THE JOURNAL OF THE COMMITTEE ON MONETARY AND ECONOMIC REFORM

comer

$3.95 Vol. 20, No. 10 • OCTOBER 2008

CONTENTS

TRYPTYCH

Washington D-Day Goes and Comes Back

Washington is hard put to cope with the emergency that threatens to bring down the financial system of the US. Clearly the system suffers from a financial bureaucracy trained for over a century to respond to any major banking crisis in a double way: to bail out the banks from their losses, and to make further concessions to enable them to gamble bigger if not better.

The present emergency puts US legal tender under a big question mark. Since 1971 when the US (and the world with it) went off the gold standard), government debt was considered the last great immorality. However, with the departure from gold, central government debt became the only *legal tender*.

Yet, at the same time, commitments to be covered by adding to central government debt – no matter what they may be incurred for – were considered sinful. There has never been an election campaign for decades on either side of the border without the question being asked before TV cameras, how much the government debt will be reduced, or, better yet, completely retired? And we have yet to see any of the major party leaders trying to explain that without central government debt, the nation would have to resort to barter, or, still worse, depend on support by collateral debt usually of questionable merit.

Now this improvised subprime credit system has given way, and the US government apparatus has neither the know-how, nor the motivation to save the country's legal tender. Nor has the government apparatus been organized or educated to inform the public of where the country's legal tender and bank credit have gone and how they can be restored.

Listen to *The New York Times* express that dilemma (27/08, "D-Day Has Arrived for Congress" by Joe Nocera): "Just nine days ago – Thursday, September 18 – financial Armageddon was warded off when the word began to leak about the government's giant bailout plan. The news first broke ground around 2:10 pm when Bloomberg moved an article quoting Senator Charles E. Schumer, Democrat of New York, as saying the government was considering a 'permanent' plan to address the financial crisis.

"Then, less than an hour later, CNBC reported that an RTC – type plan was being readied by the Treasury Department. That did it. In the time between the Bloomberg article and the CNBC report, stock rose another 270 points. The Dow closed up 410 points.

"And by the time Treasury Secretary Henry M. Paulson Jr. made his big speech on Friday morning, laying out some of the details of the government's $700 billion bailout plan, a good deal of the pressure on the markets had eased. The credit-default swap spreads narrowed on Morgan Stanley and Goldman Sachs, meaning that the credit market was less worried about the possibility that they might default. "Morgan Stanley, which had been frantically negotiating a merger with Wachovia, stopped the negotiations. Money market funds, which had been hard hit by withdrawals earlier in the week, saw an inflow of money. Other indicators also suggested that the credit markets were unfreezing.

"Here we are a week later, and guess what? Armageddon is again approaching. All week

Continued on page 4

COMER

FOUNDING EDITOR
John Hotson 1930–1996
PUBLISHER–EDITOR
William Krehm
(comerpub@rogers.com)
CONTRIBUTORS Vol. 20, No. 10
Ian Angus, William Krehm, Richard Priestman, Keith Wilde
CARTOONIST
Allen Good
INFORMATION SECRETARY
Herb Wiseman (herbwise@cogeco.ca)
WEBMASTER
John Riddell

Economic Reform (ER)
(ISSN 1187–080X) is published monthly by COMER Publications
245 Carlaw Avenue, Suite 107
Toronto, Ontario M4M 2S6 Canada
Tel: 416-466-2642, Fax: 416-466-5827
Email: comerpub@rogers.com
Website: www.comer.org

COMER Membership: Annual dues (includes *ER* on request plus 1 book or video of your choice), in Canada CDN$50, foreign US$45

***Economic Reform* Subscription only:** One year, 12 monthly issues, in Canada CDN$30, Foreign US$35

Send request and payment to:
COMER Publications
245 Carlaw Avenue, Suite 107
Toronto, ON M4M 2S6

***ER* Back Issues:** CDN/US$4, includes postage; additional copies same issue, $2; additional issue same order, $3. Send requests for back issues to Herb Wiseman, 56 Robinson Street, Peterborough ON K9H 1E8.

Publications Mail Agreement 40018485.

Postmaster, please send address corrections to:
COMER Publications
245 Carlaw Avenue, Suite 107
Toronto, Ontario M4M 2S6

LAYOUT
Tony Koch (comer@pagecraft.org)
Pagecraft Computer Services

PRINTING AND DISTRIBUTION
Watt Solutions Inc., London

Printed in Canada on recycled paper.

The End of Wall Street?

In *The Wall Street Journal* (22/09, "The End of Wall Street") the title seemed to be missing a question mark. The piece deals with the device of the "holding company" that is being widely used to put financial corporations in control of those other "financial pillars" – which under F. D. Roosevelt had in 1933 been prohibited from acquiring any interest – stock brokerages, insurance and mortgage companies. For by doing so they had parlayed their cash resources applying the bank multiplier in turn to the cash reserves that these other "pillars" needed for their own businesses. This applied the "bank multiplier," the multiple of the cash actually in their coffers that they were able to lend out to a far broader base.

For that was the essence of the art of banking that made possible not only Europe's conquest of the planet, but also of skyscrapers of deceit with one-way elevators able only to rise at ever-accelerating speed. To descend from these giddy heights require ever greater disasters. Since we are in the midst of one just such, enjoy it to the fullest and even more important, learn from the experience what you can.

Roosevelt's restriction on what banks could do was set forth in the *Glass-Steagall* legislation. The formal removal of the *Glass-Steagall* legislation was achieved in August 2002 when the *Sarbanes-Oxley* law formally replaced the restrictions that with the years had become largely ignored. The immediate purpose of applying *Sarbanes-Oxley* to restructure the American banks appears in a recent piece in *The Wall Street Journal.* The present concern in applying the *Sarbanes-Oxley* legislation is to reshuffle the bank types to get the greatest amount of government assistance with the least possible degree of inspection from government agencies.

"'The world has changed,' said the Morgan Stanley spokesperson yesterday, and you can mark that down as the understatement of the year.

"She was explaining the company's decision late Sunday night to convert back into a bank holding company some 75 years after the *Glass-Steagall Act* sundered the House of Morgan into J. P. Morgan, the bank and Morgan Stanley, the investment firm. Under pressure from the Federal Reserve. Goldman Sachs made the same choice this weekend.

"And so, in a single week, the era of the independent investment bank has ended. Six months ago there were five major investment banks. Two – Lehman Brothers and Bear Stearns – have failed, Merrill Lynch is selling itself to Bank of America, and now the last two are becoming commercial banks.

"Both Morgan Stanley and Goldman Sachs will have two years in which to arrange their affairs to conform to the capital requirements and other rules that govern such commercial banks as Wells Fargo, BofA, and Citigroup. That will mean less leverage – assets that are perhaps 10 times their capital bases instead of the 20 or 30 to 1 they have sported as investment banks."

This every higher leverage of banks was one of the results of the weakening and then in the late 1990s, the complete abolition of the *Glass-Steagall* legislation. This made possible the takeover of the world economy by investment banking, jazzed up still further with derivative swaps and other devices that brought the world to its current plight.

In Search of Consumer Deposits

In exchange, the retailored banks "will be able to accept *consumer* savings deposits as a ready source of funds" – their great problem today. They also get the promise of greater stability and continued access to the Federal Reserve lending facilities such as the discount window.

To be more pointed, they'll have a better chance of survival, not least because they also will be able to avoid certain "mark-to-market" accounting rules that have forced write-downs on troubled securities. Bank accountancy, that kept the original cost on the books as part of a bank's capital – as we have often emphasized over the years – has been one of the basic fictions of bank accountancy that turned the alleged capital of banks that were deregulated to conquer the world, into an inevitable source of the nasty surprises that the world is currently experiencing.

"This year's market turmoil had called into question the viability of the investment banking business model as far back as March, with Bear Stearn's collapse. The Fed gave the remaining banks access to emergency lending, but it was clear from the start that this taxpayer lifeline wasn't sustainable without a greater degree of federal oversight. What Morgan Stanley and Goldman did Sunday night was to choose their poison – committing themselves to commercial banking regulation rather than have it imposed on them either through legislation or merger, as Merrill Lynch recently chose to do in submitting to takeover by the BofA.

"The result will be a sturdier, but also less innovative financial system than we have had in recent decades. That has its benefits; we're paying the price for some of the more dubious innovations right now. Direct lending is highly efficient and has provided funds for many useful ends. But it is also riskier in a panic because it lacks a capital cushion to absorb the losses when capital values decline. In another sign of the new world, Morgan Stanley followed the weekend's news by announcing it had sold a 20% stake to Japan's Mitsubishi.

"In some sense, the pure-play investment bank was itself a regulatory artifact: in the depths of the Depression, separating the investment functions from the banks was considered necessary for the stability of the commercial banks. Thus *Glass-Steagall* was born, and this week that separation can finally be said to be undone."

However, those ever-rising skyscrapers of cash reserves meant for non-banks, and served by elevators going only up at ever greater speed in order not to fall and crash, really have nowhere to go except in pursuit of military options. Even our mega bankers can no longer go on getting bigger if not better. The rest of us must also rethink the official creed that has brought us into so unholy a mess.

W.K.

TRYPTYCH

Bringing in Government Investment in Human and Environmental Capital to Fill the Gap in Purchasing Power Needed by Both the Banks and Society

The problem that we are up against is the lack of solvent credit to get both our banking system and our society functioning again. From our record in every instance except a single one in the rejigging of the banking system from their mammoth speculative losses, the banks have always emerged not only bailed out at public expense, but headed for the next bailout with further empowerment over the government and society. The one exception was the bailout of 1933, and that was uniquely restrictive rather than a bailout cum surrender to the banks. The reason for that exception was that by the time Roosevelt was inaugurated for his first term, the banks were simply *hors combat* – 9,000 US banks had shut their doors one of the first things Roosevelt did was to declare a bank moratorium that lasted a month.

In every other instance of a major bank bailout from their losses, they have emerged from the crisis with further power over the government and its treasury and central bank. In that way everything was in place for the banks to resume its gambles on a more monumental scale.

We Stand at a Crossroad

We stand at such a crossroad in the present subprime crisis. But the means of heading it off is by resurrecting the buried work of some of our great economists.

The baffling problem in getting the banks out of their trouble today is the need for perfectly solvent purchasing power both for the commercial banks and society as such. And one of the most valuable lessons that came out of the great sacrifices of World War II was the key importance of investment in human and environmental capital for which Theodore Schultz was briefly celebrated and then utterly forgotten. For what he had discovered clashed with the politically ever-more-powerful investment banks that had taken over.

Schultz had been one of hundreds of young economists sent to Japan and Germany at the end of WWII to study the damage inflicted on the two major defeated powers and predict how long it would be before they could emerge as formidable trade competitors again. Two decades later Schultz published a series of papers pointing out the reason for the incorrect forecasts he and his colleagues of that day had made. They had concentrated on the material destruction and overlooked that the highly educated and dedicated work force of the two great defeated powers had come out of the war virtually intact. From that he concluded that investment in human capital was the most productive investment a government can make.

And that implied, of course, that everything that protects the vessels in which this key investment is kept also belongs to this same top productive category. This provides our governments and our countries today with a way out of the banking crisis that baffles the experts in charge seeking s solution to the multiple problems that have beset both our banks and the societies they have become accustomed to feast upon.

But first, we must remember how the concepts of serious double-entry accountancy had been extended in 1996 in the US and in 2002 in Canada. In the 1980s the banks of the United States in particular were allowed to take over the Savings and Loans. Eventually they had to be bailed out at a cost to the taxpayers of some 1.4 trillion dollars.

To replace the loss of so much capital the Bank for International Settlements – a sort of central bankers' club based in Switzerland that served as a war-room for the banks to plan a comeback to the glory – days before 1929. In 1988 BIS declared the debt of developed countries risk-free and hence requiring no down-payment for banks to acquire. In Canada, as a result of this, our banks increased their holdings of government debt from $20 billion to $80 billion without putting up any money of their own. At the same time BIS shoved interest rates to the highest ever to flatten out prices for all time to come – to kill inflation stone-dead. But two things had escaped the attention of the BIS.

Not all price increase is inflationary – i.e., due to an excess of demand over supply. Nobody about to move from a town of 20 thousand to New York City is idiot enough to expect that his living costs will remain the same. How then could prices stay flat, when society makes precisely the same move? And when modern technology requires a university education where a couple of generations a primary education and a bit of a secondary one would do? And the sky-high interest caused the value of the pre-existent bond hoards the banks had loaded up with nothing down thus shriveled in value. This got through to the Clinton government the message that the days of high interest rates were over.

