Leiden Journal of International Law (2018), 31, pp. 289–313
© Foundation of the Leiden Journal of International Law 2018 doi:10.1017/S0922156518000134

INTERNATIONAL LEGAL THEORY

Analyzing the Constitutional Theory of Money: Governance, Power, and Instability

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Abstract
At the heart of the constitutional theory of money is the argument that money is central to governance. This article explores the ways in which the core mechanism of the publicly undergirded monetary system, involving the incentivization and disciplining of private investors in the money creation process, creates its 'fiscal value' and generates both power struggles and possible instability in the unit of account. This twin dynamic of power and instability is intrinsic to a *longue durée* analysis of money. It is argued that since the current jural relations allocate money and power in particular ways, the basis is created for potential future political challenges to the status quo *ante*, thereby creating instability. Further, the article emphasizes the centrality of the indeterminacy criterion which is at the core of the critical legal studies (CLS) framework, and its intimate connection to Keynes's notion of uncertainty. The indeterminacy/uncertainty nexus is used to explore how currency stability is determined or undermined by expectations, power struggles, tax contestations, and broader policy frameworks. Finally, the article relates this monetary theory to the literature on state-led industrialization and shows how such a constitutional money theory of industrialization is an alternative to the New Institutionalist perspective which emphasizes the centrality of 'clear and well-defined' property and contracts in order to create an 'efficient' economy.

Keywords
critical legal studies; governance; law and economics; money; taxation

1. Introduction

The constitutional theory of money is a new contribution to the existing literature on the nature of money and provides important theoretical and methodological insights that will challenge both neoclassical and heterodox economists. Drawing on Christine Desan's pioneering work the current article analyzes this new monetary framework, in particular its focus on how a unit of account is established, and extends it in several ways. Specifically, this article deals with the issues of power and market instability, two topics of central concern for heterodox political economists who, however, do not analyze these issues through the lens of legal analysis.

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I would like to thank Christine Desan for extensive discussions on monetary theory, Martha McCluskey on broader ones on legal theory, John Haskell for his enthusiastic encouragement of this project, Geoff Gordon for his insightful comments, and Jennifer Taub for her helpful advice on an earlier version of the paper. The usual disclaimers apply.

https://doi.org/10.1017/S0922156518000134 Published online by Cambridge University Press

The literature on money is dominated by the neoclassical barter-based approach in which the central bank adds money at its discretion 'to reduce the inconvenience of barter' and keep inflation in check, i.e., money is exogenous. Heterodox economists, drawing on both Marx and Keynes, have long rejected this view, emphasizing instead the fundamentally monetary nature of markets and the fact that money is endogenous, i.e., money is created by the need to produce and circulate commodities.[1] A further theoretical development in heterodox economics, Modern Monetary Theory (MMT), has gained considerable influence in recent years. By emphasizing the public nature of the unit of account, MMT explicitly introduces public authority into the creation of high-powered money. An important inspiration of MMT is George Friedrich Knapp who took the position that 'Money is a creature of law. A theory of money must therefore deal with legal history.'[2]

While sharing common ground with the MMT approach, it will be argued in this article that the constitutional money framework, rooted in the broad CLS tradition, is quite distinct from that of the MMT since it is based on a different methodological approach. Money can be treated in both contract and property terms and thus involves a complex bundle of rights that require public authority for enforcement. MMT scholars would not dispute this argument. However, while stressing the role of money as a governance project, this article also stresses the centrality of private decision making as well as conflict, power, and instability in the legal foundations of markets.[3] Thus the capitalist political economy is at the heart of the constitutional theory of money, as the former provides the context which determines the existence and relative stability of the unit of account.

Basing itself on Hohfeld's legal relations framework,[4] Section 2 discusses money's relationship to governance and how currency instability can occur. Section 3 discusses the political/legal foundations of the unit of account and its 'fiscal value', and how its stability is determined or undermined by expectations, power struggles, tax contestations, and broader policy frameworks. A central issue underlined here is the *indeterminacy of laws* as emphasized by the CLS tradition. Section 4 elaborates on how the state-enforced currency could be destabilized via power struggles in the context of a *longue durée* analysis, a framework pioneered by Fernand Braudel. It is argued that in the *longue durée* monetary instability is intimately connected to the Keynesian notion of *uncertainty* and that the latter is reinforced by the indeterminacy of laws.[5] Finally, this section deals with open economy considerations. It is argued

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[1] See C. Rogers, *Money, Interest and Capital: A Study in the Foundations of Monetary Theory* (1989).

[2] G.F. Knapp, *The State Theory of Money* (1924), 1. Cited in R. Kreitner, 'Legal History of Money', (2012) 8 *The Annual Review of Law and Social Science* 415, at 416. On endogenous money and the MMT view see L.R. Wray, 'Modern Money Theory: The Basics', *New Economic Perspectives*, 24 June 2014, available at neweconomicperspectives.org/2014/06/modern-money-theory-basics.html (accessed 19 January 2018).

[3] See also D. Kennedy, 'The Stakes of Law, or Hale and Foucault!', (1991) 25 *Legal Studies Forum* 327; J.K. Moudud, 'Looking into the Black Box: Policy as a Contested Process', in F.S. Lee and B. Cronin (eds.), *Handbook of Research Methods and Applications in Heterodox Economics* (2016), 400.

[4] W.N. Hohfeld, 'Some Fundamental Legal Conceptions as Applied in Legal Reasoning', (1913) 23 *Yale Law Journal* 16.

[5] See Kennedy, *supra* note 3, and R.W. Gordon, 'Critical Legal Histories', (1984) 1368 *Yale Law School Faculty Scholarship Series* 57. For analyses of the *longue durée* framework see R.E. Lee and I. Wallerstein (eds.), *The Longue Durée and World-Systems Analysis* (2012).

https://doi.org/10.1017/S0922156518000134 Published online by Cambridge University Press

that since industrialization by definition involves monetary flows and capital accumulation, the constitutional theory of money completes the literature on export-led industrialization. Section 5 rebuts the New Institutionalist claim that the Glorious Revolution provided an appropriate set of legal 'handcuffs' to restrain public authority and thus created the basis for 'clear and well-defined' private property rights as a recipe for industrialization and development. Section 6 is the conclusion.

2. Governance, Hohfeld, and instability

Money can be characterized in terms of both property and contracts. However, these are not self-defining categories and Hohfeld's seminal contribution was to challenge the lay view of property as something that arises from the fruits of one's labour or 'contract-as-agreement' between private parties. For Hohfeld property and contracts are aggregates of '*abstract* legal relations'[6] that are enforced via public authority, which allocates power to each individual or institution vis-à-vis others. Which of Hohfeld's state-enforced jural relations prevails is 'ultimately a question of justice and policy'[7] and in making laws:

> . . . judges may appeal to "natural justice" or some similar abstraction, to public policy, to "eternal" justice, to the "right" as opposed to wrong, to the settled convictions of the community, to business and social custom, to the *mores* of the time.[8]

Finally, as Arthur Corbin observed, the jural relations may themselves lead to conflict and disagreement:

> Of course, people do not agree in their notions of right and justice. They do not agree on the policies that make for general welfare and for individual survival. The interests of nations and of individuals are often necessarily in conflict. We can therefore expect war and litigation; and in many important fields the living law will continue to be inconsistent and uncertain.[9]

Thus, by implication, instability and uncertainty are inevitable in property and contract regimes. This insight is of vital significance to the current article.

Hohfeld is central to the constitutional theory of money.[10] A core implication of his framework is that monetary movements are structured by the state-enforced jural relations that determine all property and contracts. Money is central to governance in the constitutional money view, and like all property and contracts, the politically enforced background laws[11] determine what makes an asset a 'safe' one and confer liquidity on it.[12] Economists generally take for granted the characteristics of money (unit of account, store of value, medium of exchange, and means of payment) without

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6 See Hohfeld, *supra* note 4, at 24 (emphasis in original).
7 Ibid., at 36.
8 A.L. Corbin, 'Jural Relations and Their Classification', (1921) 30 *Yale Law Journal* 226, at 237–8 (emphasis in original).
9 Ibid., at 238.
10 For an elaboration of this proposition see C. Desan, 'The Market as a Matter of Money: Denaturalizing Economic Currency in American Constitutional History', (2005) 30 *Law & Social Inquiry* 1.
11 See Kennedy, *supra* note 3.
12 C. Desan, 'The Monetary Structure of Economic Activity', (2016) unpublished paper, Harvard Law School.

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interrogating what makes something *legally* money with all the qualities which we attribute to it. The general assumption seems to be that 'market forces' create these qualities but this is an empty assertion which, by being devoid of legal content, essentially naturalizes money and markets. On the other hand, law is constitutive of markets in the Legal Realist and CLS traditions, quite simply because property and contractual relations need to be cemented in order to be stable. Thus, what constitutes *money* in a given polity has undergirding it a complex structure of jural relations, themselves the results of politics, policies, and ideology. This is where Hohfeld comes in.

