*The Biblical Critique of Inflation*

A Chapter taken from

# An Introdution to Christian Economics

BY DR. GARY NORTH

## Chapter I

# THE BIBLICAL CRITIQUE OF INFLATION

The Hebrew prophets came to Israel and Judah with the call to repentance. Invariably, the call was expressed in concrete terms. God, they announced, requires repentance from specific, concrete sins. That is the reason why they were so unpopular. R. H. Tawney, in his study of Puritan origins, comments that "No church has ever experienced any great difficulty in preaching righteousness in general: no church has found a specific to disguise the unpalatableness of righteousness in particular. . . ."[1] The same problem faces modern critics of society who come to God's people (let alone the religious rebels ) to demand that they amend their specific ways of doing business or operating the civil government. All the flabby moral platitudes that roll off the tongues of hired servants in the pulpits—those vague calls to godliness devoid of concrete guidelines of daily behavior-receive the automatic "amens" from the congregations that do the hiring. Let the preaching become specific, and "the preacher is meddling in areas that he knows nothing about." What the congregations pay for is a weekly affirmation of their status quo. Of course, their status quo may be somebody else's revolution, so they may regard themselves as being very, very daring, very hip, very chic, the vanguard of change; always, however, ***their*** status quo is left undisturbed. That is what they pay for, just as the people of Israel paid for it in the eighth century, B.C. ( Ezek. 14). The result for the people of Israel was captivity.

There is an unfortunate tendency for modern commentators to emphasize the spiritual and personal aspects of the prophetic message to the people as individuals, and to ignore the stated transgressions of the nation as a whole. The pietistic inheritance of social antinomianism runs deep in modern Christianity. It is, as Rushdoony has called it, the heresy of the faithful.[2] Yet it was the message of the

1. R. H. Tawney, "Introduction; Thomas Wilson, *A Discourse Upon Usury* (London: Frank Cass, [1925] 1969), p. 114.
2. R. J. Rushdoony, *The Biblical Philosophy of History* (Nutley, N. J.: The Craig Press, 1969) [chap. 32, below].

prophets to the kings as national leaders that got them into so much trouble with the civil governments of the day. Their critique of Hebrew life involved all the spheres of life in the Hebrew commonwealth: politics, religious idolatry, economics, jurisprudence.

The prophet Isaiah presented a catalogue of sinful practices to the people of Israel. These charges against the nation are found in the first chapter of the book of Isaiah. If the nation continues in its defiance of God's civil law-order, he announced, then the people will be carried into captivity by a gentile nation. Transgression, in short, requires punishment; if rebellion is national and collective, then the punishment will be national and collective. This has great importance today: similar sins should produce similar punishments.

In verse 21 of the first chapter, we read that judgment and righteousness once lodged in the faithful city, but now murderers inhabit its streets. Verse 23 is equally specific: the nation's princes consort with thieves, seek after bribes, and render corrupt judgments. But for our purposes, verse 22 is the key passage: "Thy silver is become dross, thy wine mixed with water."

It is a sign of the social and cultural impotence of contemporary Christianity that commentators interpret this verse in a so-called "spiritual" fashion. It is supposed to refer only to the souls of individual citizens. Passages such as Psalms 119:119 or Ezekiel 22: 18-19 can be cited as "proof" of this thesis. The problem with this interpretation is that the prophets used known social and economic deviations in order to point out to the people their spiritual sins, a device used by Christ in many of the parables. They went from the concrete sin of the defrauder to the ethical deviation of the citizenry. If the legitimacy of the prophetic charge against the economic practice in question is denied, then the impact of the critique of men's souls is thereby undercut. Verse 22 appears between concrete criticisms of specific political and social deviations, yet commentators are afraid to take verse 22 as referring to equally concrete sins. This is not the way to exegete the Bible.

Precious metals, then as now, were considered valuable economic resources. Well over 350 references to gold appear in Strong's ***Concordance,*** and about the same number of references to silver. Even in Genesis 2:11, prior to the fall of man, we read of the wonders of "the whole land of Havilah, where there is gold," 'and the next verse informs us that "the gold of that land is good. . . ." Abram's wealth was counted in "cattle, in silver, and in gold" (Gen. 13: 2). Gold played an important role in worship, whether godly

(Ex. 25; 26; 28; 37) or pagan (Ex. 20:23; 32). The glories of the judgments of God are compared to fine gold; they exceed the value of gold, gold apparently being the most commonly understood commodity of historic value ( Ps. 19:9-1 O). Similarly, godly wisdom is compared favorably with gold, and is said to be even more desirable ( Prov. 3: 14; 8:10, 18, 19). Both silver and gold functioned internationally as money. Benhadad, king of Syria, when he beseiged Israel, sent messengers to Ahab announcing Syria's sovereignty over Israel's gold and silver (I Kings 20:3 ).[3] Payment was made by the king of Syria to the king of Israel when he wanted the leprosy of Naaman, his commander, cured (H Kings 5:5). There is no question that gold and silver were the money of Israel and Judah (II Kings 12, esp. vs. 13).