Violating Principles of Accountancy

And then the US Treasury did a most cunning thing. Up to that point when governments pretty well throughout the world made a physical capital investment, they carefully "amortized" the debt incurred over the likely useful life of the investment, but depreciated the asset value of the investment itself in a single year. The result was that it violated the principle of double-entry bookkeeping and showed a deficit that was simply not there. Not only did this help keep spending on social programs to a minimum, but with valuable capital assets on the books at a token single dollar it made possible some stunning privatizations that have become much sought after by international financial giant corporations.

As of 1996 the US government started depreciating its physical capital investments over a period closer to its useful life. But this was not called "investment" but "savings," which it was not since savings implied cash or securities readily exchanged for cash, and many of the assets referred to might be 100-year old buildings, roads, buildings, bridges. Be that as it may, carried back to 1959, the conversion from "cash" to "accrual accountancy" or "capital budgeting," brought to the books something like $1.3 trillion dollars. A wink and a nudge to the appraising agency got the point across. The result was a period of low interest rates, that gave Clinton his second term and prolonged the high-tech stock market boom until the 2000 bust.

But that still left out in the cold the investment in human capital, that Theodore Schultz had found on the basis of the wrong forecasts of his and his numerous colleagues had may of the prospects of Germany and Japan becoming powerful competitors on world markets once again.

With the proper depreciation of physical capital investments straightened out, extending the concept to human capital is cookie cutter stuff. It requires the same treatment as the necessary depreciation of physical capital by government, but if anything to a greater degree. For the advantages of investment by government in human capital extends beyond a single generation. The children of physically healthier parents are likely to be more healthy, the children of better-educated parents are likely to be better educated, and better adjusted. And children raised in a better preserved environment are likely to be in better peace with themselves.

So what we have here is the means of increasing savings that our banks stand in desperate need of to make saving banks more independent of the high leverage and the speculative gains of investment banks. Instead of turning our backs on the *Glass-Steagall* bank reforms and embracing the *Sarbanes-Oxley* model, it is a return to the *Glass-Steagall* restraints on banks getting into the other financial pillars that is desperately needed – and within our grasp. And with the revival of what Schultz and World War II taught us there will be plenty of authentic homespun savings around to cut the adventurous leverages of deregulated and globalized banking drastically.

The missing item is the recognition of the key importance of human capital investment, which, of course, includes saving and restoration of the environment. That will make feasible in a vast liberating way the stunted creativity of re-empowered democracies.

William Krehm

Washington *from page 1*

long, the credit-default swap spreads on Morgan Stanley widened until by Friday, they actually rose. By then they were at the same level as during the previous week. (And this time, the chief executive, John J. Mack, cannot blame the short sellers for his troubles, since short-selling in financial stocks has been temporarily banned.)"

Armageddon Returns for Another Bow

"On Thursday, investment-grade loans were trading lower than junk bonds, because investors were selling off their most liquid assets to raise capital. Wachovia, the nation's fifth-largest bank holding company, suddenly appeared in deep trouble. 'Wachovia is trading as if it's going to fail.' Dave Klein, a manager at Credit Derivatives research said on Friday. Washington Mutual was seized by the government. The markets may not be as panicked as they were last week, but with every passing day, the situation is getting increasingly dangerous.

"Last week I wrote a column suggesting that the Paulson plan was unlikely to fix the enormous problems facing the country's faltering economy. I am still not sure it will work – but this week I have a different more urgent concern.

"We're running out of time.

"I know there is something tremendously galling about the prospect of Americans putting $700 billion – or more – of their tax dollars at risk to come to the aid of banks and investment banks whose reckless behavior has so damaged the country. They gamed the system. They lined their pockets. They made terrible, terrible mistakes about it."

However, Mr. Nocera and his editor should tell the complete tale of how the banks had brought a decade of deep depression onto the world and their land. By the time President Franklin Roosevelt was inaugurated for his first term in January 1933, 9,000 banks had shut their doors, and the new president, after declaring a bank moratorium that lasted a month, brought in the *Glass-Steagall Act* that prevented banks from acquiring interests in other financial "pillars," i.e., stock brokerages, insurance and mortgage firms. That plus government deposit insurance for bank deposits, allowed the banks decades of useful banking. But by 1959 the banks were sufficiently restored to hanker after the grand financial adventures that helped bring on the Depression. But these lessons were forgotten and Rooseveltian laws still on the books were more and more ignored.

There is a moral obligation for the leading press and our universities to tell the complete tale, including the teachings of dozens of great economists of the postwar whose life's work had to do with Depressions and how they can be avoided. However, all this has been completely suppressed.

That is missing in the *Times* coverage of the mess that Washington is making of the current breakdown of a system that cannot fill the bill. Even the casual reader today worries about his job, his home, and perhaps his children's university fees. He should also be scandalized to note that had the *Glass-Steagall* law passed under Roosevelt been kept on the books and applied, there could have been no subprime mortgages, no subprime banks, insurance companies, and subprime universities, let alone subprime governments that depend on former high officials of the corporations that created the deep trouble to lead the country onto dry land again.

W.K.

The Myth of the Tragedy of the Commons

From The Bullet*, a Socialist Project e-bulletin, No. 133, August 25, 2008*

Will shared resources always be misused and overused? Is community ownership of land, forests and fisheries a guaranteed road to ecological disaster? Is privatization the only way to protect the environment and end Third World poverty? Most economists and development planners will answer "yes" – and for proof they will point to the most influential article ever written on those important questions.

Since its publication in *Science* in December 1968, "The Tragedy of the Commons" has been anthologized in at least 111 books, making it one of the most-reprinted articles ever to appear in any scientific journal. It is also one of the most-quoted: a recent Google search found "about 302,000" results for the phrase "tragedy of the commons."

For 40 years it has been, in the words of a World Bank Discussion Paper, "the dominant paradigm within which social scientists assess natural resource issues" (Bromley and Cernea 1989: 6). It has been used time and again to justify stealing indigenous peoples' lands, privatizing health care and other social services, giving corporations "tradable permits" to pollute the air and water, and much more.

Noted anthropologist Dr. G.N. Appell (1995) writes that the article "has been embraced as a sacred text by scholars and professionals in the practice of designing futures for others and imposing their own economic and environmental rationality on other social systems of which they have incomplete understanding and knowledge."

Like most sacred texts, "The Tragedy of the Commons" is more often cited than read. As we will see, although its title sounds authoritative and scientific, it fell far short of science.

Garrett Hardin Hatches a Myth

The author of "The Tragedy of the Commons" was Garrett Hardin, a University of California professor who until then was best-known as the author of a biology textbook that argued for "control of breeding" of "genetically defective" people (Hardin 1966: 707). In his 1968 essay he argued that communities that share resources inevitably pave the way for their own destruction; instead of wealth for all, there is wealth for none.

He based his argument on a story about the commons in rural England.

(The term "commons" was used in England to refer to the shared pastures, fields, forests, irrigation systems and other resources that were found in many rural areas until well into the 1800s. Similar communal farming arrangements existed in most of Europe, and they still exist today in various forms around the world, particularly in indigenous communities.)

Where's the evidence?

"Picture a pasture open to all," Hardin wrote. A herdsmen who wants to expand his personal herd will calculate that the cost of additional grazing (reduced food for all animals, rapid soil depletion) will be divided among all, but he alone will get the benefit of having more cattle to sell.

Inevitably, "the rational herdsman concludes that the only sensible course for him to pursue is to add another animal to his herd." But every "rational herdsman" will do the same thing, so the commons is soon overstocked and overgrazed to the point where it supports no animals at all.

Hardin used the word "tragedy" as Aristotle did, to refer to a dramatic outcome that is the "inevitable but unplanned result of a character's actions." He called the destruction of the commons through overuse a tragedy not because it is sad, but because it is the inevitable result of shared use of the pasture. "Freedom in a commons brings ruin to all."

Given the subsequent influence of Hardin's essay, it's shocking to realize that he provided "no evidence at all" to support his sweeping conclusions. He claimed that the "tragedy" was inevitable – but he didn't show that it had happened even once.

Hardin simply ignored what actually happens in a real commons: "self-regulation by the communities involved." One such process was described years earlier in Friedrich Engels' account of the "mark," the form taken by commons-based communities in parts of pre-capitalist Germany: "The use of arable and meadowlands was under the supervision and direction of the community….

"Just as the share of each member in so much of the mark as was distributed was of equal size, so was his share also in the use of the 'common mark.' The nature of this use was determined by the members of the community as a whole….

"At fixed times and, if necessary, more frequently, they met in the open air to discuss the affairs of the mark and to sit in judgment upon breaches of regulations and disputes concerning the mark" (Engels 1892).

Historians and other scholars have broadly confirmed Engels' description of communal management of shared resources. A summary of recent research concludes: "What existed in fact was not a 'tragedy of the commons' but rather a triumph: that for hundreds of years – and perhaps thousands, although written records do not exist to prove the longer era – land was managed successfully by communities" (Cox 1985: 60).

Part of that self-regulation process was known in England as "stinting" – establishing limits for the number of cows, pigs, sheep and other livestock that each commoner could graze on the common pasture. Such "stints" protected the land from overuse (a concept that experienced farmers understood long before Hardin arrived) and allowed the community to allocate resources according to its own concepts of fairness.

The only significant cases of overstocking found by the leading modern expert on the English commons involved wealthy landowners who deliberately put too many animals onto the pasture in order to weaken their much poorer neighbours' position in disputes over the enclosure (privatization) of common lands (Neeson 1993: 156).

Hardin assumed that peasant farmers are unable to change their behaviour in the face of certain disaster. But in the real world, small farmers, fishers and others have created their own institutions and rules for preserving resources and ensuring that the commons community survived through good years and bad.

Why does the herder want more?

Hardin's argument started with the unproven assertion that herdsmen always want to expand their herds: "It is to be expected that each herdsman will try to keep as many cattle as possible on the commons…. As a rational being, each herdsman seeks to maximize his gain."

In short, Hardin's conclusion was predetermined by his assumptions. "It is to be expected" that each herdsman will try to maximize the size of his herd – and each one does exactly that. It's a circular argument that proves nothing.

Hardin assumed that human nature is selfish and unchanging, and that society is just an assemblage of self-interested individuals who don't care about the impact of their actions on the community. The same idea, explicitly or implicitly, is a fundamental component of mainstream (i.e., pro-capitalist) economic theory.

All the evidence (not to mention common sense) shows that this is absurd: people are social beings, and society is much more than the arithmetic sum of its members. Even capitalist society, which rewards the most anti-social behaviour, has not crushed human cooperation and solidarity. The very fact that for centuries "rational herdsmen" did not overgraze the commons disproves Hardin's most fundamental assumptions – but that hasn't stopped him or his disciples from erecting policy castles on foundations of sand.

Even if the herdsman wanted to behave as Hardin described, he couldn't do so unless certain conditions existed.

There would have to be a market for the cattle, and he would have to be focused on producing for that market, not for local consumption. He would have to have enough capital to buy the additional cattle and the fodder they would need in winter. He would have to be able to hire workers to care for the larger herd, build bigger barns, etc. And his desire for profit would have to outweigh his interest in the long-term survival of his community.

In short, Hardin didn't describe the behaviour of herdsmen in pre-capitalist farming communities – he described the behaviour of "capitalists operating in a capitalist economy." The universal human nature that he claimed would always destroy common resources is actually the profit-driven "grow or die" behaviour of corporations.

That leads us to another fatal flaw in Hardin's argument: in addition to providing no evidence that maintaining the commons will inevitably destroy the environment, he offered no justification for his opinion that privatization would save it. Once again he simply presented his own prejudices as fact: "We must admit that our legal system of private property plus inheritance is unjust – but we put up with it because we are not convinced, at the moment, that anyone has invented a better system. The alternative of the commons is too horrifying to contemplate. Injustice is preferable to total ruin."

The implication is that private owners will do a better job of caring for the environment because they want to preserve the value of their assets. In reality, scholars and activists have documented scores of cases in which the division and privatization of communally managed lands had disastrous results. Privatizing the commons has repeatedly led to deforestation, soil erosion and depletion, overuse of fertilizers and pesticides, and the ruin of ecosystems.

As Karl Marx wrote, nature requires long cycles of birth, development and regeneration, but capitalism requires short-term returns.

"The entire spirit of capitalist production, which is oriented towards the most immediate monetary profits, stands in contradiction to agriculture, which has to concern itself with the whole gamut of permanent conditions of life required by the chain of human generations. A striking illustration of this is furnished by the forests, which are only rarely managed in a way more or less corresponding to the interests of society as a whole…" (Marx 1998: 611n).