Naturally, the preferences of people with regards to currency holdings may at times clash with the official currency, generating changes in the bundle of jural relations. For example, in the American colonies residents of one province would either be granted a privilege by the legislature to use another one's paper currency or have it taken away. Alternatively, as in Pennsylvania, there could be a wholesale adoption of another province's (Delaware) currency.[13] Such currency substitutions have an exact parallel in the contemporary world outside the US when dollarization occurs.[14] What emerges from this discussion, as elaborated below, is that currency emitted by a state will be readily accepted by the population provided that it is not deemed to be 'excessive' (i.e., as long as the government is committed to retiring that money as taxation at some future date) and/or there are no inflationary pressures, growing trade deficits and foreign debt, or political uncertainty. Currency depreciation under such circumstances can have negative feedback effects on the economy, thereby possibly increasing its economic problems and raising uncertainty.[15] For example, a loss of trust in the currency by major investors could influence others and spark a currency crisis, as in Venezuela, and pressures for dollarization by business groups, as in Nigeria or Mexico.[16] Clearly, a rejection of the currency by large segments of the population can destabilize current political and legal institutions, requiring some political response by the state regarding the future legal foundations of the monetary system.

It must be emphasized here that Hohfeld[17] does not discuss how a particular combination of jural relations is established. The technical nature of the jural relations should not give the false impression that the legislature necessarily has full autonomy in putting in place the particular bundle of rights it desires. For example,

[13] See Desan, *supra* note 10, at 28.

[14] Dollarization is usually a consequence of macroeconomic and/or political instability. See N. Duma, 'Dollarization in Cambodia: Causes and Policy Implications', (2011) IMF Working Paper WP/11/49; M. Mecagni et al., 'Dollarization in sub-Saharan Africa: Experience and Lessons', (2015) IMF. This issue is of relevance for countries notably in sub-Saharan Africa, but also in Latin America, and parts of South and East Asia.

[15] L. Taylor, *Varieties of Stabilization Experience: Towards Sensible Macroeconomics in the Third World* (1988); L. Taylor, *Reconstructing Macroeconomics* (2004).

[16] Herrero and Casey, 'In Venezuela, Cooking With Firewood as Currency Collapses', *The New York Times*, 2 September 2017, available at www.nytimes.com/2017/09/02/world/americas/venezuela-nicholas-maduro-inflation-economic-collapse.html (accessed 19 January 2018); C. Obianwu, 'Why the Central Bank is Legally Wrong on Dollarisation', 2015, available at www.templars-law.com/wp-content/uploads/2015/08/Why-the-Central-Bank-is-Legally-Wrong-on-Dollarisation.pdf (accessed 19 January 2018); and for Mexico D. Salvatore, J.W. Dean, and T. D. Willett (eds.), *The Dollarization Debate* (2003).

[17] See Hohfeld, *supra* note 4.

https://doi.org/10.1017/S0922156518000134 Published online by Cambridge University Press

Christine Desan points out, in discussing rights and privileges in the context of the private creation of money in the American colonies:

> As in the case of rights, the distribution of privileges in constituting money affected both monetary value and related conceptions. *Private parties inventing their own exchange could influence amounts of public money demanded by supplementing it with another currency. On another level, their struggle over the power to produce money played out a debate over the character of public and private authority.*[18]

It could be inferred here that since an existing bundle of jural relations determines the *current* distribution of money, and thus of power, the latter could in turn shape the *future* content of the bundles of rights. As Warren Samuels wrote in his classic article on Robert L. Hale:[19]

> Who will use government as a source, ratifier or general supporter or reenforcer of private coercive power? In other words, every economic system inevitably comprises the problem of control of the government. Hale's analysis makes it abundantly clear that the state (government or law) is not something exogenous to economic life, but rather, *that law is a dependent as well as independent variable*, that the realization of economic interests is a function of government, and that the role of government is also a function of economic interests, that is, of those interests which are able to get into a position to use government.

We will come to the question of the law-power nexus later on in the essay and how, to use Robert W. Gordon's pithy expression, when 'another set of interests gets its paws'[20] on the law, the latter may (or may not) change. Suffice it to say here that the political economy and ideational contexts determine the nature of the jural relations and thus the fate of a currency.

3. Sovereignty, currency (in)stability, and indeterminacy

As its very name suggests, in the constitutional theory of money the unit of account is the culmination of profoundly political processes. One could conceptualize any society which is more or less devoid of liquidity, say fifth- or sixth-century England, when economic activity and the centralized state structure collapsed after the departure of the Roman forces, or the American colonies which confronted an acute shortage of gold and silver because of England's policies.[21] Under such circumstances a unit of account cannot arise and *establish* itself to mark property and contracts as a purely spontaneous private initiative for two reasons. First, such a situation in a given polity would produce multiple privately created and rival units of account, thereby making stable market transactions impossible. Profit-making from production activities requires that input costs and output prices should be in the same unit of account. With multiple units of account in the same polity this would, at the very least, be extremely challenging. There has to be one unit of account, but

[18] See Desan, *supra* note 10, at 27–8 (emphasis added).

[19] W.J. Samuels, 'The Economy as a System of Power and Its Legal Bases: The Legal Economics of Robert Lee Hale', (1973) 27 *University of Miami Law Review* 261, at 344 (emphasis added).

[20] See Gordon, *supra* note 5, at 88.

[21] See Desan, *supra* note 10, and C. Desan, *Making Money: Coin, Currency, and Coming of Capitalism* (2014).

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that can only be created and *maintained* if there is some political authority which can enforce the legal institution of that unit of account. After all, how otherwise would the bundle of rights undergirding property relations and contracts between strangers get created and enforced, or conflicts between creditors and debtors get adjudicated?

Such a political authority (or stakeholder) could be a local religious potentate, tribal head, landlord, or central state (whether democratic or despotic).[22] But if money arises and establishes itself only in a collectivity then the stakeholder at the political center has to ensure the defence of the territory and provide for the 'common good' (however that is defined), including with fortifications, roads, canals, etc. The stakeholder, therefore, has to extract material resources from the society to even exist. In a society parched of liquidity, the latter has to be legally created as a political project so that public authority can purchase goods and services from the population and stable market transactions between private individuals can take place.

If one considers paper money that is not backed by specie (as in the American colonies), what determines citizens' willingness to hold it?[23] In the American colonies, the 'good as gold' quality of paper depended on a stable state–citizen consensus or agreement that the paper issued by the public authorities would be absorbed back at some determinate future date in the form of taxes. In the stakeholder model, in short, when private individuals sell goods and services to the sovereign authority they, in effect, extend the latter a credit which is redeemed when they pay the latter taxes. This is what constitutes the money's 'fiscal value'. Thus, at its heart this future taxation constitutes an anchoring demand for the currency. However, the money also has to have a *cash premium* by providing all the advantages of holding currency, notably giving holders purchasing power.[24] This abstract theoretical argument, which determines the foundational anchor of money, is grounded in the way that it actually originated and evolved in England and later on in the American colonies.[25]

The strategy described above is at the *core*[26] of the monetary system. Of course, in the constitutional money view the fiscal actions of the public authorities cannot possibly provide for all the monetary needs of the society given the potentially erratic and uncertain nature of fiscal policy. Thus, in the case of England, by the tenth century, sovereign authorities established the practice of creating money on demand via the so-called 'free minting' system. This is an early example of endogenous money creation in which those with silver bullion had the right to bring it in to the royal mint and the latter had the duty to return a certain number of

22 The stakeholder model discussed here is adopted from Desan (2014), *supra* note 21. Desan coined the term 'stakeholder'.

23 See below for the discussion of money that is specie-backed.

24 See Desan (2014), *supra* note 21, at 64 and 47.

25 For the American colonies see F. Grubb, 'Is Paper Money Just Paper Money? Experimentation and Variation in the Paper Monies Issued by the American Colonies from 1690 to 1775', (2016) 32 *Research in Economic History* 147.

26 C. Desan, 'The Constitutional Approach to Money: Monetary Design and the Production of the Modern World', in N. Bandelj, F.F. Wherry, and V.A. Zelizer (eds.), *Money Talks* (2017), 109, at 119.

https://doi.org/10.1017/S0922156518000134 Published online by Cambridge University Press

coins after charging a minting fee. The officially minted coins then became the basis of tax payments, market transactions, and legal tender. Similarly, in the American colonies supplementary money was created via publicly established land banks which provided credit on demand to those with land. The paper bills created via the loans were used to pay debts and taxes, and circulated as money.[27] Of course – and this is an important point – despite free minting and later monetary developments, the English suffered from a chronic shortage of money until the eventual legal establishment of paper currency and bank credit.[28]

Since the fiscal actions of public authority anchor the value of the currency, what determines its potential instability, involving the relationship between money supply and demand, in this framework? This is an important question and relevant to a *longue durée* perspective of money. For example, in his tax-based model of money Charles Calomiris[29] provides data on currency depreciation and instability in the American colonies. However, Calomiris uses a rational expectations-monetarist framework to give a theoretical explanation for depreciation, an approach that would be contested by all heterodox economists. On the other hand, the MMT literature does not analyze the currency over-issuance/depreciation nexus. Yet the data provided by Calomiris needs to be explained, given the reality of currency instability throughout the history of capitalism.

