

THE FUNCTION OF MONEY

Money plays a vital role in the economy as a medium of exchange of wealth, but it is not itself wealth. Wealth is the product of labour applied to the natural resources of the Earth to produce useful goods and services. In a modern economy, wealth is produced both individually and by groups working together. Groups include, in this context, the government, which provides goods and services to the whole community. The wealth produced is exchanged with the wealth produced by others so that all may satisfy all their needs and it is only in this process of exchange that money has a part to play.

The production and exchange of wealth is a highly complex process of interlocking chains of production. A farmer may work for a year or more before a crop can be taken to market. The purchaser may keep it in stock for a considerable time until sale to the next in the production chain. A dentist may complete her work in a few minutes. Years of effort and claims on wealth may be needed in order to provide the highest standard of service to the community. The work of entrepreneurs produces a continuing flow of greater wealth, and custom with regulation will ensure that the increase benefits the community as well as the entrepreneur.

At each stage in the process from extraction of natural resource to final use of the wealth of goods and services, money is used as a token to represent the value of wealth put in and taken out in exchange. When the payment is due, it may be made in cash, or, more usually, by bank transaction. There may be a need for money in order to claim wealth before wealth is produced, for example to buy a car or to finance the work of the entrepreneur. The money may come from the community as a government service where appropriate, but it is usually provided as a bank loan. Banks can arrange a loan from the savings of other customers of the bank, if it is used to produce wealth the proceeds of sale of which will be sufficient to repay the loan. Maintaining the exchange of wealth in this way ensures that wealth is being put into exchange by borrowers repaying their loans, ready to complete the exchange when the savers need to spend their savings.

Banks can also create additional money for lending, with the same need to ensure that it is used to produce wealth the proceeds of sale of which will be enough to repay the loans. These valuable services provided to the community by banks are a production of wealth, for which the banks can claim wealth in exchange. The tokens of this uncompleted exchange are usually in the form of loan interest, which can sometimes be at unjustifiably high rates. The necessary supervision of commercial banks can be by a central bank such as the Bank of England.

The salient fact in the whole process is that money is just a token representing a communally accepted obligation to complete an exchange of wealth. The possessor of the money has either provided to the community wealth to that value or has accepted the obligation to provide newly created wealth of that value in the future. In a naturally functioning community, the quantity of

money in circulation would naturally accommodate the ebb and flow of exchanges. This continual reciprocal process of exchange automatically controls the money supply, and it is only a mistaken belief about home ownership that causes an apparent shortage or surplus of money.

It is reasonable to desire the benefits of home ownership and it is reasonable to use money earned from the production of wealth as the means of exchange with the wealth produced in building a house. But the house price includes the value of its location as well.

The location value is due to the communally provided services, such as good transport links, schools, shops, traders and facilities of all kinds which are wealth that would not be so readily available in a desolate place. When wealth represented by the location value is produced by the community as a whole, it can reasonably be argued that the location value belongs to the community as a whole and not to the owner of the house. Home owners may believe that having paid the capitalized location value when buying the house, they are entitled to receive the benefit as rent free occupation, or to let it for occupation by a tenant, but this is a mistake because the payment was made to the previous owner and not to the community as a whole, to whom it is due. The same argument applies to commercial and industrial land. The location value belongs to the community as a whole and buildings or other improvements to the land belong to the owner.

The development of the community which brings wealth to land location also brings the need for the communal administrative, protective and regulatory services of government, and the monetary value of that location wealth, represented by the rent of land, should therefore naturally be regarded as government revenue to complete the exchange for government goods and services. The situation now is that land owners, in particular home owners, claim the rent and the community has to meet the cost of government services by paying tax on their earnings. This continual diversion in the flow of money as claims on wealth prevents the natural functioning of money as the medium in the exchange of wealth.

To facilitate this unnatural process, banks lend for the purchase of land, particularly for home ownership. This is not a proper use of money because it simply facilitates the claiming of future land location wealth by the new owner, who produces no wealth in exchange.

Further distortions in the natural use of money follow as much of the location value gained by owners as rent-free occupation and profits from the sale or renting out of the land is used to buy more land as second homes and buy-to-let properties or deposited in banks and other financial institutions to acquire shares and loans including government bonds. These investments yield further claims on wealth in the form of rent, dividends, interest and profits, without any production of wealth in exchange.

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A highly sophisticated finance industry has grown up. It has developed new schemes for trading in money including foreign exchange transactions amounting to trillions of pounds daily which are not necessary for the exchange of wealth and carry a risk of default which could disrupt the natural wealth trading economy. It is essential to curb these unproductive activities by preventing the creation of money by banks unless it is to be used by the borrower for the creation of wealth or for temporary loans in emergency.

As a result of the inequality caused by the present unnatural flow of money, those who do not benefit from the ownership of land begin to suffer and there is discord in the community. Governments then provide state benefits, and more taxation is needed, which brings more hardship, needing more welfare and more taxation. It is a self-sustaining spiral, and eventually the government must borrow to meet its commitments. This national debt then remains as an uncompleted exchange until it is repaid by taxing future earnings from the production of wealth.

Government borrowing has been increased considerably by the repercussions from the Covid epidemic. The Bank of England helped temporarily by creating money to increase the funds available for investing in government securities, but the intention is to withdraw this temporary funding, leaving the government with the need to find alternative lenders when there is already a very much larger national debt to repay.

A very large total of national debt has accumulated, and is still accumulating, as a result of the diversion of the land location value as the private appropriation of the rent of land. It must at present be repaid by increasing the taxation of earnings or reducing state benefits. The better way is to collect instead the rent of land, the natural source of government revenue, to complete the exchange for government goods and services. Recovering the natural function of money in this way will bring a natural equitable exchange of wealth and transform society. The transition will need a change of heart by land owners, including home owners, but if economists and politicians were to declare the simple truth openly, reasonable people would accept the need for change.

In a natural economy, money would only come into use as a token of the value of wealth either already produced or to be produced by labour on natural resources and put into exchange. Only then can it represent a genuine claim on wealth in exchange. Beginning to collect the rent of land as government revenue would create a virtuous spiral of reduced taxation of earnings and reduced welfare expenditure. There would normally be a balanced budget and no national debt. Even additional government claims on wealth caused by exceptional events such as war and epidemics could be met over time by a naturally prosperous community.

It might then be possible to honour the presently outstanding debt obligations in an orderly way over time and to look forward to living in a natural state of Prosperity and Freedom. [🔗](#)