A Politically Useful Myth

Contrary to Hardin's claims, a community that shares fields and forests has a strong incentive to protect them to the best of its ability, even if that means not maximizing current production, because those resources will be essential to the community's survival for centuries to come. Capitalist owners have the opposite incentive, because they will not survive in business if they don't maximize short-term profit. If ethanol promises bigger and faster profits than centuries-old rain forests, the trees will fall.

This focus on short-term gain has reached a point of appalling absurdity in recent best-selling books by Bjorn Lomborg, William Nordhaus and others, who argue that it is irrational to spend money to stop greenhouse gas emissions today, because the payoff is too far in the future. Other investments, they say, will produce much better returns, more quickly.

Community management isn't an infallible way of protecting shared resources: some communities have mismanaged common resources, and some commons may have been overused to extinction. But no commons-based community has capitalism's built-in drive to put current profits ahead of the well-being of future generations.

The truly appalling thing about "The Tragedy of the Commons" is not its lack of evidence or logic – badly researched and argued articles are not unknown in academic journals. What's shocking is the fact that "this" piece of reactionary nonsense has been hailed as a brilliant analysis of the causes of human suffering and environmental destruction, and adopted as a basis for social policy by supposed experts ranging from economists and environmentalists to governments and United Nations agencies.

Despite being refuted again and again, it is still used today to support private ownership and uncontrolled markets as sure-fire roads to economic growth.

The success of Hardin's argument reflects its usefulness as a pseudo-scientific explanation of global poverty and inequality, an explanation that doesn't question the dominant social and political order. It confirms the prejudices of those in power: logical and factual errors are nothing compared to the very attractive (to the rich) claim that the poor are responsible for their own poverty. The fact that Hardin's argument also blames the poor for ecological destruction is a bonus.

Hardin's essay has been widely used as an ideological response to anti-imperialist movements in the Third World and discontent among indigenous and other oppressed peoples everywhere in the world.

"Hardin's fable was taken up by the gathering forces of neo-liberal reaction in the 1970s, and his essay became the 'scientific' foundation of World Bank and IMF policies, viz. enclosure of commons and privatization of public property…. The message is clear: we must never treat the earth as a 'common treasury.' We must be ruthless and greedy or else we will perish." (Boal 2007)

In Canada, conservative lobbyists use arguments derived from Hardin's political tract to explain away poverty on First Nations' reserves, and to argue for further dismantling of indigenous communities. A study published by the influential Fraser Institute urges privatization of reserve land: "These large amounts of land, with their attendant natural resources, will never yield their maximum benefit to Canada's native people as long as they are held as collective property subject to political management… collective property is the path of poverty, and private property is the path of prosperity" (Fraser 2002: 16-17).

This isn't just right-wing posturing. Canada's federal government, which has refused to sign the United Nations Declaration on the Rights of Indigenous Peoples, announced in 2007 that it will "develop approaches to support the development of individual property ownership on reserves," and created a $300 million fund to do just that.

In Hardin's world, poverty has nothing to do with centuries of racism, colonialism and exploitation: poverty is inevitable and natural in all times and places, the product of immutable human nature. The poor bring it on themselves by having too many babies and clinging to self-destructive collectivism.

The tragedy of the commons is a useful political myth – a scientific-sounding way of saying that there is no alternative to the dominant world order.

Stripped of excess verbiage, Hardin's essay asserted, without proof, that human beings are helpless prisoners of biology and the market. Unless restrained, we will inevitably destroy our communities and environment for a few extra pennies of profit. There is nothing we can do to make the world better or more just.

In 1844 Friedrich Engels described a similar argument as a "repulsive blasphemy against man and nature." Those words apply with full force to the myth of the tragedy of the commons.

Ian Angus

Ian Angus is editor of *Climate and Capitalism,* www.climateandcapitalism.com, and an associate editor of *Socialist Voice*, www.socialistvoice.ca.

A Skyscraper Project with an Elevator that Must Always Rise Ever Faster

It's is a long and winding tale like the road to Tipperary, but with the bridges all down, and the facts buried deeply without markers to remind us of them. And that is the main reason why we have difficulty in coping with our present problems – we have officially no access to this crucial past.

The 1920s were years of recovery and financial boom. So much so that shoe-shine boys on Wall Street were in the stock market, and gave their clients hot market tips as they shined their shoes. High executives of leading corporations wrote articles for ladies' magazines saying that there was no reason why all Americans should not end up as millionaires. And then suddenly with little advance notice Wall Street had crashed, brokers were jumping out of windows of top floors of buildings and the breadlines in Lower Manhattan three abreast circled entire city blocks to get to the charity handouts. And it stayed that way for a good four years without very much coherent or really relevant ideas having to do with understanding why the boom so suddenly had turned into a bust. By the time F. D. Roosevelt was inaugurated for his first term as president in January 1933, one of the new president's first acts was to declare a bank moratorium that extended for an entire month. During the 1920s few social service organizations existed for such emergencies, that were simply declared non-existent under a free market. Roosevelt had no great knowledge of economics, but was a humane person who had open ears for almost anyone with a view of how the world could work its way out of the Depression. He listened to them all, brought in bank deposit insurance so that banks could be entrusted with the savings of the relatively few folks who still had jobs. And in the same year new banking legislation was passed by Congress that set the guiding principles that banks had to observe in the US. The basic principles of this is never referred to in attempting to understand the present troubles that have hit the world's banks and economy today. That is not because they have no relevance to our current difficulty, but, on the contrary, precisely because they have.

For banking laws are the hooks from which hang the keys to society's wealth and to its acquisition. Like all near-magic, its powers are too immense not to be abused. Yet, properly controlled, banking has unquestionably contributed to society's development. The origins of precious metal coins in Asia Minor seem to have had more to do to do with religious and social rites of different communities than with commercial activities. A neighbouring community – possibly even speaking a different language, would give gold or silver to another community as a sign of good will. It was expected, even though that was not even uttered, that it would be reciprocated. Failing which, the failure of this to happen would be a declaration of unfriendliness and even a cause for warfare.

When Monarchs Duelled for Lack of Money

Under the Romans money expanded fully into its monetary role. "Money," in fact, derives from the Semitic word for "counting."

But with the collapse of the Roman Empire even the art of mining was forgotten. and for several centuries no mining took place in Europe. What gold and silver circulated was largely dug up in graves of eminences, and usually ended up in churches dedicated to the Lord. During these centuries, gold and silver coins fell almost wholly out of use. All activities that required hiring people disappeared except in the most rudimentary form. If two states were at war, that was often handled by a duel of monarchs, for lack of the wherewithal to pay armies. Likewise police and school teachers. The excellent Roman Roads that perdured – were infested with brigands. Of this we have reminders in the very language we speak today. Our word for "slave" comes not from the Latin which is "servus" but for the name of many of the tribes who were pouring in from Asia – slaves – the slavs. These were used not only for the heavy work of those who bought them, but served as currency to ease the exchange of other items.

It was only when the discovery of the lost art of silver mining in Germany in the 8th century, I believe – as distinguished from gold which continued being panned in Africa – that commerce resumed with great difficulty. The Roman roads were still intact, but were infested by brigands. The merchant travelled with his goods which was dangerous enough, but to carry gold or silver would be suicidal. So the practice spread of leaving with a trusted goldsmith say in Milan the proceeds of a Dutch wool merchant of a load of wool to a cloth-maker in Lombardy. What the merchant would take back with him was a credit note from the Milanese goldsmith which he could use in redeeming a credit left in Amsterdam with another goldsmith that had the confidence of the Milanese goldsmith.

It was in this way that the art of banking was cradled, though it called for much nursing and care. In good time such a goldsmith in the process of evolving into a banker would note that in his coffers he had a lot of idle precious coins. Could he not lend them out at interest, without their rightful owner even realizing what he had done? If he was very conscientious, he could even split the interest he earned in this way with the rightful owner. But what was not an option was lending out too much of other folks' money left with him in trust. If that happened the game was up in the most disastrous way. For his credibility was gone.

There was never enough silver from Europe's own mines or gold from Africa to support the vast explorations that opened up so much of the rest of the planet to Europeans. It was banking that arranged the bridging of the shortcoming that unleashed floods of precious metals to bridge the gap.

By the 17th century banking was well established as the means of financing the wars that accompanied the consolidation of the great European countries. The coining and, no less important, the clipping with decreased precious metal content became the privilege of the Crown. When the Crown did that, historians used to consider an abuse. Modern historians tend to see it as a form of taxation, easier on what was a largely illiterate population.

Professional bankers showed themselves brighter from the beginning than the British Crown, even though it had Isaac Newton in charge of the Mint during a crucial period. Thus the Anglo-Dutch company that obtained its bank charter and was immediately given the right to recoup what it had paid the Crown for its Charter through an issue of paper money, and on top of that the debt of the government to the Charter bank made available to it at the bank's opening remained valid. Either there was corruption involved, or the Crown's advisers brought to their task an excess of professional stupidity.

However, for our immediate purposes, the important thing to note is that the monopoly of the Crown in issuing legal tender has some very solid historical antecedents. People caught infringing it, were in a sense lucky if they paid for their encroachment with having a hand rather their head chopped off. Amazing then that we shall see our banks not only get bailed out of their ever increasing gambling losses, but in addition are then further deregulated to equip them to gamble bigger if not necessarily better.

That pattern had already asserted itself in the 1920s, and brought on the stock market crash of October 1929. By the time F. D. Roosevelt was inaugurated for his first term in 1933, and one of the new president's first acts was to declare a bank moratorium that lasted a month.

Shortly after, new banking legislation was brought in that explicitly forbade banks to acquire an interest in the "other financial pillars," i.e., at the time, stock brokerages, insurance, and mortgage institutions. The reason by then was clear: each of these other financial pillars maintained a cash reserve to cover the needs of their own industry. Allow the banks to acquire an interest in, or an entire corporation in the non-banking pillars, and they will lose no time in using the cash reserves thus acquired through the non-banking pillars, mingling them with their own cash base for the application of the banking multiplier as developed by the banks' goldsmith ancestors. At the end of World War II that multiplier stood at approximately 10:1. But by the end of World War II, our banks had regained their liquidity under the strict regime imposed on them, and had began languishing after the free scope of activities that had brought on the Great Depression.

The Other Financial Pillars Barred to Banks

One by one the restrictions on the banks entering these other pillars were removed. And as this occurred the banks took over the other financial pillars one after another, and the distinction between legal tender issued by the central bank was weakened and eventually entirely lost.

At this point I would urge my audience to perk up their ears carefully because I will mention a couple of background stretches that never turn up in the coverage by our media and other seekers after solutions of the current financial mess.

1. In 1938 thanks to the insights and dedications of a remarkable high school – drop-out in Vancouver, who pressured Mackenzie King, the Liberal Prime Minister on the matter, the Bank of Canada was nationalized.

This goes much farther than John Maynard Keynes ever went. At the time, Keynes was still suggesting that the use of interest rates alone might do the job. That step put Canada in a near-unique position internationally in financing necessary infrastructures during the Depression on a near-interest-free basis. That conclusion is obvious enough: as sole shareholder of the BoC since 1938, the financing of infrastructure through the BoC would bring the interest paid on its debt to the BoC back to it as dividends less some handling costs to the BoC. This made possible Canada's financing her WWII on a considerably lower rate than either the US or the UK whose central banks during the war were privately owned.

Apart from the considerably lower financing costs, the government ownership of the central bank, this arrangement kept clearly separated the credit of the central bank which since 1971 when the US and hence the world went off the gold standard, there was less mingling of what has become the sole legal tender along with whatever other bank securities the banks had accumulated during their business operations. Obviously this has made its contribution to the problem of subprime collateral that is currently plaguing the economy.

2. The cash and "near-cash" reserves of the "other financial pillars" that with the progressive deregulation banks were allowed to acquire would likewise include supposedly short-term investments as well as non-interest-paying cash. This also brought into the legal tender of the land a strain of potentially subprime investments that have contributed to the present mess.

But these aspects of the deregulation process were secondary alongside the basic structural one.

Whether the purest legal tender or subprime, the construct resulting from the breach of the ban on the banks acquiring interests in the "non-banking financial pillars" results in a structure of assets dedicated to growth at an ever accelerating rate. The inevitable result is a forced emulsion of legal tender and subprime that is under unrelenting pressure to grow ever more quickly. Today's achievements are judged not by whether the equalled yesterday's but how much more quickly it shot up beyond it. For this is the age of derivatives which it is the rate of increase over yesterday's achievement.