The *ex ante-ex post* distinction, pioneered by the Stockholm School[30] and also central to Keynes's framework, is crucial to the following discussion. Given the prevalence of fundamental uncertainty[31] in a decentralized market economy, it would be coincidental if the net money injected into the economy on the basis of *ex ante* plans and expectations would necessarily equal the *ex ante* demand for money or what the actual *ex post* outcomes would be. The question is what effects do monetary disequilibria have? In what follows I propose two related scenarios pertaining to net money growth from a growing budget deficit, one of which pertains to uncertainty and the other to power relations and the macroeconomic effects of budget deficits. Both scenarios relate centrally to the *indeterminacy criterion* emphasized by the CLS tradition, since they point to the possibility, but not the certainty, of currency instability.

3.1. Uncertainty and tax contestation

In the constitutional money view, if a government emits currency and is *credibly* committed to its citizenry to remove it from circulation at some point in the future, then the latter's state of confidence about the currency would be maintained. This condition is, however, strongly dependent on expectations and citizens' *trust* in the political system.

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[27] C. Desan, 'From Blood to Profit: Making Money in the Practice and Imagery of Early America', (2008) 20 *The Journal of Policy History* 26, at 28.

[28] See Desan (2014), *supra* note 21.

[29] C.W. Calomiris, 'Institutional Failure, Monetary Scarcity, and the Depreciation of the Continental', (1988) 48 *Journal of Economic History* 47.

[30] C. Hamilton, 'Expectations and the "Stockholm School"', (1979) 81 *The Scandinavian Journal of Economics* 434.

[31] Keynes distinguished uncertainty from risk where the former cannot be estimated in probabilistic terms. See J.M. Keynes, 'The General Theory of Employment', (1937) *Quarterly Journal of Economics* 51.

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In *The General Theory*, John Maynard Keynes[32] related the current state of confidence to their expectations, in which future market conditions are fundamentally unknown and economic variables such as prospective rates of return on investments cannot be calculated in a probabilistic sense. Especially in hard times, people's expectations will be subject even more to 'waves of optimistic and pessimistic sentiment'[33] and investor confidence in both good and bad times will depend on the broader economic, political, and institutional climate[34] which shapes policies. As with Michal Kalecki,[35] Keynes advocated 'full employment' policies but was very aware of the problem of capital flight that such policies could provoke given their political implications:

> I see no reason to feel confidence that the more stable conditions [of the post-war era] will remove the more dangerous movements [of capital]. These are likely to be caused by political issues. Surely in the post-war years there is hardly a country in which we ought not to expect keen political discussions affecting the position of the wealthier classes and the treatment of private property. If so, there will be a number of people constantly taking fright because they think the degree of leftism in one country looks for the time being likely to be greater than somewhere else.[36]

Since wealth and private property are ultimately functions of the law, one may infer from Keynes's observation that the legal-institutional frameworks and political climates prevailing in different countries are fundamental to the shaping of investor expectations.

Capital flight, of course, involves the abandonment of the domestic currency and the flows of money to other countries, and this is how Keynes meant it in the above context. However, growing uncertainties, which Keynes also argued generated an increase in liquidity preference,[37] could involve increased dollarization without money flowing overseas, i.e., the domestic substitution of foreign for local currency. In either case, the value of the domestic currency would drop. But whether or not the above outcomes happen depends on the bundles of jural relations undergirding money. For example, does the law give foreign currency the attributes of liquidity? Does it allow capital outflows? The current and future state of these laws will thus affect economic decisions, either increasing or reducing uncertainty, and thus also the currency's stability.

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32 J.M. Keynes, *The General Theory of Employment, Interest, and Money* (1953), Ch. 12.
33 Ibid., at 154.
34 Ibid., at 162.
35 M. Kalecki, 'Political Aspects of Full Employment', (1943) 14 *Political Quarterly* 322.
36 J.M. Keynes, *The Collected Writings of John Maynard Keynes Vol 25. Activities 1940-1944: Shaping the Post-war World: The Clearing Union* (1980), at 148. Cited in J.R. Crotty, 'On Keynes and Capital Flight', (1983) 21 *Journal of Economic Literature* 59, at 62.
37 Keynes argued, '[O]ur desire to hold Money as a store of wealth is a barometer of the degree of our distrust of our own calculations and conventions concerning the future ... The possession of actual money lulls our disquietude; and the premium which we require to make us part with money is the measure of the degree of our disquietude.' From J.M. Keynes, 'The General Theory of Employment', (1937) 51 *The Quarterly Journal of Economics* 209, at 216.

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Keynes's insight regarding expectations can be linked to Mick Moore's distinction between different tax governance polities.[38] Moore distinguishes between *coercive* and *contractual* tax regimes. In the former the state has little credibility vis-à-vis the citizenry and extracts taxes coercively; in the latter taxes are generated by more accountable public authorities generating the possibility of state–citizen *revenue bargaining*.

Combining Keynes's and Moore's insights, one could argue that while prolonged slumps can certainly destabilize taxpayers' expectations even under contractual systems, an unaccountable government's credibility falls even more in such circumstances. With a rising degree of uncertainty, the attractiveness of the currency is likely to fall. One can thus understand why it took British colonial authorities almost 50 *years* to root out pre-colonial currencies in Nigeria and establish the sterling as the sole unit of account,[39] and why in recent years the poor governance and economic performance of Nigeria have made it challenging for the government to maintain the naira as the sole currency faced with the pressures of dollarization emanating from economic elites.[40]

Moore's argument suggests that the politics of taxation need to play a central role in the constitutional theory of money. Thus, it is important to account for both the *economic desirability* and the *political feasibility* of an appropriate tax structure to stabilize a currency, while satisfying other goals such as boosting investor confidence or reducing inequality. Joseph Schumpeter, Lord Nicholas Kaldor, and German sociologist Rudolf Goldscheid were among the first scholars to stress the importance of the need for a *fiscal sociology* of taxation,[41] a framework that calls for an interdisciplinary analysis of taxation. Lord Kaldor in particular emphasized the links between the state's taxation capacity and power relations in society:

> But the advocacy of fiscal reform is not some magic potion that is capable of altering the balance of political power by stealth. No doubt, expert advice on tax reform can be very useful ... But what can actually be accomplished does not depend merely on the individual good will of ministers or on the correct intellectual appreciation of the technical problems involved. *It is predominantly a matter of political power*.[42]

In short, the fiscal value of a currency is shaped by all the factors that determine the fiscal sociology of taxation.

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[38] M. Moore, 'Between Coercion and Contract: Competing Narratives on Taxation and Governance', in D. Bräutigam, O.H. Fjelstad, and M. Moore (eds.), *Taxation and State-Building in Developing Countries: Capacity and Consent* (2008), 34.

[39] W.I. Ofonagoro, 'From Traditional to British Currency in Southern Nigeria: Analysis of a Currency', (1979) 39 *The Journal of Economic History* 623.

[40] See, e.g., N.A.O. Abdul-Rashid, 'Stemming The Menace of Dollarization', *Economic Confidential*, 20 April 2015, available at economicconfidential.com/financial/stemming-the-menace-of-dollarization/ (accessed 19 January 2018). See also Obianwu, *supra* note 16.

[41] This term was coined by Schumpeter. See I.M. Martin, A.K. Mehrotra, and M. Prasad, *The New Fiscal Sociology: Taxation in Comparative and Historical Perspective* (2009).

[42] N. Kaldor, 'Will Underdeveloped Countries Learn to Tax?', (1963) 41(2) *Foreign Affairs* 410, at 418 (emphasis added).

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3.2. The effects of budget deficits

'Fiscal profligacy', fueling inflation from budget deficits, is a core theme in the neoclassical framework of authors such as Calomiris and Sargent.[43] While this is not the place to critique this framework it suffices to say that with widespread unemployment, a growing budget deficit could provide an economic stimulus and thus generate a robust demand for money. Thus, there is no question of 'over-issuance' of the currency here and thus no depreciation. However, this is but one scenario and there could be other situations of a growing budget deficit/currency depreciation nexus with no inflationary pressures in which all are reliant on the underlying legal-institutional framework of the economy. Such situations may lead to *incomplete fiscal stimuli.*

3.2.1. Capitalist opposition to 'full employment' policies

As James Crotty states,[44] Keynes was very aware of capitalist opposition to state-led 'full employment' policies, producing the potential for capital flight. However, Michal Kalecki,[45] and Robert Lee Hale[46] were the ones who explicitly linked such public-sector jobs programs to workers' increased bargaining power vis-à-vis capitalists. Like Karl Polanyi,[47] Kalecki emphasized the fact that capitalists would oppose such policies since 'under a regime of permanent full employment, the "sack" would cease to play its role as a disciplinary measure. The social position of the boss would be undermined, and the self-assurance and class-consciousness of the working class would grow'.[48] In short, faced with rising budget deficits and other progressive policies, there could *possibly* be a decline in the state of business confidence and, as a consequence, capital flight. As discussed above, the 'capital flight' could involve a greater domestic demand for foreign currency relative to the local currency. Taken together, there would be currency depreciation.

