

Why We Don't Understand Money and Debt – And Why It's Important That We Do

A Brief History

John E. Hemington, Jr.
September 26, 2015

Most Americans do not understand the most elementary basics of money and debt at the national level. It is widely held by the great majority that the United States government is running out of money and is about to be strangled by debt. This is not at all surprising since we are bombarded with this information by senior public officials, Congressional leaders, the President and all of the mainstream media. This is not to suggest, however, that most of those spreading this misinformation are just as confused and misled as are the rest of us. It is easily the most persistent and destructive myth of our age. The biggest error people make is comparing the federal budget to a household budget – they are not at all similar in construction or operation.

So why is it that we have come to believe that the government is broke and strangled by debt? The fact is that it would be true if the United States was on a “gold standard” where public money is concerned. However, the U.S. went off the “quasi-gold standard” completely in 1971 when Richard Nixon terminated the Bretton Woods Agreement which governed monetary issues since the end of World War II. But, even then, it was not really a “gold standard”. It was a “Dollar standard” in which the United States agreed to back the Dollar by gold and all its currency to be redeemed for gold by those holding it. This was a stop-gap at the end of the war since the U.S. possessed virtually all of the available gold reserves at that time and had the only viable economy coming out of the conflict. No other developed nation possessed any meaningful gold reserves at the time.

When President Nixon dissolved the monetary structure of the Bretton Woods Agreement the U.S. moved to a pure “fiat money” system. That is a system in which the nation is a sovereign issuer of its own money. In this mode a government creates its money out of nothing and it is backed not by gold or some other commodity but by the full faith and credit of the nation and is valid for all debts and taxes. Beyond the “full faith and credit” such money is valued because the issuing government requires that all taxes must be paid in the currency created and issued by the government. Inflation, should it occur, is kept in check by the imposition of taxes which serves to take money out of the economy. What confuses most people is that a sovereign issuer of money does not require taxes in order to spend. In fact, before taxes can be collected, the government must first “spend” money into the economy. It is, or should be, a simple straightforward process which is easily understood. Unfortunately, it is not.

The American public and, I believe, most of those elected to run the nation believe that we are still monetarily constrained by a “gold standard”, i.e., that federal government must collect taxes in order to spend; or, it must borrow the money needed to spend. This is mostly a devious myth. Mostly because the government is required to borrow its money from outside sources in order to operate, but not for the reasons most people believe. This is where the distortion arises. There is no natural reason that a sovereign issuer of its own money should ever have to borrow to fund

any program or to pay any debt denominated in its own currency. So why is it that the United States carries an enormous national debt?

This was a question which troubled me for quite some time and one which was quite difficult to find an answer to. I queried a number of persons who should know, including William Greider who wrote the definitive history of the Federal Reserve Bank, *Secrets of the Temple*, and he replied that he did not know either. It took some considerable time but I was finally able to discover just why it is that the U.S. must pay interest on the people's money it creates. It is, to put it mildly, a scam. A scam, which should come as no surprise, instigated by Wall Street banking interests.

It goes as follows: In 1913 the Federal Reserve Act was passed establishing the Federal Reserve Banking system and the Federal Reserve Bank as the central bank of the nation. This, it can be said, was also a slight of legislative hand initiated by the major Wall Street banks which are the actual owners of the Federal Reserve Bank. At the time the Fed was created the U.S. was in fact on a gold standard and had to borrow any money it needed to spend which exceeded the actual amount of gold it possessed to back the currency. (It should be noted that currency, as used here, does not refer solely to paper notes and coins which comprise only a tiny fraction of the money created and issued.) However, during the Great Depression the U.S. went off the gold standard, called in all privately held gold and implemented a fiat money system. This caused the monied interests on Wall Street some significant grief as they were no longer in a position to profit from government borrowing.

As a result a great deal of pressure was applied to those in Congress to do something about this loss of guaranteed revenue. So, in 1935, with no fanfare whatsoever, Congress quietly passed what is known as *The Banking Act of 1935*, amending *The Federal Reserve Act of 1913*, in which the Federal Reserve, which issues the money of the United States on the order of the Treasury, was no longer permitted to buy bonds directly from the Treasury at no cost. Instead, the Treasury was required to sell its bonds first to middlemen, Wall Street bond brokers, who would then sell them to the Federal Reserve so that money could be issued at interest. This is nothing more than a direct subsidy for Wall Street bond brokers written into the law of the United States. And it remains a mystery to almost all Americans to this time.

I found confirmation for this in testimony given by Marriner Eccles, Chairman of the Federal Reserve (the last good Chairman of the Fed) to Wright Patman's House Committee on Banking and Currency, March 3-5, 1947. In which Rep. Patman asked the following question:

The original act as passed in 1913, up until about 1935, gave the Federal Reserve banks that power (the power to buy bonds directly from the Treasury without interest – jeh); **is that right? . . . Yes; now, since 1935, in order for the Federal Reserve banks to buy Government bonds, they had to go through a middleman, is that correct?**

To which Chairman Eccles responded:

That is correct.

Then the following discussion ensued:

“Mr. PATMAN. In other words, Mr. Eccles, that is an argument in favor of the Government selling bonds to the commercial banks and permitting them to pay for them by a bookkeeping transaction and receive interest on them in order to pay the cost of carrying their accounts with individuals and corporations; is that correct?”

“Mr. ECCLES. That is right.”

“Mr. PATMAN. In other words, it is a subsidy, is it not?”

Rep. Patman continues:

In the beginning, may I make it plain that I am not opposed to interest being paid by individuals or corporations for the use of other people’s money that they have hired. Neither am I opposed to the payment of interest by States, counties, and political subdivisions for money that they hire. I am opposed to the United States Government, which possesses the sovereign and exclusive privilege of creating money, paying private bankers for the use of its own money. These private bankers do not hire their own money to the Government; they hire only the Government’s money to the Government, and collect an interest charge annually. . . .