The constant concern of Old Testament law with the honesty of weights and measures was equally applicable to honest money. The talent and the shekel were units of weight in the Old Testament.[4] Thus Professor Daniel-Reps writes:

> Exactness of weight was important not only for dealings in corn and other goods, but also as a guarantee of the soundness of the currency. The Proverb "Scale and balance are emblems of the Lord's own justice; no weight in the merchant's wallet but is of divine fashioning" (Prov. 16:11) refers both to honest weight and to good money. Long before money in the sense of coins struck with a symbol or a likeness existed in Israel, men had settled their debts by producing a given weight of precious metal: it was in this way that Abraham at Ephron weighed out four hundred shekels of silver, warranted silver, to buy the field and cave where his wife Sarah was buried. The word shekel was derived from the root *sekel, which* in both Assyrian and Hebrew conveyed the notion of counting as well as weighing. The practice of weighing money rather than counting it was still general in the Palestine of Jesus' day, as it was all round the Mediterranean. The scales also served to ensure that the coins were of the true metal and that they had neither been filed nor clipped; indeed, this inspection was one of the banker's and money-changer's

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3. The Assyrians used gold and silver for taxation, for tribute, and for booty: Georges Contenau, *Everyday Life* in *Babylon and Assyria (New* York: Norton, 1966), pp. 136, 138,.148, 153, 155.

4. Common weights (as distinguished from royal weights) of the Old Testament were in two varieties, heavy and light. The light weights were as follows:

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| Talent | 30 kilograms |
| Mina | 500 grams |
| Shekel | 8.33 grams |

Heavy weights were:

| | |
|---|---|
| Talent | 60 kilograms |
| Mina | 1 kilogram |
| Shekel | 16.67 grams |

See *The Interpreter's Dictionary of the Bible (New* York: Abington, 1952), I, p. 831.

> chief tasks. It must have been far from easy, when one thinks of the variety of coins current in Palestine at the time.[5]

Coins did not exist in Palestine in the days of the prophets, or so the archeological evidence indicates. They came into use only after the exile. The precious metals were probably in the form of ingots. In the time of Isaiah it appears that the people were resorting to an ancient practice; they were debasing the ingots and metallic ornaments with cheaper metals.

Counterfeiting has to be punished. If private citizens do it, the State must intervene and punish the violators, since fraud and theft are both involved. Yet the State is also to be limited by this law of honest weights and measures; it must not force its citizens to accept a unit of money which is worth less in exchange than its face value. In short, legal tender laws are immoral; currency debasement is immoral; printed unbacked paper money is immoral. To mix cheap metals with silver or gold and call the result pure gold or pure silver is totally fraudulent. Yet this is what was being done in Isaiah's day. Ezekiel warned them of the consequences of such gross (or dross) immorality:

> Son of man, the house of Israel is to me become dross: all they are brass, and tin, and iron, and lead, in the midst of the furnace; they are even the dross of silver. Therefore thus saith the Lord God; Because ye are all become dross, behold, therefore I will gather you into the midst of Jerusalem. As they gather silver, and brass, and iron, and lead, and tin, into the midst of the furnace, to blow the fire upon it, to melt it; so will I gather you in mine anger and in my fury, and I will leave you there, and melt you. Yea, I will gather you, and blow upon you in the fire of my wrath, and ye shall be melted in the midst thereof. As silver is melted in the midst of the furnace, so shall ye be melted in the midst thereof; and ye shall know that I the Lord have poured out my fury upon you (Ezek. 22: 18-22).

In short, "I will turn my hand upon thee, and purely purge away thy dross, and take away all thy tin" (Isa. 1 :25).