Post-Keynesian authors, perhaps some in the MMT tradition, would probably contest such an outcome. From their perspective, only a win-win situation can arise from higher budget deficits since the latter will boost effective demand and thus growth and employment. But business investment is motivated by the expectation of profitability[49] and both expectations and unit production costs[50] are determined by the bundle of jural relations that undergird property, contracts, and torts, and

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[43] See Calomiris, *supra* note 29; T.J. Sargent, 'The Ends of Four Big Inflations', in R.E. Hall (ed.), *Inflation: Causes and Effects* (1982), 41.

[44] See Crotty, *supra* note 36.

[45] See Kalecki, *supra* note 35.

[46] R.L. Hale, 'Bargaining, Duress, and Economic Liberty', (1943) 43 *Columbia Law Review* 603, at 628.

[47] '[T]he reform of capitalist economy by socialist parties is difficult even when they are determined not to interfere with the property system. For the mere possibility that they might decide to do so undermines that type of confidence which in liberal economy is vital, namely, absolute confidence in the continuity of the titles to property'. From K. Polanyi, *The Great Transformation* (1944), at 234.

[48] See Kalecki, *supra* note 35, at 3.

[49] See Keynes, *supra* note 32; T. Veblen, *The Theory of Business Enterprise* (1978); W.C. Peterson and P.S. Estenson, *Income, Employment, Economic Growth* (1996).

[50] Equal to the hourly wage rate per worker + materials (including depreciation) costs per worker divided by labour productivity.

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thus the nature of markets.[51] Duncan Kennedy observed in his analysis of Robert Hale's framework that the particular combination of background laws determines distributive outcomes.[52] So an increase in employment may or may not raise wages or lower work effort (e.g., how hard or long are workers made to work?) because of the multiple combinations of background laws that shape workers' coercive power vis-à-vis capitalists. For example, an increase in worker militancy from lower unemployment *could* lower profit expectations and, by provoking capital flight, put downward pressure on the currency.[53] On the other hand, one can clearly imagine other scenarios where rising budget deficits are consistent with background laws that stabilize or raise expected profits, e.g., import tariffs for sectors adversely affected by foreign competition, subsidies, industrial policies, and active labor market policies to train skilled workers. *There is indeterminacy at the core in terms of the effects of budget deficits* leading to the possibility, but not the certainty, of adverse consequences to the value of the currency.[54]

Finally, given the budget deficit, the value of the currency can still fall because of growing foreign debt stocks.[55] In particular for poorer countries, increased difficulties in paying back foreign debt with interest could make investor confidence fall and induce capital flight because of declining creditworthiness. These pressures would depreciate the currency, unless the state manages to implement countervailing export promotion policies, and perhaps quasi-protectionist ones too, to shore up the currency's value,[56] bolster foreign exchange reserves, and thus lower foreign debt. Many authors have advocated such policies.[57] However, this is hardly a straightforward issue since several authors in this tradition have emphasized the

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[51] For example, do strong tort laws prevent firms from flooding the market with a large number of low-quality and potentially harmful products? How do labour laws affect distributional struggles and thus unit labour costs? Are there import tariffs in place that expand the domestic market by restraining the sales of foreign firms? Do industrial policies promote export markets? Is the country embedded in a free trade zone, which subjects domestic firms to more efficient foreign firms and thus shrinks the former's market shares?

[52] See Kennedy *supra* note 3. See, e.g., various chapters in R. Asher and R. Edsworth, *Autowork* (1995) regarding an application of Kennedy's argument to the UAW and the auto industry.

[53] This was exactly the experience of the Mitterrand government in the early 1980s. See J. Birch, 'The Many Lives of François Mitterrand', *Jacobin*, 19 August 2015, available at www.jacobinmag.com/2015/08/francois-mitterrand-socialist-party-common-program-communist-pcf-1981-elections-austerity/ (accessed 19 January 2018).

[54] For references to the substantial international literature on business opposition to social democratic policies see Moudud, *supra* note 3.

[55] The question of foreign debt's excessiveness clearly does not affect the US since most of its debt is in its own currency. See B. Eichengreen, *Exorbitant Privilege: The Rise and Fall of the Dollar and the Future of the International Monetary System* (2011) on this issue. Thus, the discussion on foreign debt in the current article pertains to all other countries, especially those in the Global South. For all these countries, trade deficits involve a loss of foreign exchange reserves and thus increased need for foreign borrowing. Finally, there is an established post-Keynesian literature which argues that a rising budget deficit will have a negative effect on the trade balance, i.e., trade balances constrain how high budget deficits can increase. See J.C. Moreno-Brid and E. Pérez, 'Balance-of-Payments-Constrained Growth in Central America: 1950-96', (1999) 22 *Journal of Post Keynesian Economics* 131; W. Godley and M. Lavoie, *Monetary Economics: An Integrated Approach to Credit, Money, Income, Production and Wealth* (2007), Ch. 6.

[56] Export promotion and protectionist policies would raise the foreign demand for domestically produced goods relative to the domestic demand for foreign goods. Other things being equal, this situation would appreciate the value of the domestic currency. Finally, note that capital inflows would also tend to appreciate the currency.

[57] See, e.g., H. Chang, *Kicking Away the Ladder: Development Strategy in Historical Perspective* (2002); A. Amsden, *Asia's Next Giant* (1989).

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fact that both domestic political factors and international legal battles (e.g., in the World Trade Organization) determine the viability of such policies.[58]

In short there are numerous policy scenarios, which are themselves undergirded by the law, linking the budget deficit to the strength of the currency. *There may or may not be currency depreciation.* Monetary flows, per the constitutional money approach, are profoundly shaped by public authority, and in unpacking money 'we find a veritable hive of legal work'.[59] As Daniel Tarullo argues,[60] there is no 'natural state' of the market since public policies always structure business monetary costs and thus markets. Thus, the key issue is to understand how the law may or may not be successful in stabilizing (roughly, anyway) the currency. As Robert W. Gordon put it: 'The same body of law, in the same context, can always lead to contrary results because law is indeterminate at its core, in its inception, not just in its applications.'[61]

4. The public/private 'divide', drama, and *longue durée* analysis

There is a theoretical tension in the broad anti-neoliberal perspective which advocates 'bringing the state back in' in economics. The first approach, or what Duncan Kennedy calls social legal thought,[62] comes from the *administrative state* perspective adopted by Landis (in his early phase) and others.[63] Implicitly, policymakers in this view are seen as a 'committee of experts' who can deliver economic efficiency and social justice in an apolitical 'command-and-control' manner; the politics of the incentivization of those with wealth and power, not to mention the politics of policymaking more generally, play no role in this approach. I would locate MMT in this tradition. While currency instability in this literature arises from Minsky's debt accumulation model, there is no analysis of how the fiscal value of the unit of account can be destabilized because of uncertainty and power struggles around the background laws.[64]

On the other hand, Landis in his later phase explicitly accounted for the importance of business power in the policymaking process and thus questioned the effectiveness of administrative knowledge assumed by SLT scholars.[65] Louis L. Jaffe also voiced skepticism about Landis's earlier perspective since the latter assumed 'the existence in each case of relevant, value-free concepts, and an administration

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58 R. Wade, *Governing the Market* (1990); P. Evans, *Embedded Autonomy: States and Industrial Transformation* (1995); D.M. Trubek et al. (eds.), *Law and the New Developmental State: The Brazilian Experience in Latin American Context* (2013).

59 See Desan, *supra* note 12, at 2.

60 D.K. Tarullo, 'Beyond Normalcy in the Regulation of International Trade', (1987) 100 *Harvard Law Review* 546.

61 See Gordon, *supra* note 5, at 114.

62 D. Kennedy, 'Three Globalizations of Law and Legal Thought: 1850-2000', in D.M. Trubek and A. Santos (eds.), *The New Law and Economics Development: A Critical Appraisal* (2006), 19.

63 M.J. Horwitz, *The Transformation of American Law 1870-1960: The Crisis of Legal Orthodoxy* (1992), Ch. 8.

64 L.R. Wray, *Understanding Modern Money* (1998); L. R. Wray, 'Alternative Approaches to Money', (2010) 11 *Theoretical Inquiries in Law* 29; L.R. Wray, 'From the State Theory of Money to Modern Money', in D. Fox and W. Ernst (eds.), *Money in the Western Legal Tradition: Middle Ages to Bretton Woods* (2016).

65 See Horwitz, *supra* note 63, at 240–2.

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located at any given moment of time outside the political process, that is to say, outside or insulated from the power structure'.[66]

None of this implies that *laissez-faire* is a desirable or, even more fundamentally from the CLS perspective, attainable policy. Neither does it imply that the 'power structure' can mechanically shape economic policy. It merely asserts that the publicly anchored economic system has built into it structures of unequal power relations, both within the private sphere and between it and the public sphere. Writing about Hale, Duncan Kennedy[67] observed:

> What he has to teach us is that the legal ground rules of economic struggle constitute the economic bargaining power of the combatants. But he was aware that the ground rules are themselves at least in part the product of the conflicts they condition. The process of circular causation works between the private economic system and the public lawmaking system as well as within the economy . . . .

