Beggar Thy Neighbor: A History of Usury and Debt

Charles R. Geisst. 2013. Philadelphia: University of Pennsylvania Press.
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Williams v. Walker-Thomas Furniture Co. (1965) is a court case that involved credit arrangements. The furniture company sold household items and offered installment contracts with the sales. The plaintiffs were described by counsel as relatively unsophisticated and with little money income. The contracts contained a provision that all payments would be credited pro rata on all outstanding accounts. The practical effect of the provision was that if a person bought one item on the installment contract, paid some of it off, and then purchased another good, future payments were applied to both purchases. Effectively, the first good was not paid off until both were paid off. If the purchasers could not make payments, both items could be repossessed by the store, even if the total payments were more than the price of the first item purchased. The courts ruled the contract was unconscionable and therefore unenforceable.

The courts held that the firm was taking advantage of poor people who lacked options in credit markets. Defenders of the contracts argue that selling on credit to lower-income households involves more risk, and the firm needs compensation for the risk. Higher interest rates would be one approach, but many states at the time had limits on interest rates. The provision in the contract offered a way for the firm to be compensated without charging higher interest rates. Without the provision, less credit would be available to lower-income households. The issues raised by the case are similar in many ways to the issues raised in Geisst's book on usury. Geisst shows that the history of usury is one that often forced a similar dilemma on society: interest tends to work to the disadvantage of the poor but the poor often are in need of credit.

Beggar Thy Neighbor is the most recent book concerning debt to appear in recent years. David Graeber's *Debt: The First 5,000 Years* (2011) and Felix Martin's *Money: The Unauthorized Biography* (2014) are two others, with the latter arguing that money is debt. *Beggar Thy Neighbor* is less polemical than the other two books, but also not as entertaining. It offers a comprehensive examination of the history of usury, primarily in the West, over three millennia. Geisst notes that the history of usury can be thought of as an exercise in the history of ideas, of interest mostly to economic historians. He adds, "That is true but it ignores the subtext, which has proved to be one of the most powerful notions in all societies for three thousand years. As part of general natural law, it reflects societal notions of fairness and equity that have transcended ancient, medieval, and modern societies" (pp. 5–6).

After an introduction and overview of the book, Geisst considers usury from a historical perspective. He begins with the ancient world—Aristotle and Cicero—as well as some passages from the Hebrew Scriptures. Aristotle condemned interest; Cicero drew a distinction between simple interest and compound interest, condemning the latter; and the Hebrew Scriptures permitted interest on loans to foreigners but not to fellow Israelites. All three ideas can be seen throughout history.

Alongside the Old Testament, Roman Law was the other classical source which influenced later developments concerning lending at interest. While several passages from the Old Testament could have been used, the passage from Deut. 23:19-20 dominated. Here, as just noted, the Hebrews are told they should not lend at interest to other Hebrews, but could do so to foreigners. However, early loan contracts show that they did lend to Hebrews at interest, and the simple interest rate tended to be 12 percent. This rate was seen as "ratified" by Nehemiah and held for two thousand years. (See Neufeld [1954] for the relevant citation.) Geisst makes a strange claim, though. In discussing the development of Canon Law, Geisst says that the Old Testament and Roman Law were primary. "There is no substantial mention of the practice in the New Testament, except for a passage in Matthew (16:28) that mentions 12 percent monthly interest as prevalent at the time…." (p. 20). Clearly, his citation is incorrect, because it has nothing to do with debt or interest. Matthew 25:28 is part of the Parable of the Talents and may be the passage he meant. However, there is no mention of an interest rate there—two of the slaves doubled the money, but the time period is described as "a long time."

In antiquity, the terms *usury* and *interest* were usually interchangeable. The idea that usury involves excessively high rates of interest came later, although Geisst notes that one can argue that it always referred to excessive interest—with any positive rate of interest seen as excessive. Roman law permitted simple interest but condemned compound interest. The latter was referred to as *usurae usararum* and referred to adding to the principal of an unpaid loan.

An important distinction was frequently made between loans for business or commercial activities, and loans for consumption spending. The former were often permitted; the latter faced condemnation. Geisst suggests that the sumptuary laws were related to usury laws. European societies enacted sumptuary laws for over a thousand years. "People were willing to borrow in order to purchase items that allowed them to aspire above their station in life, a practice those in power deemed inimical to the common good, so consumption was often banned" (p. 8). These laws were designed to prevent those in lower classes from mimicking the upper classes. People were supposed to know and keep in their proper place.

While authorities, especially church authorities, condemned usury for centuries, lending at interest occurred in all ages. Often this involved subterfuge that fooled almost no one, but allowed authorities to turn a blind eye. In fact, it was often church officials who lent funds at interest. Usurers were encouraged to seek forgiveness late in life and to make restitution. Many people made provisions for restitution in their wills.