The link between the debasement of precious metals and the immorality of government had been made long before Isaiah's day. The Proverbs record this warning: "Take away the dross from the silver, and the smith has material for a vessel; take away the wicked from the presence of the king, and his throne will be established in righteousness" ( Prov. 25:4-5, RSV). Weights and measures are to be kept honest; silver is not to be mixed with tin; wine is not to be

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5. Henry Daniel-Reps, *Daily Life in the Time of Jesus* (New York: Hawthorn Books, 1962), pp. 222-223.

mixed with water; and kings are not to consort with wicked men. This is concrete preaching.

· Currency debasement is the oldest form of monetary inflation. It is not surprising that Isaiah should, in the same verse, refer to the debasement of silver and the debasement of wine. Monetary inflation is very often accompanied with a disastrous fall in the quality of economic goods, especially in the last stages of the inflation. Professor Rothbard has described this interrelationship, and it is a grim picture:

> To gauge the economic effects of inflation, let us see what happens when a group of counterfeiters set about their work. Suppose the economy has a supply of 10,000 gold ounces, and" counterfeiters, so cunning that they cannot be detected, pump in 2,000 "ounces" more. What will be the consequences? First, there will be a clear gain to the counterfeiters. They take the newly-created money and use it to buy goods and services. In the words of the famous *New Yorker* cartoon, showing a group of counterfeiters in sober contemplation of their handiwork: "Retail spending in the neighborhood is about to get a needed shot in the arm." Precisely. Local spending, indeed, does get a shot in the arm. The new money works its way, step by step, throughout the economic system. As the new money spreads, it bids prices up—as we have seen, new money can only dilute the effectiveness of each dollar. But this dilution takes time and is therefore uneven; in the meanwhile, some people gain and others lose. In short, the counterfeiters and their local retailers have found their incomes increased before any rise in the prices of the things they buy. But, on the other hand, people in remote areas of the economy, who have not yet received the new money, find their buying prices rising before their incomes. Retailers at the other end of the country, for example, will suffer losses. The first receivers of the new money gain most, and at the expense of the latest receivers.
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> Inflation, then, confers no general social benefit; instead, it redistributes the wealth in favor of the first-comers at the expense of the laggards in the race. And inflation is, in effect, a race—to see who can get the new money earliest. The latecomers-the ones stuck with the loss—are often called the "fixed-income groups." Ministers, teachers, people on salaries, lag notoriously behind other groups in acquiring the new money. Particular sufferers will be those depending on fixed-money contracts—contracts made in the days before the inflationary rise in prices. Life-insurance beneficiaries and annuitants, retired persons living off pensions, landlords with long-term leases, bondholders and other creditors, those holding cash, all will bear the brunt of the inflation. They will be the ones who are "taxed."
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> Inflation has other disastrous effects. It distorts that keystone of our economy: business calculation. Since prices do not all change

> uniformly and at the same speed, it becomes very difficult for business to separate the lasting from the transitional, and gauge tmly the demands of consumers or the cost of their operations. For example, accounting practice enters the "cost" of an asset at the amount the business has paid for it. But if inflation intervenes, the cost of replacing the asset when it wears out will be far greater than that recorded on the books. As a result, business accounting will seriously overstate their profits during an inflation —and may even consume capital while presumably increasing their investments. Similarly, stock-holders and real estate owners will acquire capital gains during an inflation that are not really "gains" at all. But they may spend part of these gains without realizing that they are thereby consuming their original capital.
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> By creating illusory profits and distorting economic calculation, inflation will suspend the free market's penalizing of inefficient, and rewarding of efficient, firms. Almost all firms will seemingly prosper. The general atmosphere of a "sellers' market" will lead to a decline in the quality of goods and of services to consumers, since consumers often resist price increases less when they occur in the form of downgrading of quality. The quality of work will decline in an inflation for a more subtle reason: people become enamoured of "get rich quick" schemes, seemingly within their grasp in an era of ever-rising prices, and often scorn sober effort. Inflation also penalizes thrift and encourages debt; for any sum of money loaned will be repaid in dollars of lower purchasing-power than when originally received. The incentive, then, is to borrow and repay later than save and lend. Inflation, therefore, lowers the general standard of living in the very course of creating a tinsel atmosphere of "prosperity."[6]

Rothbard's analysis indicates why God so opposes monetary inflation, whether practiced directly by the State or simply private fraud which is tacitly sanctioned by the State. Currency debasement is theft. It involves the redistribution of wealth. Those on fixed incomes suffer. The quality of production tends to decline. Monetary inflation (currency debasement ) is a fraudulent, invisible tax, and the Bible prohibits it. The nation which permits monetary inflation to persist, as if it were not a terrible moral evil, will suffer the consequences described by Isaiah and Ezekiel.