As Kennedy discussed in this article, it is this tension that constitutes the potential for instability in the underlying legal framework and for the background rules to recrystallize over time with one of many different new configurations. In a careful reading of Kennedy's analysis of the stabilization and destabilization of background laws,[68] with his discussion regarding their circular causal relations, cumulative feedback effects, dynamic disequilibria, and constantly changing context, the attentive reader cannot help but notice the non-linearities built into the framework. There is thus a high level of unpredictability about the future course of the economy, because the indeterminacy criterion teaches us that there are many combinations of laws which constitute markets. I would argue that it is this indeterminacy which undergirds Keynesian uncertainty since the composition of the laws that ultimately get stabilized (if only for a while) cannot be deterministically predicted *ex ante*.

The second anti-neoliberal perspective is this CLS approach. The course of English monetary history, as discussed by Christine Desan and other historians, from the 'free minting' period to the enlistment of Bank of England (BoE) investors via the profit motive, fits solidly in this perspective. It is a *longue durée* analysis *par excellence* with its layered historical narrative, spanning several centuries and producing a dynamic, often turbulent, and generally unpredictable process of money creation. While money had a legal base enforced by public authority, the latter needed to enlist the support of merchants and financiers at every step of the way, incentivizing them as well as constraining them in the *longue durée* involved in going from metallic coin to paper money.

In order to create a viable political economy public authority was necessary to irrigate it with a tax-based monetary system. In the free minting system the injection of coins was demand-driven by the private sector.[69] This endogenous expansion

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66 L.L. Jaffe, 'The Illusion of the Ideal Administration', (1973) 86 *Harvard Law Review* 1183, at 1187.

67 See Kennedy, *supra* note 3, at 336. In this quote Kennedy draws on insights from R.L. Hale, *Freedom Through Law: Public Control of Private Governing Power* (1952) pages 541–50; D. Kennedy, 'Legal Formality', (1973) 2 *The Journal of Legal Studies* 351, at 383–6; W.J. Samuels, 'The Economy as a System of Power and Its Legal Bases: The Legal Economics of Robert Lee Hale', (1973) 27 *University of Miami Law Review* 261, at 344–54.

68 See Kennedy, *supra* note 3, in particular at 335–7.

69 See Desan (2014) *supra* note 21, Ch. 1.

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of money was the result of the right of bullion holders to be returned coins that the sovereign authority had a duty to satisfy. However, the mint price charged in this transaction was administratively determined, underscoring the public nature of money creation and a right on the part of the state. Very importantly, the unit of account was politically determined so that money did not travel on the basis of its precious metal content, i.e., the principle of nominalism ruled. And yet, the legal framework underpinning this system had the twin objectives of maintaining sovereign authority while eliciting political co-operation on the part of merchants who had bullion. Merchants would only bring in the bullion if the mint price (the number of coins returned to them) was high enough. Clearly the cash premium of the coins was an important factor in private sector decision-making about their own coin/bullion portfolio choice.[70] If the mint price and/or alloy content of coin were unsatisfactory and/or another country's government offered a 'better deal' to merchants, the flow of bullion to the mint could slow down. Thus the possibility of capital flight was a real one,[71] an outcome that was a privilege granted by the government to merchants (i.e., to hold domestic or foreign coin), which the former had a no-right to stop. Put simply, given a particular bundle of entitlements undergirding money, 'groups in a community may strategize methods of accounting in order to escape from an official unit of account to another anchoring coin that they prefer'.[72] Domestic individuals could also attempt to bring in foreign coin but, parallelling protectionist industrial policies[73] foreign coin was prevented by the government from entering the country.[74] Here then, the jural relations were such that private individuals were disallowed from importing foreign coin and the government implemented its right to enforce protectionism.

The Case of Mixed Money, a landmark case with far-reaching power beyond commodity money, upheld the principle of nominalism. This makes theoretical sense since governance ultimately has to rest on a viable political economy with the latter undergirded by uniform monetary measures of property, contracts, and torts. Even in a commodity money system, the count value of money, as opposed to its metal content, has to prevail since if the precious metal content of coin changed, the relative appreciation or depreciation of the currency (count value relative to metal content) would destabilize contracts such as debts, taxes, or rents, thereby destroying the principle of equality in contracts.[75]

The principle of nominalism also prevails under fiduciary currencies; ignoring dollarization, the exchange rate with respect to foreign currencies is generally of no import in domestic debt contracts (e.g., mortgages). In short:

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[70] Ibid., at 64.

[71] Ibid.

[72] Ibid., see North and Weingast, *infra* note 116, at 59. See also Desan's discussion (ibid., at 127) regarding people's occasional desire to convert the domestic currency into bullion so as to send it abroad in order to be reconverted into a foreign currency. As she points out, sometimes this was done for arbitrage purposes.

[73] See Chang, *supra* note 57.

[74] See Desan (2014), *supra* note 21, at 96.

[75] Ibid., at 271 and Ch. 3.

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> The foundational nature of public obligation comports with the government's primary role in setting the prevailing standard or unit of account. It suggests as well the imperative that the government maintain that unit uniformly over time. Otherwise, people (as well as businesses and even governments) could be paid in one unit of account and taxed in another. The bait and switch would hurt people holding money individually and upset the system more generally by undermining the existence of a stable currency.[76]

Power inequalities played a central role in English monetary history. This is particularly true with regard to taxation. The free minting period relied on 'strong money' (i.e., coin with high metal content) with heavy taxes to undergird their fiscal value. As a mutually beneficial political arrangement between landowners and the Crown, such a policy doubly disadvantaged the poor, who faced a chronic shortage of small-denomination coins and bore the brunt of the taxes.[77] Recourse to private credit was thus a major imperative for the poor and excessive debt was the consequence, with disputes and litigation taking place in the courts.[78] In short, political authority spread artery-style through the body economic with the legal design of money structuring class relations and the distribution of wealth and power.

The chronic shortages of cash persisted for centuries even as money creation evolved in a different direction, culminating in non-interest-bearing currency. The centrality of public authority persisted but the latter was hardly omnipotent. Various forms of public debt arose to finance the government's growing fiscal needs, however, the Crown (under Charles I for one) faced challenges in obtaining relatively low interest rate loans in credit markets: 'sovereign immunity combined with the possibility of default made the monarch a bad risk'.[79] Treasury Orders (TOs) incentivized investors to loan to the government at a profit and were tied to revenue streams which gave them credibility as debt instruments. While TOs furnished some liquidity to the acute, cash-parched seventeenth-century economy,[80] they did not have the legal backing as cash to be used to pay taxes.[81] Thus, the government faced a fiscal crisis[82] with its combination of growing expenditures and insufficient tax revenues.

The growth of public debt, via the sale of bonds by the government to private investors, was the 'solution' to the problems of public finance and the economy's cash shortage issue, although this result was itself the culmination of a long turbulent process. Over time this enlistment of the private sector began to be coupled with a new ideational framework which sought to recast profit-seeking behavior (via the

[76] C. Desan, 'Beyond Commodification: Contract and the Credit-Based World of Modern Capitalism', in D.W. Hamilton and A.L. Brophy (eds.) *Transformations in American Legal History: Laws, Ideology, and Markets. Essays in Honor of Morton J. Horwitz* (2010), Vol. II, 111, at 113. Quoting the Supreme Court (*Norman v. Baltimore & O.R. Co.*, 294 U.S. 240, 304 (1935)), Desan observes at 114 that '"the authority to impose requirements of uniformity and parity" is "an essential feature" of controlling a currency in "accord with the usage of sovereigns"'.

[77] See Desan (2014), *supra* note 21, at 153 and 165.

[78] Ibid., at 218 and 219.

[79] Ibid., at 243.

[80] Ibid., at 255

[81] Ibid., at 261.

[82] Ibid., at 264.

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provision of loans to the government) as a patriotic duty.[83] Here then we have the origins of the familiar market ideology that equates the pursuit of self-interest with the social good.

The ideational framework must have also created a legal consciousness that elevated the political power of financiers, culminating in *The Case of the Bankers*. This landmark case, in which creditors successfully sued the government, arose from a set of delayed debt payments by the Crown, beginning with Charles II's Stop of the Exchequer (1672).[84] By setting the stage for fiduciary currency, *The Case of Mixed Money* and *The Case of the Bankers* are jointly of enormous theoretical significance. If the former case reinforced sovereign prerogative to determine the nature of money,[85] the latter legitimated the political power of capitalist investors by, more broadly, stabilizing contracts and thus giving them the confidence to engage in profit-making activities. Thus, at last, over a period spanning several centuries, a model of money creation involving both the incentivization as well as the disciplining of investors had been installed, albeit in a highly turbulent manner. This fundamental logic became the basis of money creation with the enlistment of the BoE by the government.

