groups, such as the Chamber of Commerce.

The second, and perhaps most important role, would be to adapt local monetary policy as needed to complement changes in the dollar economy. As a complementary exchange system, its purpose is to operate counter-cyclical to the general economy. When the general economy is in decline, the Board (in consultation with participating banks) may choose to increase access to trade credits. This could be achieved through a general increase in member debt and credit limits. During periods of boom in the dollar economy, debt and credit limits could be lowered to reflect the decrease in demand for trade credits.

Although the hybrid model does overcome some of the limitation inherent to mutual credit systems, one glaring problem remains: credit inconvertibility. To maintain the system's integrity, trade credits cannot be converted into national currency. If conversion were permitted it would disrupt the program's credit balance making it more difficult for debtors to repay their obligations. I attempted to mitigate this limitation by expanding participation, assuming that a more diverse system will be more self-sufficient.

However, the problem still remains. In the end the hybrid model represents an ideal local system. Whether or not it's possible remains to be seen, but it does provide a direction for future experimentation.

Conclusion

We need to see our communities not only as places of residence, recreation, and retail but also as places that nurture active citizens who make the rules that govern their lives and who have the skills and productive capacity to generate real wealth. Local economies must be more than branch plants of planetary corporations. Local government must be more than simply a body that reacts to higher levels of government.

— David Morris, “Communities: Building Authority, Responsibility and Capacity.”

I would be the first to admit that an interest-free monetary system will not bring about a new global utopia. The world has far too many problems for there to be any one simple solution. However, I do believe that monetary reform is an important step towards establishing what David Korten calls “a mindful market economy,” an economy that gives us the freedom to pursue what we know to be healthy, valuable, and just.

To this end, I suggest that future reformers should keep in mind one general principle, the *Principle of Subsidiary Function*. As explained by economist, and well-known advocate of decentralization, E. F. Schumacher, this principle could provide a starting point towards creating a more humane and democratic society. Citing a famous formulation of the principle, Schumacher writes:

It is an injustice and at the same time a grave evil and disturbance of right order to assign to a greater and higher association what lesser and subordinate organizations can do. For every social activity ought of its very nature to furnish help to the members of the body social and never destroy and absorb them (Schumacher, 1999).

In other words, let decisions be made at the smallest appropriate level. The Principle of Subsidiary Function does not negate the need for national as well as international decision-making bodies. But it does challenge the assumption that an international corporation will automatically be wiser and more efficient with its use of a community’s resources than the actual inhabitants – an implicit assumption of economic deregulation.

Attendant to the Principle of Subsidiary Function is an implicit burden of proof: proponents of deregulation must prove a community is unable to use its resources effectively, and that the responsibility could be better fulfilled by a large corporation. The goal is to prevent authority from being usurped from the appropriate decision-making body, with the assumption that smaller is better. To continue the quotation:

Those in command should be sure that the more perfectly a graduated order is preserved among the various associations, in observing the principle of subsidiary function, the stronger will be the social authority and effectiveness and the happier and more prosperous the condition of the State... Thereby [the center] will more freely, powerfully and

effectively do all those things which belong to it alone because it alone can do them: directing, watching, urging, restraining, as occasion requires and necessity demands (Schumacher, 1999).

In the future, economic policy should be designed with this understanding: the most effective authority comes not from the top down, but the bottom up. To create a truly mindful market economy, the democratic accountability of those who establish economic policy must be assured.

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