### *Multiple Indebtedness*

The Bible regards debt as a form of slavery.[7] "The rich ruleth over the poor, and the borrower is servant to the lender" ( Prov.

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6. Murray N. Rothbard, *What Has Government Done to Our Money?* (Colorado Springs: Pine Tree Press, 1964), pp. 28-29. Available from the Foundation for Economic Education, Irvington-on-Hudson, New York 10533.

7. R. J. Rushdoony, *Politics of Guilt and Pity* (Nutley, N. J.: The Craig Press, 1970), pp. 204-205,250 ff.

22:7). Thus, the New Testament lays down this rigorous principle: "Owe no man anything, but to love one another . . ." (Rem. 13: 8a). The message of the Scriptures is not perfectionist, however, so that this general principle may legitimately be transgressed under certain emergency situations, but very definite restrictions are placed upon every believer's entry into debt.[8]

> The believer cannot mortgage his future. His life belongs to God, and he cannot sell out his tomorrows to men, nor bind his family's or country's future. This means that long-term personal loans, deficit financing, and national debts involve paganism. What we cannot do to ourselves we cannot permit either our families or our fellow believers to do to themselves. A country which is Christian is similarly to be governed. But we cannot expect unbelievers to live by our faith or by God's law; and to allow them the liberty of their way is no sin, providing we deal justly with them.[9]

This is why it was legitimate to take interest from the unbeliever, but not from the believer ( Lev. 25: 36-37; Deut. 23: 19-20). The unbeliever is, by definition, a slave to sin; the believer is not.

In Exodus 22:25-27, we find one of the key passages dealing with indebtedness. It lays down two general rules: no interest shall be taken from fellow believers for a charity loan; and the collateral, if it is necessary for the debtor's existence, must be returned to him when he needs it. In the first case—the loan to a believer-the foregone interest constitutes a charitable donation to the one in need. That seems clear enough; the lender could have, used the goods or money for his own purposes during the period of the loan, yet he forfeits his right to receive compensation for the loss of the use of his goods. The second clause, however, is not generally understood.

The raiment taken by the creditor as collateral must be returned to the debtor in the evening. This is a very peculiar kind of collateral. The more common kind is the kind that I once heard a priest used for loans in his predominantly Mexican-American parish: he took two of the car tires. There was a great incentive, he said, for the family to get its loan paid off. But a garment which must be returned to the debtor each evening, and taken by the creditor during the day, is strange, on the surface. It does the creditor no visible good, and the debtor does not forfeit the use of his collateral when he really needs it, i.e., during the cold of the night. If anything, it seems to be a nuisance for the creditor.

The collateral ("surety") in this case is a benefit to the creditor

8. *Ibid.,* p. 243 ff.

9. *Ibid.,* p. 249.

only indirectly. Its real function is to limit the indebtedness of the borrower. The man who needs a loan is permitted to indebt himself and his family only up to the value of his collateral. His immediate property determines the extent of the mortgage on his future. While his collateral is in the possession of one creditor, it cannot simultaneously be used as collateral for additional loans from other creditors. The benefit to the creditor is indirect: his possession of the collateral during the day guarantees him that the debtor is not in debt beyond his probable capacity to repay. The size of the loan (and therefore the extent of the debtor's enslavement) is limited by the debtor's general economic capacities. He is forbidden to indebt himself too far.

The general principle of biblical debt is simply this: multiple indebtedness is prohibited. Debts may not be incurred beyond the value of one's immediate assets. A man (and, by inference, an institution) may not mortgage its future beyond very definite limits. This protects the creditor from extending loans to unreliable, overextended, basically wasteful debtors. It protects the debtor from going into debt beyond his reasonable capacity to repay.

It should be understood that one's "immediate assets" include such things as integrity, past performance in repaying debts, and potential capacity to repay in the future. Henry Hazlitt, in his excellent little book, Economics *in One Lesson,* has commented on the nature of credit:

> There is a strange idea abroad, held by all monetary cranks, that credit is something a banker gives to a man. Credit, on the contrary, is something a man already has. He has it, perhaps, because he already has marketable assets of a greater cash value than the loan for which he is asking. Or he has it because his character and past record have earned it. He brings it into the bank with him. That is why the banker makes him the loan. The banker is not giving him something for nothing. He feels assured of repayment. He is merely exchanging a more liquid form of asset or credit for a less liquid form. Sometimes he makes a mistake, and then it is not only the banker who suffers, but the whole community; for values which were supposed to be produced by the lender are not produced and resources are wasted.