To summarize, the harnessing of the profit motive for a public purpose had become central to the money creation process in England by the seventeenth century. In the new system, the Crown borrowed from the BoE, paid the latter back in its own note with interest, and also injected it into circulation when undertaking public expenditures. Citizens were willing to hold this note, which was non-interest bearing, because it satisfied the need for liquidity and was accepted as taxes, both features determined by the state-enforced jural relations.[86] The public debt of the Crown to the BoE had now assumed the characteristic of *money*, a *denouement* that was the culmination of many centuries of unexpected twists and turns. In the same vein, in the American context after independence private bankers were incentivized by the legislature to augment the money supply by creating interest-earning credit on demand. Thus, then as now, banks sat atop a public base as Morgan Ricks and others have argued.[87]

In the eighteenth century, the British government's borrowing capacity was undergirded by a tax system in which excise, customs, and land taxes made up the lion's share of revenue collected; of these, excise taxes (which are generally considered regressive) constituted 'the most important source of revenue'.[88] On the other hand, public debt promoted enormous wealth accumulation, especially by financiers. In short, the legal foundation of the new public finance system allocated wealth and power in a particular way.

[83] Ibid., at 281 and Ch. 7 more generally. See G. Alexander, *Commodity and Propriety: Competing Visions of Property in American Legal Thought 1776-1970* (1997) for parallel ideological processes occurring in the US with the growing commercialization of society.
[84] See Desan (2014), *supra* note 21, at 281.
[85] Ibid., at 269 and 270.
[86] Ibid., Ch. 8.
[87] See Desan, *supra* note 27; and M. Ricks, *The Money Problem: Rethinking Financial Regulation* (2016).
[88] See Desan (2014), *supra* note 21, at 387.

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But the story of constitutional money does not end here. It was only in the early to midnineteenth century that the decisions of a number of court cases (e.g., *Carr* v. *Carr*) allowed banks to treat funds attracted via deposits as their own as opposed to remaining the property of the depositor.[89] In the absence of this legal permission to engage in fractional reserve banking, the use of depositors' funds to make further loans would have constituted theft. Thus, as the CLS tradition has emphasized, property is not a self-defining category but one which can take many forms because of varying bundles of jural relations underpinning them.[90] Finally, and crucially, the ability of banks to create money 'at the stroke of a pen' rested atop the fiscal-backed supply of high-powered money. In short, the private incentivization/public discipline nexus persisted with this new institutional form of money creation.

Scholars who study the history of industrialization will find in the legal history of money in England a fascinating parallel to the literature on state-led industrialization, pioneered by authors such as Alice Amsden, Ha-Joon Chang, and Peter Evans, which has also emphasized the selective disciplining and incentivization of capitalists by the state. As with the public/private enmeshment in this literature, consider the relationship between the government and the BoE investors who were granted monopoly privileges to issue legal tender over and above rival investors of the National Land Bank.[91] In fact the government 'planned for its [the Land Bank's] demise'.[92] In the meantime, 'in the spring of 1697, the directors of the Bank of England capitalized on the National Land Bank's failure. Demanding relief from future competition, they obtained legislation that granted the Bank monopoly stature as long as its charter lasted'.[93] Thus:

> While the practices that constituted the novel way of representing value were rooted in public debt, they licensed a new agent, an investment consortium, to issue notes at a profit. 'Making money' thus depended directly on the decisions of investors. In those circumstances, the matter that later generations might call monetary policy seemed to be a function of the market, although it stood atop a public base.[94]

At the end of the day, the Whig promoters of the BoE were 'more adept than their Tory competitors at financing war, enlisting the aid of the manufacturing and commercial classes, and developing the industry of public and private credit'.[95] In short BoE investors were able to exploit their power, a phenomenon that would resonate

[89] 'Money, when paid into a bank, ceases altogether to be the money of the principal; it is then the money of the banker, who is bound to return an equivalent by paying a similar sum to that deposited with him when he is asked for it. The money paid into the banker's, is money known by the principal to be placed there for the purpose of being under the control of the banker; it is then the banker's money; he is known to deal with it as his own; he makes what profit he can, which profit he retains to himself.' (*Foley v. Hill* (1848) 2 HL 28, 38–9; 9 ER 1002, 1006–1007). Cited from Desan (2014), *supra* note 21, at 393 and 394.

[90] J.W. Singer, 'Property', in D. Kairys (ed.), *The Politics of Law: a Progressive Critique* (1998), 240; J.W. Singer, *No Freedom without Regulation: the Hidden Lesson of the Subprime Crisis* (2015).

[91] See Desan (2014), *supra* note 21, at 368–9. For literature on state-led industrialization see *supra* notes 57 and 58.

[92] Ibid., at 369. Officers of the BoE were associated with the Whig Party while the National Land Bank's promoters and supporters were Tories (ibid., at 368).

[93] Ibid., at 369.

[94] Ibid., at 329

[95] Ibid., at 370.

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with scholars in the state-led industrialization literature.[96] In fact, one can imagine that the political power of BoE investors went up the more the BoE became the 'central nervous system' of public finances and financial markets – even though public authority undergirded those markets. We are far away here from the MMT methodology in which neither power struggles nor the incentivization and political power of private investors play any central role.

The MMT framework follows a logic that places enormous power, ability, and autonomy in the state to orchestrate the capitalist economy according to policymakers' choices. But this is precisely the methodology criticized by Morton Horwitz in his discussion of New Deal historians:

> By and large, the New Deal historians were much more concerned with finding evidence of governmental intervention than they were in asking in whose interest these regulations were forged. To a surprisingly great extent, they treated all instances of state intervention as equally proving their point …
>
> One of the most important consequences of this approach is that the historical writing of the last generation tended to ignore all questions about the effects of governmental activity on the distribution of wealth and power in American society. They tended to assume that virtually all regulation was in the public interest without ever providing any real criteria for such conclusion.[97]

In a vein that parallels Christine Desan's work, Horwitz noted:

> During the eighty years after the American Revolution, a major transformation of the legal system took place, which reflected a variety of aspects of social struggle. That the conflict was turned into legal channels (and thus rendered somewhat mysterious) should not obscure the fact that it took place and that it enabled emergent entrepreneurial and commercial groups to win a disproportionate share of wealth and power in American society.
>
> The transformed character of legal regulation thus became a major instrument in the hands of these newly powerful groups.[98]

After all, as Horwitz observed with regard to the American case, it is not as though the state taxed the wealthy to finance its activities; instead it *borrowed* from them, thereby enabling them to increase their wealth.[99] This observation by Horwitz would, of course, resonate with Marxist authors. However, with the notable exception of Ellen Meiksins Wood, who draws in part on E.P. Thompson and Robert Brenner in criticizing the base/superstructure approach,[100] the Marxist tradition, for the most part, accepts the separation of the 'economic' from the 'political' (or the 'private' from the 'public' spheres). On the other hand, for Horwitz and the CLS tradition the law is constitutive of markets as Gordon, also drawing in part on Thompson and Brenner, discussed in his classic article.[101]

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96 A.L. Murphy, 'Dealing with the Threat of Reform: The Bank of England in the 1780s', in A.T. Brown, A. Burn, and R. Doherty (eds.), *Crisis in Economic and Social History: A Comparative Perspective* (2015), 283, at 284; E.M. Kim, *Business Business, Strong State: Collusion and Conflict in South Korean Development, 1960-1990*, (1997).

97 M. J. Horwitz, *The Transformation of American Law 1780-1860*, (1977), at xiv.

98 Ibid., at xvi.

99 Ibid., at xiv.

100 E.M. Wood, *Democracy Against Capitalism: Renewing Historical Materialism* (2016).

101 See Gordon, *supra* note 5.

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There is a long tradition in intellectual history, spanning Aristotle and Nicholas Oresme to the Mercantilists and the Physiocrats, which has likened money to blood, or as Jerah Johnson put it in his review essay, seemingly quoting these authors, 'Money is the Blood of the State'.[102] This metaphor emphasizes the fact that money is integral to the body politic and economic. One can thus understand, from this perspective, the intellectual antecedents of the constitutional theory of money which locates money creation as the deliberate act of a polity to promote both political governance and private production and exchange.[103]

And yet there is also a parallel strand in money's intellectual history which treats money not as the product of a political community but rather as something apolitical and natural. This view, generally identified with David Ricardo and David Hume in their analysis of international trade, equated gold with money which, like water, would find its own level under free trade. Via the operation of the quantity theory of money (QTM) free trade in these authors' view would also bring about balanced trade with the appropriate market-driven distribution of specie. Monetary inflows into trade surplus countries would raise prices there; conversely, monetary outflows from trade deficit countries would lower their prices. This was also the position of the Currency School.[104] The consequence of these relative international price movements would be balanced trade.

This money-price linkage was rejected by authors in the Banking School, Marx, and later on Harrod and Keynes.[105] For these authors, international money flows impact interest rates, which would fall in surplus countries and rise in deficit ones because surplus countries' banks would accumulate foreign exchange reserves while those of deficit countries would experience the opposite. Finally, given the absence of relative international price variations, a major implication of this alternative framework is that trade imbalances are likely to be persistent.[106] International money will not find its own level.