Geisst identifies the year 1202 as an important date for the practice of usury. Fibonacci wrote *The Book of the Abacus*, a treatise devoted to calculating using Arabic numbers. He included material on decimals, fractions, and square roots, among others. Interest rate calculations were also a topic in the book. The Holy Roman Emperor Frederick II was interested and posed questions to Fibonacci, who "…demonstrated to the royal audience how many rabbits could be expected to breed in a year after a pair was left alone (377 pairs)" (p. 39). Fibonacci had other interests that rate examples in his book. For example, if a man has one denaro and he expects it to double every five years, how many would he have after one hundred years? Analysis of his calculation makes it clear that he uses an interest rate of 14.355 percent compounded semi-annually, but he does not specify the interest rate in the book. After Fibonacci, other people developed tables to help with calculations, but again failed to specifically say they were using compound interest.

Commercial developments gradually led to changes. Before insurance existed, the traditional way of sharing risk in business was to form a partnership. As insurance became available during the 14th century, the plans used vague language to structure a partnership that got around the restrictions on paying interest. Annuities developed during the same time period, and managed to escape the usury prohibitions. They involved established financial contracts and they fit the definition of usufruct in Roman law. Geisst notes, "The idea of a loan repaid as a fixed payment over a specified number of years is one of the oldest…financial products in history" (p. 68). There is evidence of such contracts in use in ancient Babylon and Egypt. It was often government bodies that utilized annuities to obtain borrowed funds. The additional feature that helped keep annuities legal was that they involved people with some wealth, not the poor.

Usury and debt often involved sovereigns. Wars were expensive and taxes could be difficult to collect and were unpopular. Two solutions were to borrow funds and to debase the currency. Both were used. But sovereigns also were known to default on debt, especially if the lenders were foreigners or Jews.

A confluence of factors slowly led to serious reconsideration of usury and interest. These included increased maritime trade, the increased use of money in the economy, the rise of banking in Italy, and the Reformation, especially the Calvinistic side of the Reformation. Grotius' *The Rights of War and Peace* included a refutation of Aquinas' treatment of usury, and this "…proved to be a death knell for the pietistic treatment of usury and usurers" (p. 87). Over time, a distinction was drawn between usury and interest. But compound interest continued to be suspect.

In a chapter entitled "The Great Experiment," Geisst discusses the debate that developed over interest. "After almost four millennia of prohibitions and condemnations, the abolishment of usury ceilings was an experiment that became an inexorable force in the face of rapid social and economic developments" (p. 137). What would happen if usury ceilings were lifted? Would there be chaos? The debate went on in both Britain and the newly-formed United States. Ricardo urged repeal of the ceilings. In Britain, the ceilings were finally repealed in 1854. Usury laws in the United States tended to operate at the state level. It took many more years before many states abolished their ceilings, and a number of states still have them. For example, Michigan has an interest rate ceiling of 25 percent.

Once the modern industrial and financial economy formed, there continued to be innovations in forms of debt. The concept of leverage appeared in the 18th century. Bankruptcy laws and policy were at the center of the debate between Federalists and Jeffersonians. Hamilton sought a bankruptcy law with a vision based on manufacturing while Jefferson's vision was an agrarian society.

Wars generated pressure on government finance. Debt from the U.S. Civil War dwarfed previous levels of government debt. Jay Cooke developed a technique for selling bonds in small denominations to working people—an approach used by the government in World Wars I and II. Early in the 20th century, Gustav Cassel described usury as arising from defects in the organization of credit markets. Banks tended to lend only to businesses; the Bank of Italy in California was the first bank to seek retail customers. Geisst argues that for consumer markets to develop and flourish, it was necessary to allow consumers to have greater latitude in how they paid for purchases. Installment buying became more common, although credit usually required collateral. Poorer households did not have access to the normal credit markets, often turning to either pawnshops or loan sharks.

The first credit card, Charg-It, was used by local merchants in New York City. The year was 1946. Diners' Club began in 1950. The first bank credit card was offered by the Franklin National Bank, but required balances to be paid off each month. Bank of America (the former Bank of Italy) was the first to offer the modern credit card. No longer was credit tied to collateral, and household debt began to rise.

Since World War II, there have been huge increases in debt and types of debt instruments available. Further, academics helped provide intellectual support for debt—the Modigliani-Miller Theorem and the capital-asset pricing model generated a financial revolution. Usury laws in states limited some expansion, but banks located credit card facilities in South Dakota to escape New York's stringent interest rate limits. Geisst's narrative moves quickly into securitization, derivatives, and financial crises involving sovereign debt of developing countries, and finally the financial crisis that began in 2007.

The penultimate chapter discusses Islamic law and debt. "Of all the prohibitions against undesirable activities in the Koran, usury is mentioned the most" (p. 275). But, as in medieval Europe, some changes began to occur after the oil price rises in the 1970s. As several oil-rich nations that subscribed to Islamic law began to have huge sums of money to invest, adjustments in treatment of interest developed. In 2002, the Al-Achar Islamic Research Institute in Egypt issued a *fatwa* (pronouncement) on the topic, making a fixed return on deposits permissible. The term used was a "predetermined" profit rate.

Beggar Thy Neighbor offers a comprehensive look at the intellectual treatment of usury, as well as how practice often differed from law—both civil and canon. It traces both the reasons for the harsh treatment of interest for much of European history and the reasons the treatment of interest ultimately changed. It is not written from a Christian perspective, but clearly the Church's role in European history makes references to the views of the Church essential to the discussion. There are some interesting events and characters that show up in the narrative, but I do not think the book will appeal to the general public or even to most economists.

References

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