Therefore, a person who is not destitute (unlike the case of the poor man who wants an interest-free charitable loan from his brother in the faith) has assets with which to bargain for a loan. But the Bible is clear: it is best not to be in debt at all (Rem. 13:8), and a six-year debt limitation is the maximum that is morally legitimate (given the provisions of the sabbatical years regarding the cancellation of all debts, as well as the jubilee year; Deut. 15:1-6, 12-18; Lev. 25).

The importance of this law for monetary affairs cannot be overstated. Contemporary society—indeed, society since the Middle Ages —has ignored this restriction on multiple indebtedness with impunity. From an economic standpoint, the chief private violators institutionally are the fractional reserve banking system and the limited liability corporation. The entire public sphere of civil government rests on the violation of the principle. The whole structure of modern credit is based upon the idea that men should never escape from perpetual debt. The public debt of the federal government, already approaching half a trillion dollars (excluding future commitments like Social Security payments, bank insurance, and other "agency" debt ), is steadily eroding the monetary unit, in the process described by the nineteenth century theorist, Charles Holt Carroll, as "the organization of debt into currency," or the monetization of debt.[10] The central bank of every nation—the Federal Reserve System in the United States—prints up the money to finance the deficits of the central government, and in return for this fiat currency, the government gives an interest-bearing bond to the bank. The Federal Reserve System receives about $4 billion a year in this way at the present time, and it will go higher as time (and unsalable government indebtedness) continues. (The government pays out over $20 billion in interest altogether—to insurance companies and other institutional investors, including local banks, as well as to citizens. The FRS returns most of its interest payments to the Treasury each year, however. ) From a biblical standpoint, this is utterly corrupt: "The wicked borroweth and payeth not again" (Ps. 37:21 a). The civil authorities do not intend to reduce this debt and repay the principal. They favor perpetual indebtedness. Laws that are transgressed in God's universe will be found to contain their own built-in punishment. The French Revolution came when the king had to assemble the *Estates-General,* for only they could raise needed new taxes, and the interest of the bloated French national debt was absorbing half the revenues of the kingdom annually. The British interest payments were about the same in this same period.[11] It had been the attempt of the British government to impose new taxes on the American colonies that had triggered the American Revolution. Massive national indebtedness is highly dangerous.

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10. Charles Holt Carroll, *The* Organization *of Debt Into Currency (New* York: Amo Press, 1971).

11. R. R. Palmer, *A History of the Modern World* (3rd cd.; New York: Knopf, 1965), p. 338.

The modern banking system is based upon the use of fractional reserves. Few citizens seem to understand the mechanism involved. With a ten percent reserve requirement (imposed by the central bank, itself a quasi-governmental agency), a single deposit of $100 can be used to create $900 worth of loans throughout the entire banking system. Fractional reserve banking has vastly outstripped the State's printing of paper money as a means of inflation, even as paper money vastly outstripped outright coin clipping and the debasement of money metals after the sixteenth century. All it takes for the process to begin is for a citizen to make a deposit of $100 in his local banking account, either checking (demand deposit) or savings (time deposit ). In his lucid discussion of fractional reserve banking, Professor Wilhelm Roepke makes it plain that the existence of modern banking rests upon the systematic violation of the biblical prohibition on multiple indebtedness.

> We find, too, that the same sequence of credit expansion which is associated with the issuance of bank notes occurred in the case of demand deposits. Thus, to the extent to which demand deposits circulated as money, the banks felt themselves freed of the obligation of maintaining a 100 per cent cash reserve behind these deposits, despite the fact that they are debts of the bank subject to payment on demand (hence the name "demand deposit"). To provide the necessary minimum liquidity (the ability to meet expected demands for cash) it was deemed sufficient to maintain a supply of money equal to, let us say, 10 per cent of the total demand deposits outstanding. The banks could loan out the remaining 90 per cent and earn enough in the process to administer the deposits without charge or even to pay a small amount of interest on them. Henceforth, the whole art of banking management consisted in effecting a daily compromise between the two opposed principles of liquidity and profitability, with the over-all goal being the maintenance of minimum liquidity and maximum profitability. Small errors of calculation could be corrected by recourse to the so-called "money market." Thus, the whole system is truly "minutely adjusted to reflect the smallest increment in weight which it can just support." We can now observe what an important bearing banking has on the entire monetary system. Prior to the development described above, only cash money circulated. Thenceforth, demand deposits circulated simultaneously with the greater part of the cash which gave rise to these same deposits. The circulation of demand deposits or check money was equivalent in short to the "creation" of an additional supply of money.
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> There is yet another angle from which we can observe how the modern banking system affects the supply of money. A businessman, for instance, may establish a demand deposit (checking account) not only by depositing hard cash in the bank, but by getting the bank to extend him a loan for this purpose. Thus, by