Here again, insights from the constitutional money approach are important. With the BoE and UK commercial banks at the heart of the Gold Standard[107] it is no surprise that bankers profited enormously from the country's balance of payments transactions. During periods when England experienced trade deficits, the bankers benefited from charging high domestic interest rate on loans; during surplus periods they charged high foreign interest rate on loans to countries experiencing deficits and shortfalls of foreign exchange. The legal monetary architecture clearly benefited the financial sector, which public authorities had promoted over several centuries.

[102] J. Johnson, 'The Money = Blood Metaphor, 1300 – 1800', (1966) 21 *The Journal of Finance* 119.

[103] See Desan (2014), *supra* note 21.

[104] L.R. Wray, *Money and Credit in Capitalist Economies* (1990). See also David Ricardo's chapter 'On Foreign Trade' in his *On the Principles of Political Economy and Taxation* (1817), in which he likened foreign trade to barter, with money finding its own level, available at www.marxists.org/reference/subject/economics/ricardo/tax/ch07.htm (accessed 19 January 2018).

[105] A.M. Shaikh, *Capitalism: Competition, Conflict, Crises* (2016); M. Smith, *Thomas Tooke and the Monetary Thought of Classical Economics* (2011); R.F. Harrod, *International Economics* (1957); W. Milberg, 'Say's Law in the Open Economy: Keynes's Rejection of the Theory of Comparative Advantage', in S. Dow and J. Hillard (eds.) *Keynes, Uncertainty and the Global Economy: Beyond Keynes* (2002), Vol. II, at 239.

[106] See Shaikh, *supra* note 105.

[107] See Desan (2014), *supra* note 21, at 418.

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Finally, the likening of money to either water or blood[108] is significant in two further respects. First, the water characterization of money by Hume and others essentially naturalizes the market as a fundamentally barter system. Money does not need to be created so that law and politics evaporate in this framework. On the other hand, the money-interest rate link centralizes the role of banks and thus the politics and the jural relations undergirding these institutions.

Second, *contra* the tendency by the Bullion Committee and others to naturalize markets,[109] trade performance and industrialization were *always* a function of public policies and not spontaneous 'market forces'.[110] This is essentially consistent with the argument made by Daniel Tarullo[111] regarding the fundamental embeddedness of public policies in markets. Thus, given the monetary nature of markets, money creation is logically profoundly political. For example, an examination of the Corn Laws, before and after their repeal, would reveal the politics of the British government's development strategy vis-à-vis agriculture and manufacturing[112] and thus, implicitly, the jural relations undergirding trade policy and foreign exchange accumulation. Quite simply, in regard to money, 'there was no invisible hand at work in the dawn of modern capitalism; the fingerprints of public authority, along with those of its business allies and the larger community, were all over the new medium'.[113] Thus 'making money' in the international economy was also always a function of public policies and the law; there was no 'natural flow of commerce' as the Bullion Committee claimed.[114] Significantly then, the constitutional money approach fills an important lacuna in the state-led industrialization literature[115] since the latter is silent about how the 'blood' that animates markets and industrialization gets created. To conclude this discussion, such a synthesis points to a *constitutional money theory of industrialization.*

5. 'Clear and well-defined' property rights versus legal indeterminacy

In line with the New Institutionalist framework, North and Weingast[116] argue that The Glorious Revolution was crucial to the creation of 'clear and well-defined' property rights and contracts by limiting the power of the state to interfere in the economy. Abuse of power in this framework arises primarily from public authorities

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108 See Desan (2014), *supra* note 21, 'Conclusion'.
109 Ibid., at 418.
110 See *supra* notes 57 and 58.
111 See *supra* note 60.
112 C. Schonhardt-Bailey, *From the Corn Laws to Free Trade: Interests, Ideas, and Institutions in Historical Perspective* (2006); P.S. Ho, *Rethinking Trade and Commercial Policy Theories: Development Perspectives* (2010).
113 See Desan (2014), *supra* note 21, at 328.
114 Ibid., at 418.
115 See *supra* notes 57 and 58.
116 D.C. North and B.R. Weingast, 'Constitutions and Commitment: The Evolution of Institutions Governing Public Choice in Seventeenth-Century England', (1989) 49 *The Journal of Economic History* 803.

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and thus appropriate legal 'handcuffs' are needed to limit state action, restrain 'fiscal profligacy' and create efficient markets.[117]

It is, of course, true that the stability of contracts and property is necessary for development. But the New Institutionalist view is off the mark for a number of reasons.[118] First, the relatively stable free minting system, tallies, and Treasury Orders pre-dated the Glorious Revolution and the onset of the *laissez-faire* period. Further, as discussed by Ha-Joon Chang[119] in regards patent laws and David Kennedy[120] more generally, there are no fundamental legal-institutional principles which are prerequisites to development. Instead, following the CLS view, for economic development to take place there are 'multiple trajectories of possibility',[121] each the consequence of political struggles and compromises. The post-Glorious Revolution produced *one* set of institutional prerequisites for economic development, i.e., one of the other types of bundles of rights which existed before.

Perhaps the post-Glorious Revolution set of rights was the most 'efficient'? This brings up the second problem with the North and Weingast argument. In the neoclassical view excessive public debt/GDP growth implies 'fiscal profligacy'. However, empirically one sees dramatic increases in public debt in the period 1800 and 1821 and again between 1914 and 1946 (see Figure 1), long after the English had established the 'efficient' political/legal infrastructure as defined by the New Institutionalists. In both those periods the public debt/GDP ratio went up to 250 per cent.

In fact, if the attainment of central bank independence is the epitome of market efficiency, the data in Figure 1 is a puzzle from the orthodox view: The BoE remained in private hands, although functioning like a publicly regulated utility, until it was nationalized in 1946 and then eventually granted operational independence in 1997. From a neoliberal perspective, one would have expected high or rising public debt/GDP for much of its history prior to 1997 given its lack of independence – especially under Labour governments. From a CLS perspective, on the other hand, Figure 1 is not at all a puzzle: One would clearly expect multiple legal and political trajectories, not to mention macroeconomic ones, over the 1694–1997 period, which would explain both rising, falling, and relatively stable public debt/GDP ratios. Public choice theory, which informs North and Weingast's argument, is fairly limited in its belief that optimal legal structures can impose discipline on politicians and create 'efficient' markets.

Third, the post-Glorious Revolution political and legal settlement involved the stabilization of one set of private property rights but, as North and Weingast point out,[122] this privileged the wealthy. These elites benefited inordinately from the new system of public finance and the broader thrust of public policies which by

[117] For further elaborations along these lines see W.E. Oates, 'An Essay on Fiscal Federalism', (1999) 37 *Journal of Economic Literature* 1120; B.R. Weingast, 'The Economic Role of Political Institutions: Market-Preserving Federalism and Economic Development', (1995) Spring *Journal of Law, Economics, and Organization* 1.

[118] See Desan (2014), *supra* note 21.

[119] See Chang, *supra* note 57.

[120] D. Kennedy, 'Some Caution About Property Rights as a Recipe for Economic Development', (2011) 1 *Accounting, Economics, and Law* 1.

[121] See Gordon, *supra* note 5, at 112.

[122] See Desan (2014), *supra* note 21, at 292.

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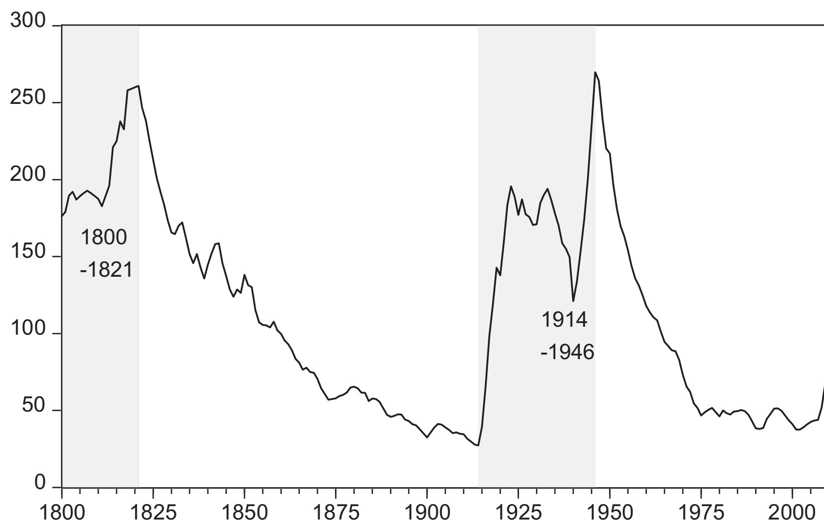

Figure 1: British Public Debt/GDP (%) 1800–2011. Source: P. Mauro et al., 'A Modern History of Fiscal Prudence and Profligacy', (2013) 13/5 *IMF Working Paper*, International Monetary Fund, Washington, DC (data downloaded from www.imf.org/external/np/fad/histdb/).

mid-nineteenth century led to Britain's global dominance. But this reinforcement of private property and the creation of 'efficient' markets were selective as the post-Glorious Revolution settlement also produced the disastrous government-sponsored South Sea venture (which involved slave trading) as well as draconian taxation measures imposed on the working class and peasantry.[123]

It may be pertinent to mention here that North and Weingast's view regarding the post-Glorious Revolution settlement is also selective given that the development of capitalism was intimately connected to the growth of the slave economy, in particular in the American South because of the centrality of cotton, as a number of authors have discussed.[124] The basic argument here is that capitalist industrialization was fueled by cotton production, and this in turn increased the demand for slaves who grew the cotton. Thus, slavery and capitalism were mutually constitutive.