That is the mathematics of the exponential curve that is also that of the atomic bomb. As early as 1988 it had already brought one hedge fund organized by decorated laureates, who obviously had no understanding that mathematics *per se* have no empirical content, but are a most powerful *means* of analysis.

What results is a skyscraper of growth each floor inserted over the other, with an elevator perpetually accelerating, which can only ascend.

Clearly that leaves the world with only a military option, for though that is a gamble it still has a gambler's chance of a stroke of luck whereas, as a peaceful economic project, success must eventually be recognized as excluded.

William Krehm

Beware of False Friends

Gerald McGeer, MP: "Why should a government with the power to create money give that power away to a private monopoly? And especially, why should it then borrow from the banks and pay interest?"

Graham Towers, Governor, Bank of Canada: "Parliament can change the way the banking system operates if it wishes to do so."[1]

The foregoing exchange is from the 1939 Parliamentary committee proceedings to discuss the first annual report of the Bank of Canada to the Government. It encapsulates an issue that has festered among groups with an interest in the nature of money and credit since at least the Great Depression days following the virtual collapse of an over-extended banking system. Money Reformers in general are incensed by the power of banks and want governments to issue money directly. The American Monetary Institute spearheaded by Stephen Zarlenga is a contemporary exemplar of this position. Zarlenga has produced a substantial book to support his call for a fourth branch of government to be in charge of "100 percent money." Other proponents of government against bankers are not so thorough in their advocacy and sometimes get inflamed by arguments that are half-baked superstitions based on fragments of "evidence "that do not make the case.

One of these inflammatory arguments is that Abraham Lincoln was assassinated by a conspiracy of international bankers who feared that he was about to curb their power over money and credit by putting the United States on a fiat, paper money standard. Lincoln had in fact been forced to issue Notes based on "the credit of the United States government" (by an Act of 1862) instead of on the promise to redeem in gold, in order to finance the Civil War. "Sound money" men opposed this and "greenbacks" did not become the norm in US monetary policy. They continued to have advocates, however, throughout the remainder of the 19th century. They were favored by people who believed that inflation is a better climate for prosperity than is deflation, and they were joined in this attitude by advocates of bimetallism. The latter was actually official policy for some time, and it means that silver as well as gold were recognized as monetary standards, a silver dollar being defined as a certain weight and fineness of the white metal. Bimetallism was favored by those who believed that there was not enough gold in the country to serve as the basis of a sufficient money supply to support a growing level of commerce. Also, of course, by people in the silver mining and refining business (depending on the price of silver for non-monetary purposes).

Whether or not Lincoln was assassinated by a conspiracy of international bankers is a question I will leave to those who find it interesting. It has spawned a more recent conspiracy theory, however, which is much easier to debunk. This one is that John F. Kennedy was assassinated by the same gang of thieves because he dared to commit the same monetary heresy as Lincoln. Unfortunately for the campaign of the Canadian Action Party, a version of this conspiracy theory was circulated widely in August of this year. The article is signed by one John P. Curran as of April 2007 and may be consulted at www.rense.com/general76/jfkvs.htm.

In Search of Exciting Fiction

The opening paragraph reads as follows: "On June 4, 1963, a virtually unknown Presidential decree, Executive Order 11110, was signed with the authority to basically strip the Federal Reserve Bank of its power to loan money to the United States Federal Government at interest. With the stroke of a pen, President Kennedy declared that the privately owned Federal Reserve Bank would soon be out of business. The Christian Law Fellowship has exhaustively researched this matter through the Federal Register and Library of Congress. We can now safely conclude that this Executive Order has never been repealed, amended, or superceded by any subsequent Executive Order. In simple terms, it is still valid."

Every sentence of the foregoing is false. Kennedy did sign EO 11110 on the said date, but the intent and effect was not at all what the author claims. The research claimed by the Christian Law Fellowship is either woefully incompetent or a deliberate lie. The said Executive Order has been in fact revoked. Furthermore, it would not have had the effect of emasculating the Federal Reserve System even if it were still in force. The author was ignorant of big elements of US monetary history and did not know how to read the documents.

The Executive Order itself may be read at www.presidency.ucsb.edu/ws/index.php?pid=59049&st=&st1=.

The conspiracy theorists do reproduce its text accurately in observing that it gave the Treasury Department the explicit authority: "to issue silver certificates against any silver bullion, silver, or standard silver dollars in the Treasury." This means that for every ounce of silver in the US Treasury's vault, the government could introduce new money into circulation based on the silver bullion physically held there.

Accuracy ends there, however, for in his next breath the author says that this brought into being a substantial issue of United States Notes! If it were so, it contravened the Order, which called for issuance of Silver Certificates. If United States Notes were in fact issued after June 4, 1963, it had nothing to do with this particular Order. The author obviously did not know the difference between Silver Certificates and United States Notes, or he was deliberately making a big lie and depending on the ignorance of readers (too often a successful tactic). He does say that the amount of currency issued after the Order was about $4 billion. That would be a believable figure if the currency was actually Silver Certificates rather than United States Notes, for the amount of silver in the Treasury is acknowledged to be limited. That fact of physical limitation is why EO 11110 was never a threat to the dominance of the Fed. It is a picayune quantity compared to the total money and credit supply, even that many decades ago. The U.S Treasury had silver in its vaults probably as a carryover from days when the government was obliged by law to purchase a limited quantity of silver every year, if offered by suppliers, under the 19th century policy of bimetallism.

The author compounds his error in the next paragraph by asserting that "United States Notes were issued as an interest-free and debt-free currency backed by silver reserves in the US Treasury." It is highly unlikely that this statement was ever true because of the existence of Silver Certificates that were so backed. It seems from his other statements that the author has never seen a Silver Certificate, which suggests that he isn't very old. I lived in the United States for about twelve years between 1955 and 1973 during which time I was conscious that the currency in my pocket could be labeled any one of Silver Certificate, United States Note or Federal Reserve Note, although the latter were by far the most common. I was introduced early to the distinction by university courses in US economic history and its money and banking institutions, and as a consequence I had an interest in examining the contents of my billfold from time to time.

I have not seen a Silver Certificate for a long time, on infrequent visits to the US, and it seems plausible that by this time they would all have been redeemed as the price of silver for industrial purposes rose to exceed its value as money. (If you have ever priced a silver dollar from coin collectors or a mint you will get the idea.) For the same reason, silver producers would not have been bringing their metal to the Treasury even if the Silver Purchase Acts were still in force. United States Notes are a fiat currency, the successors of Lincoln's greenbacks. In this respect the money reformers are correct, although one of my American correspondents tells me that at some times in the past the Notes have been redeemable in gold. That cannot be anymore, of course, since the United States cancelled its commitment to redeem its currency in gold, in 1971.

As I was thinking about the preparation for this rant, I encountered some evidence that the preposterous idea of Kennedy's assassination because of Silver Certificates may be due to the ignorance of authors rather than vicious mendacity. While browsing idly in a professor's office last week I picked up a copy of *A New Economic History of America,* published in 1976 and written by Gerald Gunderson. If it is typical of such history texts published since 1975 then the blame should lie with a failure of education programs. A brief section on the money supply between the end of the Civil War and the initiation of the Federal Reserve System makes no mention of bimetallism and the silver issues. Those words do not even appear in the index, let alone any mention of silver purchase acts. The section speaks only of gold-backed money and the retirement of greenbacks as the policy of sound money advocates. The consequence is noted to have been a long period of general deflation, but with no mention of the pressure from Populists for inflation via silver backed money or greenbacks.

As for the longevity and continuing applicability of EO 11110, failure to notice that it has been revoked is the consequence of failure to read carefully. The author reproduces the following information from an official source: Executive Order (EO) 10289 dated Sept. 17, 1951, 16 F.R. 9499, was as amended by: EO 10583, dated December 18, 1954, 19 F.R. 8725; EO 10882 dated July 18, 1960, 25 F.R. 6869; EO 11110 dated June 4, 1963, 28 F.R. 5605; EO 11825 dated December 31, 1974, 40 F.R. 1003; EO 12608 dated September 9, 1987, 52 F.R. 34617.

Then he says that, "The 1974 and 1987 amendments, added after Kennedy's 1963 amendment, did not change or alter any part of Kennedy's EO 11110. A search of Clinton's 1998 and 1999 EOs and Presidential Directives has also shown no reference to any alterations, suspensions, or changes to EO 11110."

He is wrong there, for it was revoked in EO 12608 in 1987. Notice above that all of the EOs above are based on EO 10289, which is officially described as "Providing for the performance of certain functions of the President by the Secretary of the Treasury."

(In other words, don't bother the President about these administrative trivialities.)

When we get down to EO 12068 in 1987, it is titled as: "Amendment of Executive Order No. 10289 as Amended, Relating to the Performance of Certain Functions Affecting the Department of the Treasury."

(And the next lines identify the original document.)

Source: The provisions of Executive Order 10289 of Sept. 17, 1951, appear at 16 FR 9499, 3 CFR, 1949-1953 Comp., p. 787, unless otherwise noted.

And here is the wording of the original: "By virtue of the authority vested in me by section 1 of the act of August 8, 1950, 64 Stat. 419 (Public Law 673, 81st Congress), and as President of the United States, it is ordered as follows:

"1. The Secretary of the Treasury is hereby designated and empowered to perform the following-described functions of the President without the approval, ratification, or other action of the President:

"…(c)…" etc., down to "(i) The authority vested in the President by Section 5318 of the Revised Statutes, as amended (19 USC 540), to employ suitable vessels other than Coast Guard cutters in the execution of laws providing for the collection of duties on imports and tonnage. [Para. 1 amended by EO 10583 of Dec. 18, 1954, 19 FR 8725, 3 CFR, 1954-1958 Comp., p. 232; EO 10882 of July 18, 1960, 25 FR 6869, 3 CFR, 1959-1963 Comp., p. 413; EO 11110 of June 4, 1963, 28 FR 5605, 3 CFR,

Eureka — We are Learning in Brazil What We Forgot at Home

In *The New York Times* (July 2), we read: "The study by the Brazilian National Confederation of Industry last September found that more than half of the 1,715 industrial firms polled could not find the skilled workers they needed. Of these 69% said the lack of a qualified work force resulted in inefficiency; 36% said it led to lower quality goods; and 36% said it made acquiring or assimilating new technologies more difficult.'

"That reality is leading thousands of Brazilian companies into the education business. Some teach basic literacy and arithmetic to janitors and manual workers. Other more advanced courses help factory and production line workers better understand math, science and composition. And major companies are increasing the amount of on-the-job training they give to engineers and professionals.

"'We are planning to invest $11 billion this year and $60 billion over the next five years just in organic growth projects,' said Maria Gugel, director of human resources, planning and compensation at Vale, one of the world's largest mining companies. 'The people behind these projects are geologists and engineers whose specialties are ports, railways and mines. These are areas where we have shortages. It would be impossible to grow without the specialized training of this sort.'

"A typical program is the one at Embraer, one of the largest manufacturers of aircraft. The company has doubled in size since the start of the decade and currently has orders in excess of $20 billion. It expects to deliver nearly 200 aircraft to clients this year.

"That is because in 2001, company directors realized that with only three universities offering courses in aeronautical engineering, there would not be enough graduates available to help them design, build and sell planes in a rapidly growing market.

"So the company created a program that selects the country's best engineering graduates and puts them through an 18-month specialization course. In Embraer's classrooms, overlooking a shop floor scattered with fuselages, they learn the skills that will help them become aeronautical engineers.■

1959-1963 Comp., p. 770; EO 12608 of Sept. 9, 1987, 52 FR 34617, 3 CFR, 1987 Comp., p. 245]"

There we have the original wording plus the information about subsequent amendments. Notice in particular that Paragraph 1 ends at sub-paragraph (i). The infamous EO 11110 amended Paragraph 1 by adding sub-paragraph (j). (It also revoked another clause in another part of EO 10289 which does not concern us.)

So, after Kennedy's EO 11110, the primary document contained an additional subparagraph 1(j).

Turn next to EO 12608 of 1987 and note that it is a big housecleaning Order, to get rid of obsolete, no longer relevant items. I reproduce the opening lines:

"Executive Order 12608 – Elimination of Unnecessary Executive Orders and Technical Amendments to Others

"September 9, 1987

"By the authority vested in me as President by the Constitution and laws of the United States of America, and in order to eliminate certain Executive Orders that are no longer necessary, and to make technical amendments in others to correct outdated agency references or obsolete legal citations, it is hereby ordered as follows:

"Section 1. The following Executive Orders are revoked…."