In the beginning, may I make it plain that I am not opposed to interest being paid by individuals or corporations for the use of other people’s money that they have hired. Neither am I opposed to the payment of interest by States, counties, and political subdivisions for money that they hire. I am opposed to the United States Government, which possesses the sovereign and exclusive privilege of creating money, paying private bankers for the use of its own money. These private bankers do not hire their own money to the Government; they hire only the Government’s money to the Government, and collect an interest charge annually. . . .

The testimony continues on how money is created:

“Mr. PATMAN. The stock is less than \$140,000,000 and you do several hundred billions dollars’ worth of business a year sometimes, and furthermore, when you actually hold and claim now over \$2,000,000,000 in Government securities which you claim you bought. How did you get the money to buy those \$2,000,000,000 of Government securities?”

“Mr. ECCLES. We created it.”

“Mr. PATMAN. Out of what?”

“Mr. ECCLES. Out of the right to issue credit, money.”

“Mr. PATMAN. And there is nothing behind it, is there, except the Government’s credit?”

“Mr. ECCLES. We have the Government bonds.”

“Mr. PATMAN. That’s right, the Government’s credit.”

“Mr. ECCLES. That is what your money system is.”

On the system being absurd:

“Mr. ECCLES. That is all we have ever done. That is the way the Federal Reserve System operates. The Federal Reserve System creates money. It is a bank of issue.”

...

“Mr. PATMAN. What better evidence do you want than that, gentlemen? There is no dispute about what I say, and I insist it is absolutely wrong for this committee to permit this condition to continue and saddle the taxpayers of this Nation with a burden of debt that they will not be able to liquidate in a hundred years or two hundred years.

Do you know that we are carrying a million dollars' worth of bonds that were issued during the War between the States and we have paid 4 billions in interest for every \$1 that was borrowed? We are still paying on them and still owe them. Do you know that on the Panama Canal convertible 3's, we have already paid more than \$50,000,000 in interest and we will soon have paid \$75,000,000 in interest and still owe the \$50,000,000 principal on those bonds? If you judge the future by the past, the people will be compelled to pay a dollar, \$2, and \$5 in interest for every \$1 they borrow. Does any man, then, say that we shouldn't seriously consider any plan that will enable the taxpayers of this Nation to make that payment on the principal of the debt and not on the interest? Two and a half million each year, and in 40 years liquidating the entire debt, and removing that inflationary condition that we will have by reason of the expenditures during this war.

Later in the hearing Chairman Eccles was quoted as follows on the mystery of money:

“Constitutional Mandate

“The framers of the United States Constitution, in article I, section 8, very wisely said: “Congress shall have the power to coin money and regulate the value thereof. “This provision of the Constitution is mandatory. All Members of Congress are sworn to uphold the Constitution. Why has this provision never been carried out? The answer is simple. In the early days of our national existence the people were deceived into believing that the subject of money was so mysterious and intricate that only a few of the financiers understood the subject and therefore the great privilege of issuing and distributing money should be farmed out to them. This was done, and it has never been changed, except to give them more power and authority. The strange part of it all is that the ones who are the beneficiaries of this great privilege are not even charged with the duty of furnishing the people a sufficient circulating medium.

What all of this makes clear is that the people of the United States have been and are continuing to be swindled by Wall Street and their minions in Congress since almost the very conception of the nation – and in recent years things have only become worse and more egregious as greed has outpaced any interest in the national well-being. We need to come to grips with the reality that

our nation's debt is largely a fiction which is being used to bludgeon the American populace into submission to the tiny ruling minority who seek to impose austerity and privatize all of the public assets and programs worth stealing and drive the great majority into low wage slavery and helpless poverty. This is the neoliberal plan and so far it has been executed to perfection through deceit and deception.

The nation carries a national debt because Congress elected to require that it do so. Anything Congress can do by legislation it can also undo – if it can escape the clutches of the neoliberal Wall Street cabal that now runs much of the world from the cloistered corridors of central banks. This can only occur if people come to understand just how they are being swindled by the financial lords and rise up and demand that changes be made. Unless and until the people of this nation can wake up and realize that their future is being stolen from under their noses because they are systematically being deceived about how money works and thus unable to understand how and why they are being denied access to that share of the nation's wealth which is properly theirs. It will require a substantial effort to overcome years and years of mind-numbing propaganda intended to hide the theft of the nation's wealth from the prying eyes of the public. But once people come to understand just how they have been systematically robbed they will not stop until the injustice is rectified.

It was Henry Ford who once said something to the effect that if the people came to understand just how banking worked there would be an immediate revolution. Now is the time for people to look behind the curtain of deceit and have the scales fall from their eyes.

In the 1920s when Thomas A. Edison was inspecting Muscle Shoals, he remarked that the Government should operate that great project in the interest of the people. He was asked if he favored the Government borrowing the \$30,000,000 necessary to make repairs. His answer substantially was: 'No; why should the Government borrow its own credit? If it issues tax-exempt interest bearing bonds and sells the bonds to Wall Street bankers to get the money, by the time the bonds are paid the bankers will have collected as much in interest as the Government received on the bonds. In other words, the bankers, who will not furnish an ounce of material or a lick of labor, will get as much out of it as the men who do the work and furnish the material.' Mr. Edison also said at the same time: 'Any government that can issue a dollar bond, interest bearing, that is good can issue a dollar bill, noninterest bearing, that is good; the only difference is the bill is easier to redeem because it does not draw interest.'