One would therefore expect to see an increase in the relative price of slaves as industrialization proceeded in the UK and US. See Figure 2, which plots real GDP/capita in the UK and US versus the relative price of slaves in the American South (all in natural logs):

What theoretical lessons can be drawn from these striking correlations?[125] Per the constitutional money view, the creation of money is intimately connected to governance and the politics of the former legally allocate wealth and power in

[123] Ibid., Ch. 7.

[124] E.E. Baptist, *The Half Has Never Been Told: Slavery and the Making of American Capitalism* (2014); S. Beckert, *Empire of Cotton: A Global History* (2015).

[125] In each case the correlation coefficients linking the two variables exceed 0.8 and are highly statistically significant.

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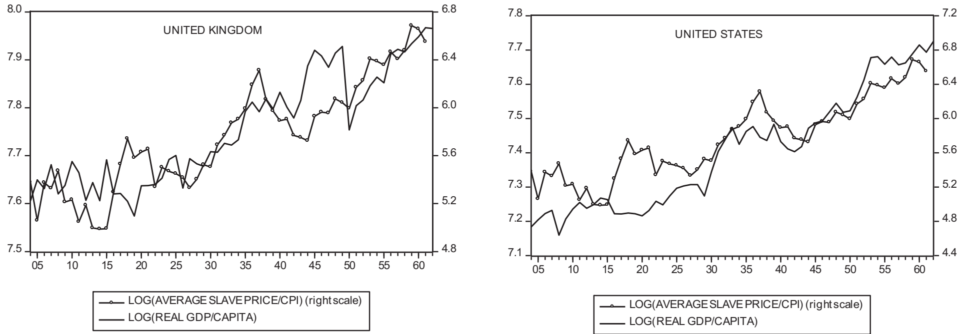

Figure 2: Average Slave Price/CPI and Real GDP/Capita in the United Kingdom and United States, 1804–1861. Sources: (a) Slave and CPI data from Historical Statistics of the United States (b) Real GDP per capita data from "Maddison Project Database" (www.ggdc.net/maddison/maddison-project/home.htm www.imf.org/external/np/fad/histdb/)

particular ways. Contrary to the New Institutionalist view, the creation of representative democracy in both countries did not lead to the spontaneous development of 'free markets' with liberty of property and contracts for all. In fact, the capitalist market economy was interlaced with the development of slavery and the politics of money penetrated and undergirded both types of economies, one with free wage labour, and the other with slavery. The jural relationships at the heart of slavery[126] can only have been possible if human beings were commodified (i.e., bought and sold in *money* form) which, of course, was a political project all the way through. The fact that slavery was eventually banned does not take away from the basic CLS principle that there simply is no 'pure' form of capitalism with a unique set of laws functionally engineered onto it. Capitalist markets are built on varieties of politically determined legal foundations:

> In fact, a community determines which goods and services can be alienated, and thus what counts as a 'commodity', when it decides what items or services money can buy ... [T]ransactions involving money would not be enforced if they were improperly made or inappropriately targeted a resource that could not be considered a 'commodity'. Later societies would decide, notoriously, to allow the sale of Africans ... Those debates are joined by a myriad of others, contests over what else is 'for sale', from honours to votes, sex to kidneys.[127]

6. Conclusion

Monetary history shows that the nominalist principle, in which the political authority legally created the unit of account, was the ruling one because a stable monetary

[126] 'Slavery is a legal relationship: It is precisely the slave's bundle of jural rights (or rather lack of them) and duties vis-à-vis others (he can't leave, he can't inherit, he has restricted rights of ownership, he can't insist on his family being together as a unit, etc.) that *makes* him a slave'. From Gordon, *supra* note 5, at 103 (emphasis in original).

[127] C. Desan, 'Money as a Legal Institution,' in D. Fox and W. Ernst (eds.), *Money in the Western Legal Tradition: Middle Ages to Bretton Woods* (2016), 18 at 30–1.

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system is central to governance. Such a stable unit of account, becoming the basis of property, contracts, and torts, cannot arise through spontaneous 'market forces' and *maintain* itself without a prior legal and political foundation. This view challenges the opposite one in which the law is epiphenomenal and accommodates itself to the 'needs' of the market system as it teleologically converges from commodity money to fiat money. In fact, this article has critiqued the New Institutionalist focus on 'clear and well-defined' property rights to promote efficient markets and economic development.

Nothing in the constitutional money framework suggests that the state has the autonomy to dictate market outcomes. This is particularly true because money creation has always entailed *incentivizing* the private sector; with the rise of capitalism it specifically involved harnessing the profit motive for the public goal of promoting a monetary economy. Such a process necessarily led to private wealth accumulation and power struggles over the legal foundations of the economy:

> Legal forms and practices are political products that arise from the struggles of conflicting social groups that possess very disparate resources of wealth, power, status, knowledge, access to armed force, and organizational capability.[128]

For example, if the *current* laws allocate money and power in a particular way, then that could potentially entail *future* political challenges to the *status quo ante*. In short:

> If the program of Realists was to lift the veil of legal Form to reveal living essences of power and need, the program of the Critics is to lift the veil of power and need to expose the legal elements in their composition.[129]

Given the above, this article has explored the various ways by which monetary instability can occur, an instability that is of course at the heart of Fernand Braudel's *longue durée* framework, with its focus on turbulence and change. Following Duncan Kennedy's analysis, it has been argued that the indeterminacy criterion, coupled with potential challenges to the background laws, produces non-linear outcomes. Such non-linearities, discussed by several law scholars,[130] provide very limited information about the future. Simply put, the indeterminacy criterion is the basis of Keynesian uncertainty since it is very difficult to predict *ex ante* what sets of combinations of background laws will recrystallize when current ones begin to dissolve.

Business opposition to 'full employment' policies, the fiscal sociology of taxation, capital flight, and foreign debt are further themes discussed here to analyze the various mechanisms that can destabilize a currency, including creating pressures for currency substitution. Here too the indeterminacy criterion plays a key role in (de)stabilizing the currency.

[128] See Gordon, *supra* note 5, at 101.
[129] Ibid., at 109.
[130] See, e.g., D.A. Kysar, *Regulating From Nowhere: Environmental Law and the Search for Objectivity* (2010), and references cited therein.

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Finally, the *longue durée* framework underpinning the constitutional theory of money is strikingly resonant with EP Thompson's observation regarding the ubiquity of legal complexity:

> For I found that law did not keep politely to a "level", but was at *every* bloody level; it was imbricated within the mode of production and productive relations themselves (as property-rights, definitions of agrarian practice) ... it was an arm of politics and politics was one of its arms ... it contributed to the definition of the self-identity both of rulers and of ruled; above all, it afforded an arena for class struggle, within which alternative notions of law were fought out.[131]

In fact, the constitutional monetary approach captures a methodology, both in EP Thompson as well as Robert Brenner's classic work on the European peasantry.[132] What is evident in all these classic studies is that the *prior* historical legacy of legal structures – both constituted by and constitutive of political struggles – accumulated over centuries, provides the context to the current nature of markets, power struggles, and thus the bundle of jural relations undergirding money. This *longue durée* framework denaturalizes markets and thereby reveals the profoundly political and legal anchoring of money as it changes historically. For example, given the centrality of taxation in anchoring the value of money, the relevance of politics and power struggles for the latter can clearly be seen in the political history of taxation.[133] In short, if MMT is a freeze frame image of the tax-money nexus, the constitutional money view describes an ongoing moving image; the latter is a *process* analysis with the *potential* for instability built into its 'genetic composition', so to speak.

At the end of the day, if a country's monetary system is a reflection of its governance capacity, theoretical analysis has to explore how such a monetary system and thus sovereignty can be *both* created and, at times, destabilized. This investigation is at the heart of the current article.

131 E.P. Thompson, *The Poverty of Theory and Other Essays* (1978), 96 (emphasis in original).
132 E.P. Thompson, *Whigs and Hunters: The Origin of the Black Act* (1975); R. Brenner, 'Agrarian Class Structure and Economic Development in Pre-industrial Europe', (1976) 70 *Past and Present* 30. See Gordon's (*supra* note 5) discussion of these authors.
133 On the political history of taxation in England see A.J. Cockfield and J. Mayles, 'The Influence of Historical Tax Law Developments on Anglo-American Laws and Politics', (2013) 5 *Columbia Journal of Tax Law* 40.

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