A list of numbered EOs follows. Then:

"Sec. 2. Each of the Executive Orders, as amended, listed in this section, and any other order that relates to functions or areas of responsibility delegated to the Office of Management and Budget, are amended by deleting the words 'Bureau of the Budget' wherever they occur and inserting in lieu thereof 'Office of Management and Budget,' and by deleting the word 'Bureau' and inserting in lieu thereof 'Office' wherever the word 'Bureau' is used as a reference to the Office of Management and Budget…."

Then follows the table of references to the EOs that are to have this change. Next, one that is irrelevant to our concern:

"Sec. 3. Executive Order No. 9979 is amended by revoking paragraph 1 and deleting the '2' introducing the remaining paragraph."

Then we get the important one:

"Sec. 4. Executive Order No. 10289, as amended, is further amended as follows:

"…(e) By revoking Sections 1(g) and 1(j), and renumbering Sections 1(h) and 1(i) as Sections 1(g) and 1(h), respectively;

"(f) Adding a new subsection (i) to Section 1:

"(i) The authority vested in the President by Section 5318 of the Revised Statutes, as amended (19 USC 540), to employ suitable vessels other than Coast Guard cutters in the execution of laws providing for the collection of duties on imports and tonnage…"

And that is the end of amendments to EO 10289.

What could be more clear? The subject of Sec. 4 above is EO 10289 *as amended* (by other EOs like 11110). And specifically revoked is section 1(j), the content of which is the ballyhooed directive to issue silver certificates.

In other words, EO11110 concerned a minor administrative detail that had reached the end of its applicability by 1987, probably because there was no more silver in the Treasury that could be committed for Silver Certificates. It was certainly no threat to the power of the Federal Reserve System. It doesn't prove that Kennedy never had an unkind thought about the Fed, but it certainly does not constitute evidence that he had mounted a campaign of sufficient significance against it to inspire his assassination.

Keith Wilde

1. This point is expressly confirmed in the Constitution Act, which may be read in full at http://laws.justice.gc.ca/en/Const/c1867_e.html#distribution. Paragraph 91 under section VI on the distribution of legislative powers includes the provisions that concern coinage, banking and issuance of paper money.

Notes re Bank of Canada Financing for Municipal Infrastructure

1. List of Municipal Resolutions

Municipalities that have formally passed resolutions on financing capital costs using the Bank of Canada:

March 1998 – "Canadians for Constitutional Money"

1. Metchosin BC (followed the Michael Journal format)
2. Nanaimo BC (first Canadian municipality to follow the Sovereignty Loan Plan)
3. Vernon BC (first Canadian municipality to vote on Constitutional Money)
4. Ladysmith BC
5. Lumby BC
6. Colborne ON
7. Haldimand County ON
8. Cramore ON
9. Colwood BC
10. Midway BC
11. Peace River Regional District BC
12. View Royal BC
13. Comox BC

Resolutions adopted since 1998:

14. Kingston ON, April 3, 2001
15. Squamish BC, April 17, 2001
16. Toronto ON, April 23 to May 2, 2001
17. Town of Lakeshore ON, June 11, 2004
18. Windsor ON, November 15, 2004

2. Kingston Resolution Adopted April 3, 2001

A. The City of Kingston request the Government of Canada,

(i) to instruct the Bank of Canada to buy securities issued by municipalities and guaranteed by the Government of Canada to pay for capital projects and/or pay off current debt; (ii) to refund to municipalities any interest paid by municipalities to the Bank of Canada;

B. That a copy of this motion be forwarded to the Federation of Canadian Municipalities, the Association of Municipalities of Ontario (AMO) for circulation to other Municipalities within the Province of Ontario with a population over 50,000, to the local MP and MPP, requesting their support and endorsement.

Moved by Councillor John Clements
Seconded by Councillor Leonore Foster

3. Toronto Resolution Adopted April 23 to May 2, 2001

May 7, 2001
The Honourable Paul Martin
Minister of Finance
Government of Canada

Sir:

I am enclosing for your information and any attention deemed necessary, Clause No. 2 contained in Report No. 6 of *The Policy and Finance Committee*, headed "Loans from the Bank of Canada," which was adopted, without amendment, by the Council of the City of Toronto at its regular meeting held on April 23, 24, 25, 26, 27, and its special meeting held on April 30, May 1 and 2, 2001.

In so doing, Council requested that:

1. The Federal Minister of Finance, in conjunction with the Province of Ontario, provide low cost, below prime, long-term

loans to municipalities, such as through the Bank of Canada; and

2. A copy of this request be forwarded to the Federation of Canadian Municipalities and the Association of Municipalities of Ontario.

Yours truly,

M. Toff/sb for City Clerk

4. FCM Resolution, September 8, 2001

FIN01.2.06CA Interest Free Loans Guaranteed by the Federal Government to the Municipalities

Be it resolved that the Federation of Canadian Municipalities urge the federal government to:

A. instruct the Bank of Canada to buy securities issued by municipalities and guaranteed by the federal government to pay for capital projects and/or to pay off current debt; and

B. refund to municipalities any interest paid by municipalities to the Bank of Canada.

5. Supporting Legislation

The *Bank of Canada Act*, Section 18

The Bank may,

A. buy and sell securities issued or guaranteed by Canada or any province;

(i) make loans or advances for periods not exceeding six months to the Government of Canada or the government of any province on the pledge or hypothecation of readily marketable securities issued or guaranteed by Canada or any province;

B. make loans to the Government of Canada or the government of any province, but such loans outstanding at any one time shall not, in the case of the Government of Canada, exceed one-third of the estimated revenue of the Government of Canada for its fiscal year, and shall not, in the case of a provincial government, exceed one-fourth of that government's estimated revenue for its fiscal year, and such loans shall be repaid before the end of the first quarter after the end of the fiscal year of the government that has contracted the loan.

It is section 18(c) which makes it possible for municipalities to sell their securities to the Bank *if they are guaranteed by Canada or any province*. This requires a willingness on the part of the government to do this – a willingness which is not there – and the co-operation of the Bank of Canada.

The world has been caught up in the extreme free market ideology since the 1960s. It provides a theoretical base for those who want removal of regulations which stand in the way of profits and privatization of government services and assets. By 1974 this ideology was adopted at the Bank of Cana-

If Subprime Debt Fails, Credit Cards Fill the Gap

The New York Times (9/11, "As Credit Lines Fade, Credit Cards Step In" by Jane Birnbaum) tells a tale of our hopeless encirclement.

"The credit card offers are in the mail.

"Just as the slowing economy has made access to cash a higher priority for a lot of small businesses, banks have become more reluctant to extend traditional credit lines to those businesses, experts say. But banks have been offering 'small businesses' credit cards.

"Bank cards and lines of credit both offer money when needed, but there is a fundamental difference: lines of credit have low fixed interest rates, while interest rates on credit cards can jump unpredictably."

And many suppliers learning from such gouging at their expense pass it on to their customers on overdue bills. So rate of 16% and 17% are starting to spread throughout the economy.

"Small-business cards have fundamentally replaced lines of credit,' said Alan L. Carsrud, executive director of the Global Entrepreneurship Center at Florida International University in Miami.

"Bob Stewart, head of the Center for Commercial Lending and Business Banking of the American Bankers Association, said he had no hard data but appeared to agree with Mr. Carsrud's assessment. 'People are driven to cards today because bank credit lines are tougher to get' as banks have tightened credit in the last six months,' he said. Lenders may adjust card rates as the perceived risk of lending to the borrower increases.

"'Entrepreneurs have long used personal credit cards to help bankroll new ventures,' said Scott A. Shane, a professor of entrepreneurial studies at Case Western Reserve University.

"The small-business cards often differ from personal credit cards in that some offer benefits like product discounts and extended payment terms. But they are identical in critical ways – users' balances that grow exponentially as interest rates rise, and tenders may sometimes raise rates and reduce credit limits at any time for any reason….

"In a survey in February of 500 owners of small and medium-sized businesses, the National Small Business Association, a lobbying group in Washington, found that 28% had used bank loans in the previous year, a record low. Forty-four percent said they had used cards to meet capital needs in the previous six months. Fifty-seven percent said their card terms had worsened over the last year.

"'I don't fault banks for charging high interest rates on cards because so many small businesses fail,' says Marilyn Landis, the group's chairwoman and a 20-year veteran banking veteran. But 'small-business owners desperately need the ability to enter contracts with card providers that are predictable, understandable, and stable.'

"Mrs. Landis, who owns a company in Pittsburgh that provides chief financial services to growing businesses, spoke from personal experiences. She said her introductory rate on a small-business card had risen to 27.9% from 3.9%, after the lender said a mailed payment had arrived one day late.

"In 2003, Stephen Strachan, a flower importer in York, PA, told members of Congress this spring that rate increases on businesses and personal cards had forced him to curtail ventures and lay off workers. Mr. Strachan made his remarks at hearings for a bill pending in Congress, the Credit Card-holders' Bill of Rights.

"'Card lenders originally offered me very high limits at very attractive rates because of my excellent credit profile,' he said in an interview. 'But once I accepted, a couple really turned up the heat. In 2003,' he said, 'one bank raised interest rates from as low as 3% to as high as 30% on four cards with a total balance of about $150,000.' The lender cited Mr. Strachan's rising total debt, and late and missing payments as the cause. Mr. Strachan said that whenever he had received statements, he had always mailed payments, 'well before their due date.'

"In May, the Federal Reserve released proposals for limiting the circumstances under which lenders could increase interest rates on existing card balances. The limits would apply to personal cards – including any business expenses charged on them – but not to business cards, a Fed spokesman said."

W.K.

da, and the government's use of the Bank to finance public debt was reduced by increased financing through the private market. This resulted in an unnecessary increase in the federal public debt of over 3,000%, from $18 billion in 1974 to $588 billion in 1997, with a corresponding increase in provincial and municipal debt, and massive interest payments (in 2006 – $32 billion for the federal government plus another $31 billion for provinces and local governments). The decision of 1974 has to be reversed if ever there will be enough funds for social needs. This won't happen easily, but municipalities working together might be able to influence the government to do so.

6. January 7, 2003

Letter from John Burrett, Manager, Economic and Social Policy, FCM.

Conclusions of the FCM research staff: "The current legislation does not allow loans directly from the Bank of Canada, nor is Bank of Canada lending interest free. Moreover, an in-depth study by the City of Toronto, in 2001, says: "Given that loans from the Bank of Canada are not interest-free and not available directly to municipalities under the *Bank Act*, we believe that the lowest cost of funds and most flexible terms can be achieved in competitive capital markets without resorting to federal loans or programs that could have higher interest rates and restrict the City's future financing program."

January 20, 2003

Reply to John Burrett from Richard Priestman: "…the information received is misleading if not incorrect. First, section 18(c) (of the *Bank of Canada Act*) states that the Bank may 'buy and sell securities issued or guaranteed by Canada or any province,' meaning that the mechanism is there for municipalities to get financing through the Bank of Canada *if* their securities were guaranteed by Canada or a province. Secondly, since the Bank of Canada is wholly owned by the government, any interest paid by the government to it is returned as dividends less the cost of administration. Rates could and should be low for provinces and municipalities, too, if the government were of a mind to refund the interest paid less the cost of administration.

7. From Richard Priestman to David Cohen

December 8, 2004

David Cohen, Director Federation of Canadian Municipalities

Dear Mr. Cohen:

You may recall my previous correspondence with you (6/12/02) regarding Bank of Canada financing for municipal capital works. I had been corresponding with John Burrett, but he informed me on May 29, 2004, that he is no longer managing FCM municipal finance work and referred me to you. Municipalities are becoming increasingly interested in this, the latest to adopt a resolution on this issue being the City of Windsor.

I was encouraged when the FCM Board adopted the resolution in September, 2001, urging the federal government to:

A. Instruct the Bank of Canada to buy securities issued by municipalities and guaranteed by the federal government to pay for capital projects and/or to pay off current debt; and

B. Refund to municipalities any interest paid by municipalities to the Bank of Canada.

However, in a letter to Kingston, January 17, 2002, the FCM stated that it had not yet received a response from the government. Hearing nothing more I wrote to you on December 6, 2002, stating that several municipalities wanted to pursue this matter and would like to know if the FCM had received a response from the government since the previous January. We also asked if the FCM would be suggesting to all the municipalities which are members of the FCM that they should write to the government in support of the resolutions, recognizing that

Curse of Uninsurable Insurance

Mr. Krehm:

In his philosophical works, Aristotle often used the expression "on pain of infinite regress" to point out the fallacy of redundancy. Infinite regress describes perfectly the process involved in credit default swaps explained in the article referenced.