adhering to a proportion of 1:10 between cash reserves and outstanding demand deposits, with 90 per cent of the actual currency paid in being loaned out, the bank-can, by granting credits, create new checking accounts (demand deposits) to an amount nine times greater than that which has been paid into it. It is clear in this case that the bank, following the same procedure as a bank of issue, grants credits not out of preceding savings, but from additional resources obtained by the creation of credit. To what extent is a bank capable of creating credit? This depends on the bank's liquidity requirements, that is, upon the amount of the reserve which the bank must maintain to meet the demands for the conversion of check money into actual cash. This preoccupation with the maintenance of liquidity, which no bank can safely ignore, more or less effectively limits the bank's power to create credit. The liquidity requirements of banks fluctuate with the degree of confidence placed in banks, with the amount of the payments made to those who are outside the circle of the bank's regular clients (payrolls, small payments to retail merchants, farmers, etc. ), and with the turnover of individual bank accounts. But more significantly, the fluctuations to which bank liquidity is subject—and ***pro tanto*** the fluctuations to which the total supply of credit is subject-coincide to a very large extent with the ***cyclical fluctuations*** of ***prosperity and depression.*** In a period of expansion the economy's supply of credit increases, while the banks' liquidity is proportionately lowered (credit expansion); in a period of depression the banks seek greater liquidity and are forced, in the process, to contract credit (deflation).

It is of great importance that we thoroughly understand the above relationships, for without such understanding we cannot adequately comprehend the perils and the problems which currently beset our economic system. Hence, no effort should be spared in getting to the bottom of these relationships. One way of doing this is to imagine an economy where all payments are effected without the use of actual currency. Evidently, in such case, there would no longer be any limit to the power of the banks to create credit. The more widely extended is the system of transactions effected without cash, the greater becomes the power of the banks to "manufacture" credit. Yet again, we may compare a bank with the cloakroom of a theatre. In both cases we deposit something: in the bank, currency and in the cloakroom? our hats; in both cases in exchange for a receipt which authorizes us to reclaim what we have deposited. But while the cloakroom employees cannot count on the theatre-goer's ***not*** presenting his receipt because he regards it as just as good as his headgear, the bank may safely assume that its clients will in fact consider their receipts (i.e., their right to claim their deposits) to be equally as good as their deposits. A bank is in consequence an institution which, finding it possible to hold less cash than it promises to pay and living on the difference, regularly promises more than it could actually pay should the worse come to the worst. Indeed, it is one of the essential features of a modern bank that alone it is

> unable to meet a simultaneous presentation for payment of all the debts owed by it ("run on the bank") .[12]

What is Roepke saying? The banks operate under the assumption that its creditors-in other words, its depositors-will not call on the bank simultaneously for their money. Banks then proceed to indebt themselves far beyond their immediate assets, by loaning money to borrowers, who have their own checking accounts established for them by the bank. Then they start to spend their money on new furniture, or a new car, or on tools, or whatever. Those who sell to them then take *their* money to their bank, and the whole process continues. If a bank run occurs, either on a single bank or on all the banks in the system, creditors are left in the cold. The hope in "bank insurance" is a stupid hope; the assets of the Federal Deposit Insurance Corporation consist almost entirely of government bonds! In case of a really serious money panic, these assets could be converted into cash only through the printing of unbacked paper money by the Federal Reserve System; in short, by monetary inflation. Elgin Groseclose has disposed of the FDIC quite effectively:

> The deposit guarantee provision can be disposed of briefly. The merits of the scheme are not easy to appraise, since the country has experienced no credit crisis since its establishment. As constituted, a government controlled institution, the Federal Deposit Insurance Corporation, was created with capital supplied to the extent of $150 million by the Treasury, by member banks to the extent of ½ per cent of their deposits, and by Federal Reserve banks to the extent of half their surplus on January 1, 1933. Membership in the insurance scheme was compulsory for members of the Federal Reserve System, and depositors were eventually to be insured as to the first $10,000 of their deposits and to a lesser proportion for deposits beyond $10,000 (75 per cent between $10,000 and $50,000 and 50 per cent beyond $50,000).
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> In the years since (through 1962) the Corporation collected some $1.9 billion in assessments; it incurred net costs of $30.5 million in losses (while disbursing some $365 million in connection with the liquidation of insured banks) and accumulated total assets of $2,645 million, all but $10.5 million of which was invested in U.S. government bonds. The fund represented (as of the end of 1962) 1.4 per cent of insured deposits; of total deposits of $297 billion in insured banks, $179 billion were insured.
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> Three inferences may be drawn from these statistics: (a) the fund is another convenient source of government deficit financing;

12. Wilhelm Roepke, Economics *of the Free Society* (Chicago: Regnery, 1963 ), pp. 91-93. This is a tine introductory study of economics.

(b) the fund, together with its collateral supervisory activities, has stemmed bank failures, both by reducing the extent of loose banking and by discouraging panics; and (c) the fund would be inadequate in the event of any major credit crisis.[13]

The "gold crisis" of the United States since 1960 was produced by the disparity between the stated promise of the United States to redeem all dollar claims held by foreign central banks at a rate of $35 per ounce and the steady persistence of deficit federal budgets, financed increasingly through indebtedness to the Federal Reserve System. We have seen the creation of vastly more IOU's to gold (dollars) than there is gold to back them up. Hence, the steady shrinkage of the nation's supply of gold; hence also the series of international monetary panics, most notably in March of 1968 and August of 1971. Multiple indebtedness brings with it bank runs, whether the banker is the fellow on the corner or the government of the United States.

The other institution that has been created by the advent of multiple indebtedness is the limited liability corporation, which has flourished in the industrialized West for almost a century. The corporation, in distinction from a partnership, is responsible only for the value of its assets. Creditors can collect, in case of a corporate bankruptcy, up to the value of the corporation's property, but they cannot gain access to the funds of the legal owners, i.e., the shareholders. In a partnership, the individual owners are responsible for all debts incurred by the company, and they may be sued for losses in case of the bankruptcy of the company. Thus, the limited liability corporation tends to become a huge, impersonal structure in which effective ownership is separated from management. Rushdoony's comments are significant:

> Liability is inescapable; by limiting the liability of the company which contracts a debt, or permits a fraud, the liability thus shifts responsibility away from the responsible to society at large. A partner or shareholder in a company will exercise cautious and conscientious control over his company, if his liability for the debts and frauds of that company are not limited to the extent of his investment. The result is sound, moral, and careful management of a company by the actual owners. But, with limited liability, a premium is placed on profit irrespective of responsibility. The shareholder is less concerned with buying responsible ownership and more concerned with buying a share in profits. And then, as the state further protects the shareholder, against liabilities in his irresponsible pursuit of profits, the shareholder be-

13. Elgin Groseclose, *Fifty Years of Managed Money* (New York: Books, Inc.; London: Macmillan, 1966), p. 198. The State *could* pay off the FDIC debts by printing money: repressed depression, leading to mass inflation.

> comes less and less concerned with the responsible and moral management of his company .[14]

Furthermore, Rushdoony argues plausibly, "limited liability has, in the long run, assured a greater readiness by corporations to assume debt."[15] Given the presence of fractional reserve banking, this propensity to borrow adds to the money supply, since ninety percent of the loan capital is created by the bank out of thin air (if the reserve requirement is ten percent, as it generally is today for demand deposits).

The separation between property and ownership, between ownership and management, has no doubt been overemphasized in the last three decades. So long as there is the possibility of the corporate take-over, there will be pressures on managers to operate an efficient firm.[16] Nevertheless, there has been an erosion of personal responsibility within the framework of large, impersonal firms, which in turn has come from government intervention into the operation of these firms.[17] Limited liability laws are one form of this intervention, and in the long run it may end, as Joseph Schumpeter has predicted, in the dissolution of capitalism and the free market. In a moving, terrifying section of his important book, ***Capitalism, Socialism, and Democracy,*** Schumpeter writes:

> On the other hand, the capitalist process also attacks its own institutional framework—let us continue to visualize "property" and "free contracting" as *partes pro toto*—within the precincts of the big units. Excepting the cases that are still of considerable importance in which a corporation is practically owned by a single individual or family, the figure of the proprietor and with it the specifically proprietary interest have vanished from the picture. There are the salaried executives and all the salaried managers and submanagers. There are the big stockholders. And then there are the small stockholders. The first group tends to acquire thé employee attitude and rarely if ever identifies itself with the stockholding interest even in the most favorable cases, i.e., in the cases in which it identifies itself with the interest of the concern as such. The second group, even if it considers its

14. Rushdoony, *Politics*, pp. 256-257. For a nineteenth century theologian's critique of the limited liability corporation, see Robert LDabney, *Discussions: Philosophical* (Richmond, Va.: Presbyterian Committee of Publications, 1892), III, p. 329 ff. The main defect in Dabney's discussion is his hope that further government intervention can cure the problems caused by the original government intervention, namely, the establishment of limited liability laws. But his general criticism of limited liability is sound: it overstimulates the creation of high-risk ventures: p. 333 ff. This is the kind of Christian teaching which the twentieth century Protestant pietists have utterly abandoned.

15. Rushdoony, *Politics*, p. 260.

16. Cf. Henry Manne, *Insider Trading and the Stock Market* (*New* York: Free Press, 1966), chap. 8.

17. North, "Statist Bureaucracy in the Modern Economy," *The Freernan* (Jan., 1970) [chap. 20, below].

> connection with the concern as permanent and even if it actually behaves as financial theory would have stockholders behave, is at one remove from both the functions and the attitudes of an owner. As to the third group, small stockholders often do not care much about what for most of them is but a minor source of income and, whether they care or not, they hardly ever bother, unless they or some representatives of theirs are out to exploit their nuisance value; being often very ill used and still more often thinking themselves ill used, they almost regularly drift into an attitude hostile to "their" corporations, to big business in general and, particularly when things look bad, to the capitalist order as such. No element of any of those three groups into which I schematized the typical situation unconditionally takes the attitude characteristic of that curious phenomenon, so full of meaning and so rapidly passing, that is covered by the term Property. . . .
>
> Thus the capitalist process pushes into the background all those institutions, the institutions of property and free contracting in particular, that expressed the needs and ways of the truly "private" economic activity. Where it does not abolish" them, as it already has abolished free contracting in the labor market, it attains the same end by shifting the relative importance of existing legal forms—the legal forms pertaining to corporate business for instance as against those pertaining to the partnership or individual firm-by changing their contents or meanings. The capitalist process, by substituting a mere parcel of shares for the walls of and the machines in a factory, takes the life out of the idea of property. It loosens the grip that once was so strong—the grip in the sense of the legal right and the actual ability to do as one pleases with one's own; the grip also in the sense that the holder of the title loses the will to fight, economically, physically, politically, for "his" factory and his control over it, to die if necessary on its steps. And this evaporation of what we may term the material substance of propert y—its visible and touchable reality-affects not only the attitude of holders but also that of the workmen and of the public in general. Dematerialized, defunctionalized and absentee ownership does not impress and call forth moral allegiance as the vital form of property did. Eventually there will be ***nobody*** left who really cares to stand for it—nobody within and nobody without the precincts of the big concerns.[18]

Limited liability laws have produced the era of the huge, impersonal corporations that have produced unquestioned material prosperity, but at the same time these laws are now producing something very foreign to free enterprise. The giant socialist bureaucracy seems less threatening to men who have grownup in the midst of impersonal economic structures. They no longer are willing to fight for private property if that property is depersonalized. The drift into socialism

18. Joseph Schumpeter, *Capitalism, Socialism, and Democracy* (New York: Harper, 1950), pp. 141-142.

continues, for it is socialism, above all other systems, which destroya personal responsibility and removes power from ownership. The people have come to live with and even enjoy limited liability and multiple indebtedness. They have learned to use the bankruptcy laws, like the couple who went into debt to the university loan programs for over $8,000, and then went to the university for a $500 loan—to be used to declare bankruptcy![19] Socialism promises paradise to such people, and these are the people being produced by a society which denies human responsibility before God, and therefore has even less respect for human responsibility before men. Monetary inflation, multiple indebtedness, and limited liability are an unholy economic trinity; they are eroding the very foundation of Western culture.

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19. This is not a fictitious example. A friend of mine says that he was in the student loan office the day this couple made an application for their student loan. They did not. tell the loan officials what they planned to do with the money, of course. They knew him, and confided in him. He, like I, regarded it as legal, but immoral.