Insuring against a bond is absurd, and the infinite regress such an absurdity created has led to the financial meltdown on Wall Street, predicted by you in the September 2008 issue. A bond is supposed to be backed by the assets of the corporation issuing the bond, and the risk involved is supposed to be measured by the interest rate of the bond, and by its trading value in the secondary market. To take out insurance on a bond first involves measuring the credit risk of the issuer of the bond by the issuer of the insurance – a task that should have been carried out by the buyer of the bond in the first place or least by the bond rating agency. Then the insurance purchaser has to pay for the insurance against the bond! Where is the money for the insurance supposed to come from – the interest rate on the bond? But would it not simply have been easier to sell the bond at a loss in the secondary market than pay the insurance? If the insurer correctly rated the risk, he ought to be charging at least as much and probably a little more than the loss incurred in selling the bond on the secondary market by the holder. Absurdity piled on absurdity!

The more complex these inter-related redundancies become, the more impossible becomes the forecast of the results of an actual default, even with computer models. Somehow, the appropriation of the assets of the company the issued the bond in the first place seems to disappear from the resolution because nobody can clearly claim to be the owner of the assets pledged against the bond. Absurdity.

Imagine having bought a bond from Lehman Brothers. Imagine then buying insurance from Lehman Brothers as a hedge against the default on the Lehman Brothers' bond. Lehman Brothers then goes into default. What's the result? You paid Lehman Brothers twice and have nothing to show for it. Lehman Brothers took money from you twice, and gave nothing back. But then Lehman Brothers played that game themselves with the money you gave them, and got burned! Burning you in turn!

These financial wizards were so smart, they outsmarted themselves!

If nothing else, Aristotle's warning against the infinite regress proved true once again. The KISS principle needs to be applied to financial markets as well.

Vincent J. Curtis

"It appears we have appointed our worst generals to command forces, and our most gifted and brilliant to edit newspapers! In fact, I discovered by reading newspapers that these editor/geniuses plainly saw all my strategic defects from the start, yet failed to inform me until it was too late. Accordingly, I'm readily willing to yield my command to these obviously superior intellects, and I'll, in turn, do my best for the Cause by writing editorials – after the fact." – Robert E. Lee, 1863

the government is more likely to act on letters from a thousand municipalities.

On January 7, 2003, I received a letter from John Burrett confirming that no response had been received from the Government of Canada other than to acknowledge receipt of the letters received from the FCM. He also stated that the current legislation does not allow loans directly from the Bank of Canada, nor is Bank of Canada lending interest free, citing information received from the City of Toronto Chief Financial Officer, Wanda Lyczyk, and Bank of Canada staff who said they were not authorized to make loans to municipalities. Regarding the latter, it only requires a decision by the government to make use of the Bank for municipal financing in order for the staff to be "authorized."

Ms. Liczyk's information had been thoroughly discounted by William Krehm who wrote to her in response to a letter she had written on June 28, 2000, to explain where her information was wrong.

This information was given to John Burrett who replied in April that, "We will take your argument under advisement and will consider this as an option in our current research on methods of municipal finance. We will be issuing a report in September (2003), at an FCM-sponsored conference on municipal finance. I will pass this email on to our consultants."

On May 27, 2004, I wrote to Mr. Burrett to learn what was decided at the September conference, which brings us full circle to Mr. Burrett's letter of May 29. Can you tell me what was decided at the September 2003 FCM-sponsored conference on municipal finance *vis-à-vis* Bank of Canada financing for municipal capital projects?

Because of the keen interest in this matter by some members of Windsor Council I have forwarded a copy of this letter to them and other members of the Committee on Monetary and Economic Reform.

Richard Priestman, COMER, Kingston

cc: David Cassivi, Ken Lewenza Jr., Tom Wilson, William Krehm, Andre Marentette, George Crowell, Gordon Coggins

8. September 2005

Letter to D'Arcy Craig Milligan (COMER) from Sylvie Delaquis, Assistant to the Director, Policy, Advocacy and Communications Department, FCM.

At its September 2005 meeting, the National Board of Directors reviewed resolution FIN05.3.06 – Interest Free Loans to Municipal Governments, submitted by the Town of Ladysmith and the City of Port Alberni, British Columbia. This resolution was originally submitted in 2001 as Resolu-

Russia Learns of a Seamy Side to Oligarchic Capitalism that is Not Helped by Military Invasion of Its Neighbours

Just when the Russian government made bold and aggressive by its oil and gas resources that Europe and the world need, is surprised by a vulnerability that had not been sufficiently considered.

It is very well having oil and gas in the ground, but getting the stuff out and shipped requires an inordinate amount of complex and daring financing. And that involves living in relative peace even with rival powers.

But let the Associated Press in a dispatch carried in *The Globe and Mail* (12/09, "Russia moves to calm tumbling markets: RIA-Novosti") recount the sudden appearance of this factor that was not even considered a couple of months ago when military solutions were on the order of the day: "Russia's top central banker warned yesterday the country's banking sector faces a liquidity shortage, just hours after President Dmitry Medvedev sought to restore calm to Russia's battered stock market and boost its investment image.

"'The situation in the stock market is, I am sure, a temporary phenomenon and obviously does not reflect the actual state of the economy,' said President Medvedev in televised comments, stepping in for the second time in as many days to reassure investors. 'The Russian stock market remains very promising for investments, and serious investors understand this.'

"Mr. Medvedev's remarks come after a miserable stretch for Russian equities. The benchmark RTS index – down 47.8% since its May high – has dropped 13.9% since the start of the week, while the MICEX where most trading takes place, is down 14.5%.

"The slide has been fuelled by dropping oil prices – Russia is the world's No. 2 oil exporter after Saudi Arabia – tensions with the West after Russia's invasion of Georgia, and concerns about government interference with business. Investors are also warily watching developments at the fourth largest US investment bank, Lehman Brothers Holdings Inc., which announced plans to shore up finances in the wake of bad bets on real-estate related holdings."

That, on top of the recent invasion of its southern neighbour, makes for a very messy potful, from which even former Soviet officials find it hard to extract the promise of enticing investment opportunities.

"Central bank chairman Sergei Ignatiev said that 'as far as liquidity is concerned, there is some shortfall in the banking sector. The central bank is taking large-scale steps to refinance several banks. Our capabilities fully allow us to increase these operations several times.

"Mr. Medvedev urged the government and the central bank to do everything within its power to attract additional investments. Finance Minister Alexei Kudrin earlier in the week said the government was considering using funds from its national welfare fund to invest in domestic equities.

"'What you see now is a full-fledged panic,' said Michael Ganske, strategist at Commerzbank in London. 'We are in a situation now where the authorities have to convince investors that it's worth investing in Russia.' The central bank has actively supported the banking sector, pumping liquidity into the market through its twice daily repo auctions, which reached a record one-day high this year of 300 billion rubles (about $12.5 billion Canadian) yesterday.

"Last August's subprime crisis sparked off a liquidity squeeze in the sector, compounded by harder-to-access funding from overseas. The central bank has won plaudits for its efforts to support the sector, but the plunging equity markets have accelerated banks' demand for more funds as they approach October when tax payments become due."

For the time being this spreading financial concern douses the government's military ardor. But if matters worsen at home a contrary effect is certainly not excluded.

W.K.

tion FIN01.2.06CA (adopted as a Category A – national municipal issues).

The Board subsequently re-categorized Resolution FIN05.3.06 as "C" – not within municipal jurisdiction. It took into consideration a number of factors to arrive at this decision. In the past several years, the federal government has honoured its commitment to redefine and strengthen its relationship with municipal sector through the New Deal. Providing municipal governments with additional financial resources, starting with refunding 100% of the GST, and more recently, sharing a portion of the federal gas tax, are key elements of the New Deal. These investments are significant. Further FCM advocacy targeting additional federal financial support to the municipal sector will be focused on securing a long term national plan to eliminate the municipal infrastructure deficit.

(In FCM's most recent discussions with the Bank of Canada, the Bank clearly stated that it is not a commercial lending institution. The Bank described its role as one which directs national monetary policy and controls the money supply, and not that acts as a lender to governments except in the most unusual of circumstances. In one of the rare instances when the Bank did make loans to governments, it was to provincial governments in order to avert a liquidity crisis during the Great Depression. While the Bank could conceivably make a loan to a municipal government, it could only do so through a provincial government and only for short periods under terms acceptable to the Bank.)

Information from Gabriel Miller, Senior Policy Analyst, FCM, re benefits received through the "New Deal for Cities and Communities" – February 15, 2007

"The 100% GST/HST rebate came into effect toward the end of 2003-2004, and the gas tax transfer began in 2005-2006, so neither of these initiatives delivered any financial benefits in 2001 or 2002.

The financial benefit to municipal governments of these initiatives up to and including 2005-2006 are as follows:

Gas tax: 2005-06 = $582M – Total = $582M

GST Rebate: 2003-04 = $100M; 2004-05 = $582M; 2005-06 = $605M – Total = $1,287M

Total Benefit = $582M + 1,287M = $1,869M

So up to and including 2005-06, the two initiatives have delivered about $1.87 billion in benefits to municipal governments.

It is important to note that projections in Budget 2006 show benefits of both initiatives running to at least 2009-10, and this fall the government committed to extend the gas tax transfer at least two more years beyond that (until 2011-12).

Compare the amount – $1,869M – to the $100,000M deficit, growing at $2,000M per year. It does not even cover the annual increase in the municipal deficit let alone the accumulated deficit of $100,000M.

The statement that the Bank is not a commercial lending institution has no bearing on the matter except that it may reflect the mindset of Bank staff who believe that government should borrow from the private sector. The statement that the role of the Bank is not "as a lender to governments except in the most unusual of circumstances" is simply not correct.

The Bank has consistently lent to the Government, although not enough in recent years to enable the government to fund capital infrastructure costs. The percentage of long-term federal debt held by the Bank ranged from 25% at the beginning of WWII to 12.8% by 1946 to 34% by 1952, going up and down and sitting at 21% in the mid seventies, then going down steadily to 5.8% and then gradually increasing to about 11% today.[1] The Bank does not see its role today as a lender to government for capital investments, but surely that is a decision that should not be left to the Bank. Municipalities can help to change this by working together.

Richard Priestman

President, Kingston Chapter, COMER

1. The Debt Management Report – 2005-2006 – Chart 19, from the *National Balance Sheet Accounts*, Statistics Canada, shows the Bank of Canada holding 10.9% of Government of Canada Market Debt.

No Halfway House to Being an Honest Man

The conclusion hit me between the eyes in reading proof of the third volume of *Meltdown,* the selection of the most significant articles in the first twenty years of *Economic Reform.*

In the *Collapse of a Great Faith* published in May 2002, or fully six years before the subprime mortgage and currency crisis, the pattern had already asserted itself. With each of the successive failed gambles of our banks, not only were they bailed out at public expense, but they were moved up a bit further above the salt towards the head of the table. The late great French economist François Perroux had identified as the "dominant revenue" of a given historical period, as the income of the ruling group which come to be identified with the well-being of society as a whole. Under feudalism it was the large landowners, then with the doing away of high protective tariffs on foodstuffs in England, it shifted to the new industrialists who could keep wages lower, and then came the day of the bankers, and more recently of speculative banks, with the world deregulated and globalized to provide them with a suitable playground.

So let us begin by quoting the article alluded to.

"For millennia Christianity and the other great faiths preached the evangel of salvation by curbing humanity's baser appetites…. The New Economy improved on that. In its view God so loved the world that He spared its inhabitants the inconvenience of curbing their greed. By this humanity would regain the innocence of children, and freed from having to rein in its voracity.

"This ended up making virtue a matter of scale. And that miracle, accepted as such because of its very absurdity, persisted even when by that very doctrine they grew into transnational corporations that rewarded their chieftains in ten and more digits.

"All this was made possible supposedly by bringing in infinitesimal calculus. About mathematics the missionaries of the new dispensation had limited knowledge. They believed that instead of revealing the implications of assumptions fed into the model, that the use of a mathematical apparatus was in itself a guarantee of high science. By multiplying the integration signs, you could intimidate the doubters.

"But what really kept the system going was that it seemed to be working. That, however, is no longer the case.

"The Wall Street Journal (28/03, "A Dwindling Supply of Credit Plagues Corporations" by Gregory Zuckerman) gives us the score: "For years the commercial paper market has served as the corporate world's automated teller machine, spitting out a seemingly endless supply of credit for businesses at super-low interest rates.

"But now, amid financial jitters caused by Enron Corp.'s collapse, the machine is sputtering, sending a surprising number of companies of all sizes to find money for their basic needs, from paying salaries to buying office supplies. Some are paying higher interest rates so that they can continue selling paper. But others have turned to raising debt by other, costlier means. These companies include Qwest Communications International Inc., Gap Inc., and Computer Associates International Inc.

"For an economy still in the tentative stages of a turnaround, the problems in the commercial paper market underscore the profound effect of Enron's collapse on the basic workings of American finance. Economists worry that the troubles could put a lid on capital spending, as companies scramble to save cash – a move that could delay or even reverse the recovery.

"For the past 40 years the massive commercial–paper market has been a critical – almost invisible – lubricant for the economy. Through the commercial paper market. companies issue IOUs for critical short-term financing, lasting for as long as 270 days or as short as a single day. Money raised in this way was used to pay for their most basic, immediate needs, though in recent years it has also covered billion-dollar acquisitions. Commercial paper generally requires no collateral. It is the cheapest sort of debt financing, with rates typically several percentages points below those of longer-term bonds and loans from banks. That's because it is less risky to lend money for a short period – the chances of a an unforeseen downturn, sending up interest rates, are less.

"The market began experiencing difficulties about a year ago, as the economy slowed. Stung by criticism that both Moody's and Standard & Poor's kept Enron at investment grade until just five days before it filed for bankruptcy, the rating agencies started poring over balance sheets, looking for companies that seemed dependent on commercial paper.

"The result: Sprint was forced to take on more expensive debt including a $1 billion new loan and $5 billion in long-term bonds, costing the company almost $2 billion in additional borrowing costs each year, according to analysts."

It is notable that at this early stage it was commercial rather than investment credit that was under a cloud.

"Last week Bill Gross, PIMCO's CEO, declared his firm wouldn't even buy commercial paper from General Electric Co., which had been relying on this market for about half its financing needs."

William Krehm

If Democracy is to Survive Calls for a Shared Notion of our Common History

With the cat otherwise preoccupied, the mice will play.

The same issue of *The New York Times* (03/08, "Korean War's Lost Chapter: South Korea Says US Killed Hundreds of Civilians" by Choe Sang-Hun) reports: "Wolmi Island, South Korea – When American troops stormed this island more than a half century ago, it was a hive of Communist trenches and pill-boxes. Now it is a park where children play and retirees stroll along a tree-shaded esplanade.

"From a hill-top across a narrow channel, Gen. Douglas MacArthur memorialized in bronze, appears to gaze down on the beaches of Inchon where his troops splashed ashore in September 1950, changing the course of the Korean War and making him a hero here. In the port below, rows of cars, beaming in the sun, wait to be shipped around the world – testimony to South Korea's industrial might [developed] since the conflict ended 55 years ago.

"But inside a ragged tent at the entrance of the park, some aging Koreans gather daily to draw attention to their side of the battle in their hometown, a carnage not mentioned in South Korea's official histories or textbooks.

"'When the napalm hit our village, many people were still sleeping in their homes,' said Lee Beom-Ki, 76. 'Those who survived the flames ran to the tidal flats. We were trying to show the American pilots that we were civilians. But they strafed us, women and children.'

"Residents say dozens of civilians were killed.

"The attack, though not the civilian casualties, has been corroborated by declassified US military documents recently reviewed by South Korean investigators.

"On Sept. 10, 1950, five days before the Inchon landing, according to the documents, 43 American warplanes swarmed over Wolmi, dropping 93 napalm canisters to 'burn out' the eastern slope in an attempt to clear the way for United Nations troops.

"The documents and survivors' stories persuaded a South Korean commission investigating long-suppressed allegations of wartime atrocities by Koreans and Americans to rule this year that the attack violated international conventions on war and to ask the country's leaders to [seek] compensation from the United States.

"The ruling was one of three by the government's Truth and Reconciliation Commission in the past several months that accused the US military of using indiscriminate force in 1950 and 1951 as troops struggled against Communists from the North and from China."

South Koreans Return to Memory's Bloody Lane

"The Commission says at least 228 civilians, and perhaps hundreds more, were killed in the three attacks.

"In one case, the commission said, at least 167 villagers, more than half of them women, were burned to death or asphyxiated in Tanyang, 87 miles southeast of Seoul, when the Americans dropped napalm at the entrance of a cave filled with refugees.

"'We should not ignore or confuse the deaths of unarmed civilians resulting from the mistakes of a few soldiers but from systematic aerial bombing and strafing,' said Kim Dong-choon, a senior commission official.

"The South Korean government has not disclosed how it plans to follow up the findings. And Maj. Stewart Upton, a Defense Department spokesman, said the Pentagon could not comment on the reports pending formal action by the South Korean government.

"Under South Korea's earlier authoritarian and staunchly anti-Communist governments, criticism of American actions in the war was taboo.

"But after investigations showed that American soldiers killed South Korean civilians in air and ground attacks on the hamlet of No Gun Ri in 1950 – and after the US acknowledged the deaths but refused to investigate other claims. A Liberal government set up the commission in 2005. More than 500 petitions, some describing the same actions, were filed to demand the investigation of allegations of mass killings by American troops, mostly in air strikes.

"The findings on the three episodes were the commission's first against the US, and it is unlikely that the group has the time or resources to investigate more before it is disbanded, as early as 2100.

"Separately, the commission has also ruled that the South Koran government summarily executed thousands of political prisoners and killed many unarmed villagers during the war. The Wolmi victims' demand for recognition tap into complicated emotions underlying South Korea's alliance with the US.

"'We thank the American troops for saving our country from Communism, for the peace and prosperity we have today,' said Han In-deuk, chairwoman of a Wolmi advocacy group. 'Does that mean we have to shut up about what happened to our families?'

"The Air strikes came during desperate times for the American forces and for the South Koreans they had come to defend.

"The war broke out in June 1950 with a Communist invasion from the north. In September, when General MacArthur planned the landing at Inchon to relieve United Nations forces cornered in the southeastern tip of the peninsula, it decided it had first to neutralize Wolmi, which overlooks the channel to the harbor."

"The mission was to saturate the area so thoroughly with napalm that all installations on that area would be burned," Marine pilots said in one of their mission reports on Wolmi retrieved by the commission from the National Archives and Records Administration of the US. Troops were seen, but the flashes observed on the ground indicated the intensity of the fire to be accurate enough to destroy any doubts about [whom they were killing].

"The Inchon landing helped UN troops recapture Seoul and drive the North Koreans back. But the tide turned again when China entered the war.

continues…

The Mystique of the Cigarette in Russia

A still undeciphered code seems to have been established amongst Russia's rulers – a strange tolerance for tobacco and alcohol. Could it be that the granting of these lesser freedoms eases the denial of the greater ones, with the further advantage that their life-shortening effect carries an unspoken sermon on the dangers of all freedom to whatever regime is in the saddle? But the contradiction remains that the drastically shortened life spans and a declining population due to alcohol and tobacco go ill with the ambitions of the eternal Imperial Russia. There are relationships and implications there still to be deciphered.

The *New York Times* (10/09, "Wary of Protests, Russia Puts Few Limits on Smoking" by Courtney Weaver) explores some of the social effects of these most paradoxical freedoms especially at a time when its expanding gas and oil puts it in a favoured position to a leading position in the concert of nations. And at the very time that its great rival, the United States, has successfully contained the lures of tobacco and has a rapidly expanding population.

"The Russian government seems reluctant to tackle the high smoking rate. Even as it tries to forestall a sharp drop in the population with campaigns promoting family life and a higher birth rate, it has barely invested in anti-tobacco ads and education.

A pack of cigarettes can cost as little as 25 cents because, unlike in the United States and many Western European countries, in Russia, tobacco is hardly taxed.

"The government appears to have allowed cigarette sales and smoking to flourish in part because it is wary of engaging in the kind of anti-vice campaigns that historically have produced a sharp backlash in Russia.

"While the Kremlin tends to keep a strong grip on Russian politics, it remains sensitive to broad-based protests over issues like inflation, pensions and housing, as well as tobacco and alcohol.

"Dmitri Tanin, chairman of the Consumer Societies Confederation, a nonprofit group in Moscow, and one of Russia's top specialists on tobacco control, said officials did not want to curb smoking because they remember the response to cigarette shortages and crackdowns on alcohol in the 1980s.

"'The ineffectiveness of these anti-tobacco measures is connected to the state being scared of provoking the protests of various social groups,' Mr. Yanin said.

"When the Soviet government ran low on state-brand cigarettes in the late 1980s, smokers took to the streets in Moscow, St. Petersburg and Kiev. Michael S. Gorbachev, then the Soviet leader, had to appeal to international tobacco manufacturers to send an emergency shipment of 34 billion cigarettes.

"Since then foreign tobacco companies have become among Russia's biggest foreign investors. The Kremlin has not ignored the issue, Russia's president Dmitri A. Medvedev, and Dr. Gennadi G. Onishchenko, the chief health inspector, have practically acknowledged that the country must do more to combat smoking.

"Dr. Onishchenko has described foreign tobacco as responsible for the, "nicotine genocide" of the Russian people, and Mr. Medvedev, said in June said that smokers may have to pay more for insurance.

"'Fifty percent of citizens are smoking in this country,' Mr. Medvedev said. 'That's the highest rate in the world.'

"Russia has the fourth highest annual rate of per capita consumption, and smoking is responsible for 42 per cent of early deaths among Russian men 38 to 59 years old, according to Euromonitor International, a consulting firm.

"Those figures are feeding fears about what will happen to the Russian economy in the coming years if, as the United Nations Population Division suggests, the Russian population experienced a drop of 21 million people to 120 million from 2000 to 2025.

"Even so, Russia's Parliament left for its summer recess without approving any new anti-smoking measures. In June, Russia signed the World Health Organization's Framework Convention on Tobacco Control, which mandated a series of measures against smoking within five years, but many health care specialists said they were skeptical that the government truly had the will to carry out the plan.

"Not only are men a source of concern for anti-smoking groups. The group's representatives said they believed that foreign tobacco companies were responsible for a sharp increase in recent years in the number of women who smoke in Russia. The companies have focussed much of their advertising on women, and the number of women who smoke has doubled since Soviet times.

"The tobacco treaty calls for states to impose higher prices for cigarettes, and the Centers for Disease Control and Prevention in Atlanta says such price increases have the biggest effect on reducing smoking among teen-agers and people with low incomes.

W.K.

"The other two attacks the commission ruled on, in Tanyang and Sansong, south of Seoul, occurred as Communist forces barreled down the peninsula. As the Allies fell back, they were attacked by guerrillas they could not easily distinguish from refugees.

"On Jan. 14, 1951, the Army's X Corpus under Maj. Gen. Edward M. Almond ordered 'the methodical destruction of dwellings and other buildings forward of the front lines which are, or susceptible of being, utilized by the enemy for shelter.' It recommended air strikes. 'Excellent results' was how American pilots summarized their strikes at Sansong on Jan. 19, 1951.

"The same day, however, one of General Almond's subordinates, Brig. Gen. David G. Barr of the Seventh Infantry Division, wrote to Gen. Almond that 'methodical burning out poor farmers when no enemy is present is against the grain of US soldiers.' At least 51 villages, including 16 children, were killed in Sansong, according to the Truth and Reconciliation Commission.

"The case appeared closed until several years ago, when, in the course of a Korean reporter's investigation, villagers acquired a copy of the American military's wartime report and read that they had been told to evacuate. They insist, and the commission agreed, that this was not true.

"Wolmi survivors said the North Korean officers' housing was about 1,000 feet away from the village. They say the American pilots, whose mission reports noted 'visibility unlimited' and firing altitudes as low as 100 feet, should not have mistaken villagers, including women and children, for the enemy.

"The victims' grievances found an outlet in 2005, when left-leaning civic groups tried to topple the MacArthur statue. But Wolmi survivors say they did not join the protest for fear they might be branded anti-American. 'We consider MacArthur a hero to our country, but no one can know the suffering our family endured,' said Chung Ji-eun, an Inchon cabdriver, whose father died at Wolmi."

Several conclusions emerge from the official investigations of these tragic episodes of Korean history. Globalization – especially when its key initiator forfeits its supreme position – teaches us some bitter lessons. These must be drawn from a reassessment of that common history. That in itself will correct the maldistribution of power and hence of even the accountancy resulting from too simplified a notion of our common history.

William Krehm

Are We Wasting Our Time in Keeping Decisive Cuts of History Alive?

For decades COMER was amongst the few organizations that even referred to what we usually call the Rooseveltian bank reform. It was brought in to deal with a very urgent emergency. The Great Depression that began in October 1929, had gone on ever deepening, until by the time President Franklin Roosevelt was inaugurated for his first presidential term in January 1933, 38% of the banks across the US had already shut their doors.

And one of his first acts as president was to declare a bank moratorium that lasted a full month. When the banks were reopened for business, depositors dared leave their savings with them only because of government deposit insurance that had been introduced. Moreover, a whole series of restrictions on what banks could do became law under the name of its congressional sponsors – the *Glass-Steagall Act.*

Since then COMER has been one of the few organizations that continued talking about that legislation. It confined banks strictly to banking, prohibiting them from acquiring interests in the other "non-banking financial pillars" – at the time, stock brokerage, insurance and mortgage institutions."

There was a good enough reason for that. Each of these institutions kept its own cash and near-cash (i.e., interest-bearing) reserves for the needs of its own business. Once the banks got their hands on these, it would use them as the base to which to apply the bank multiplier, that any economic text book printed before 1991 explained.

It was the multiple of loans that banks could lend out on the basis of the legal tender – also known as "cash" – in its vaults. The reserves of the other pillars were not carried as legal tender, because legal tender – like two, five or other dollar bills – earns no interest. So right there before *Glass-Steagall*, the banks could contaminate their supposedly legal tender reserves with interest-bearing reserves. The value of such interest-bearing debt would move in the opposite direction of the benchmark interest rates set by the central bank.

For years we made the point, and our critics used to tell us that we were wasting our time. And then suddenly a few days ago the story of *Glass-Steagall* was disclosed again after years and decades of silence. The timing could have been no accident since it was the same day that *The New York Times* and *The Wall Street Journal* suddenly made the revelation for the first time after complete silence on the matter for decades. Elsewhere in this issue of *ER* we give the details – most vital in assessing what sort of democracy we live with.

However, the main purpose of this article is to indicate how immense even with this belated disclosure by our governments, the remaining cover-up of crucial historic facts remains. On page 20 of *The Globe and Mail* (20/09, "Wall Street Meltdown" by Kevin Carmichael, Ottawa), we read after a description of the *Glass-Steagall* legislation: "By 1999, when president Bill Clinton scrapped *Glass-Steagall*, it was merely a reflection that the lines separating these two divisions of the banking world were already starting to blur."

The Scrapping of Glass-Steagall

That is a gross omission of tangled self-interested circumstance that holds the key to how the world got into this seemingly hopeless model, and how we can step out of it with ease and even elegance.

Let us briefly recount the still suppressed run of fatal history that brought the world to its present seemingly hopeless mess.

By the 1950s the bank of the world forcibly confined to sticking severely to banking, and during the war years helping the holders of government bonds use them as security for using bank financing of such bond acquisitions.

Meanwhile the Bank of Canada made use of its nationalization in 1938 to an ever greater extent to finance the infrastructures thrown up to industrialize the country to provide ever more of the arms and ammunition needed for the struggle. The gimmick in the arrangement was that almost the entire interest the federal government paid for such financing *came back to the federal government as dividends.*

And this is retold in *The Globe and Mail* (20/09, "Big Five Prove Inept at Managing

Risk"). There seems then some progress in the works of getting through with some assistance from the deepening financial crisis.

But we will let the *G&M* say its piece, and then lay forth what is still missing from this doleful tale: "For decades the Big Five investment banks had earned their money by supporting the war effort, selling bonds and stocks, and underwriting public offerings. In fact, that's all they could do, thanks to the *Glass-Steagall Act* of 1933, a law designed to stem the wild speculation that helped fuel the market crash of 1929 by ensuring that banks could not make risky gambles with customers' deposits.

Universal banks such as J. P. Morgan were forced to split into separate companies: the commercial bank, J. P. Morgan, would offer loans and take deposits; the investment bank, the newly minted Morgan Stanley, would provide advisory services and sell stocks and bonds.

"Yet in the 1990s, with the derivatives market in full swing, investment banks began straying from their roots. They became more reliant on aggressive trading standards, often with borrowed money, and devised complex products, such as securitized mortgages, that were essentially loans.

"By 1999, when President Bill Clinton scrapped *Glass-Steagall*, it was merely a reflection that the lines separating these two divisions of the banking world were already beginning to blur.

"All of this helped set the stage for the current financial crisis, which like most others, can trace its roots to the credit markets.

"In 2001 under former Federal Reserve chairman Alan Greenspan – also a monetarist in the Friedman mould – the central bank began cutting interest rates to precipitously low levels. This incited a tidal wave of new home-buying and a monstrous credit bubble.

"For investment banks, the temptation to cash in on the borrowing craze proved irresistible. Because of the cheap credit, they could borrow huge sums of money to buy mortgages of varying quality, repackage them as mind-boggling complex securities, and then sell them to investors who wanted a safe product with better returns than government bonds."

Let us stop here, encouraged by our eventually achieved success in bringing the *Glass-Steagall* legislation out of enforced oblivion, to soldier on to another hardly less crucial chapter of our history.

It has to do with the "precipitously" low levels of interest that "incited a tidal wave of new home-buying and a monstrous credit bubble."

This has to do with the disastrous effects of the repeal of the *Glass-Steagall* legislation. As a result, the US banks – and to a more modest degree the Canadian banks – rushed in to acquire the Savings and Loans (S&Ls) that in essence were mortgage trusts. Many banks lost their shirts and the Bank for International Settlements – a sort of central bankers club based in Basel, Switzerland, that had been set up as the war room to achieve the bank come-back rushed in to help the banks out of their staggering losses from their take-over of the S&Ls. BIS pushed through two major measures. The first, in 1988, declared the debt of governments of developed lands to be risk-free, and thus needing no down payment for banks to acquire. They could do so entirely on the cuff and clip the coupons.

BIS's Two Incompatible Bailout Policies and the Resulting Low Interest Rates

But intimidated, we suppose, by the no-money down major transactions that BIS had initiated, BIS declared that nothing higher than zero "inflation" – which they confuse with a flat price level – would do. However, nobody moving from a town of, say, 20,000 to New York City, expects his living costs to stay the same.

How, then, could anyone expect that to hold prices flat when society as a whole moves in that direction? Meanwhile with interest-rates pushed into the skies, the huge acquisitions of government bonds that the banks had acquired with nothing down, shrank in value, precipitating a major crisis in the NAFTA countries. Mexico's banks, that had recently been privatized from a previous nationalization, were nationalized once again. Eventually 85% of them ended up in foreign hands.

What was overlooked by BIS and the central bankers it had gathered around its knees was that when you have allowed the banks to acquire the debt of developed lands with no down payment, and then you raise interest rates into the skies to "fight inflation," you cause the market value with which you have allowed the troubled banks to buy with no down payment to drop in market price because the higher levels that current bonds will be selling at par, and those previously issued with lower interest rates will drop drastically. Surprised by this result that any freshman in an economics course could have foretold, the US, the IMF and Canada put together the largest standby fund to that date – $51 billion dollars. That forestalled a major world monetary disaster, and alerted the central banks to the incompatibility of financed bond hoards without down payment and record high interest rates. It alerted the banking fraternity that even with the political power that it had been able to amass, there were limits to its appetites if finance capitalism was to continue functioning.

And since the banks, having lost much, or all its capital in the S&L adventures, the choice had to be lower interest rates rather than foregoing a recapitalization to replace its capital losses in mortgage adventures.

But they were impressed that the days of high and ever higher interest rates were over. To cope with that problem the Clinton government brought in accrual accountancy, also known as double-entry accountancy – something that had been brought to Western Europe roughly a thousand years earlier by the Crusaders, was a must in the private sector. It requires that every transaction be entered in the ledger twice – once as the money spent or the debt incurred to acquire a capital asset as a debt and once again to record the asset acquired. In subsequent years the amount of the debt or money spent to acquire the asset is *amortized* over approximately the asset's useful life, and the asset itself is *depreciated* over a not dissimilar period. However, in government books this practice – known as capital or accrual accountancy had not been practiced. The money spent was carefully amortized but the asset acquired with the expenditure was depreciated in a single year. Clearly this left a deficit on the government's books that was not really there, but highly useful for those who did not favour social programs. It also made possible some sensationally profitable privatizations.

This, known as "cash accountancy," provided some tremendous artificial topographical features in the government books with which to pursue the interests of the speculative financial sector.

To deal with the problem of the incompatibility introduced by "cash accountancy" between the 100%-leveraged allegedly "risk-free" government bonds of advanced countries and the effect on these completely leveraged bond-hoard, the Clinton government in January 1996 brought in accrual accountancy, and working the change back to 1959 came up with another 1.3 trillion dollars of assets.

But this was entered not as investments but as "savings," which usually refers to cash assets, or assets readily convertible into cash, that government assets are usually not. On the contrary they can include bridges roads, century-old buildings or land-sites. However, a wink and nudge to the appraising company could transmit the real situation and what resulted was a vast improvement in the fiscal position that brought interest rates down. That is the whole story of the sudden plethora of assets that reduced interest rates so drastically and spared the completely leveraged bond hoards that had been causing so much trouble to the US government in 1993-1995.

In Canada the Auditor General was emboldened to withhold approval of two successive government balance sheets until a similar change had been brought into the Canadian government's bookkeeping. It was finally introduced in Canada in 2002.

W.K.

The Monetary Missteps Can Have an Immediate Effect on the Real Economy

The twisting of basic institutions from their original purposes can result in staggering confusion to society. *The Wall Street Journal* (19/22, "Oil Industry Competition Could Shrink" by Russell Gold and Ben Casselman) fills us in on the effects of the trifling of Wall Street with the US legal tender as it has already affected the gas and oil industry.

"The Wall Street credit crisis and a drop in energy prices from their recent highs are setting the stage for a wave of oil industry consolidation.

"Current market conditions could reshuffle the industry because they are helping some oil and natural gas companies and hurting others. Large, global oil companies have amassed plenty of financial clout but need to continue growing, and they now sense a buying opportunity. Smaller, mostly North American producers have lots of available land but need access to debt and equity markets to grow.

"If this smaller group faces a rising cost of borrowing, it could mean more companies putting themselves or key assets on the market.

"'I think we'll find the smaller cash-constrained companies start to consider very seriously those alternatives, which for the larger firms with better balance sheets presents a great, great buying opportunity,' said Dan McSpirit, an energy analyst with BMO Capital markets.

"Energy executives and bankers say they see emerging outlines of a buyers' market for the first time since before the commodity boom of the past few years. The buyers are expected to be large, well-financed energy companies such as European majors Royal Dutch Shell PLC and BP PLC, US majors such as Exxon Mobil Corp. or large conservative energy producers such as Devon Energy Corp. or Occidental Petroleum Corp.

"'These guys have been waiting for this correction in the market to build up their longer-term inventory of growth,' said Thomas Ebbern, managing director of investment banking for Tristone Capital Inc. in Calgary.

"Occidental President and Chief Financial Officer Steve Chazen said the Los Angeles company has been paying down debt and amassing cash for exactly this kind of situation. 'It provides opportunities in the present environment because people who got over-extended will have to sell properties.' The company with the greatest financial strength, Exxon, had about $30 billion in cash at the end of the last quarter, and holds 2.8 billion shares, worth roughly $218 billion, in its treasury.

"The big oil companies have had this financial firepower for several years. What has changed is the potential for smaller companies to face distress. Many companies focused on drilling in North America for natural gas have for years spent more cash than they generate and taking on debt to keep up their torrid pace of drilling. Questions are growing whether these companies will have to cut capital spending in coming weeks or facing a rising cost of borrowing in the face of declining commodity prices.

"[Moreover] many companies have bought drilling rights to tens of thousands of acres of land, and now must find the cash to drill hundreds of wells at a time when bank lenders are closing their windows. Investment bankers are trying to determine which companies might be gobbled up. None have disclosed financial troubles, and experts have cautioned not to expect as sudden rush of deals. Companies that have seen their share prices plummet in recent weeks may demand large premiums, believing newly depressed prices don't represent fair value."

The grouchy manners that have overtaken those in Washington who are reshaping the stance and purpose of our legal tender and so much that dangles from it, will soon be up against a new crop of doleful consequence of what they deem to be solutions for subprime debt. But the big difference is that this time around it is not improvident house-buyers that are likely to be the victims.

"Credit Suisse recently pointed out that Petrohawk Energy Corp, as Houston with a $5.5 billion market capitalization and as attractive amount of land leased in Louisiana's Haynesville gas field plans to spend $23.30 this year for each dollar its operations generate at current commodity prices. Its shares were down 1.5% on the NY stock exchange, compared to a rise of 3.6% rise for an index of comparable companies.

"The global companies have struggled to find enough new investment opportunities overseas and many have had trouble replenishing their oil and gas reserves."

To all of which the seemingly bottomless mess of the US banking system contributes endlessly.

W.K.