



Leonine Institute
for
Catholic Social Teaching

Usury and Interest: Correcting Modern Errors

Policy Paper 2020.2

Anthony M. Fernandez - Research Associate, Leonine Institute

Levi A. Russell - Fellow, Leonine Institute

(lrussell@leoinstitute.org)

Anthony M. Gentile - Research Associate, Leonine Institute

July 22, 2020

Feast of St. Mary Magdalene

Abstract

The modern debate on the question of usury seems to have settled on a position that allows for profitable interest to be charged. Curiously, most Catholics seem to think that the current system fits within the Church's teaching on usury, with the exception of what is regarded as obviously-usurious lending in the case of credit cards with very high rates of interest. In this paper we draw on the Magisterial teaching of the Church and modern economic theory to correct the record on the permissibility of lending at interest. We argue that lending at interest is always usurious and that apparent exceptions found in the writings of the past suffer either from a deficient understanding of clear Church teaching or a confusion in interpretation of modern terminology. We find that nearly all lending today is usurious and that other means can be used to allocate capital and lend to those in need. Since they avoid usury, these other means would improve the current system by making it more just.



Introduction

Usury, in its very nature, is an evil. The objective of this paper is to define usury in the modern context and explain why the only excuse for it is greed. It is important to discuss usury because, as Christians, we must strive for a world in which our Christian values are upheld.

The Church has expressed its stance on usury, as it has on many other things, consistently throughout history. Today, in our current financial world, usury plays a major role in nearly every single loan agreement. If it is an issue, and indeed a sin as the Church has echoed for centuries, there must be a point at which Christian people must speak up and meet this issue face-to-face once again. Usury, defined in the Catechism as interest on a loan, has not just been sanctified by our modern financial scene, it has also been glorified. It has become the right of certain institutions, namely banks, to wield usury as a privileged road to a profit. There is now, more than ever, a threat to charity akin only to the threat of pornography and the frequent exchange of monies that comes with it. It is, as *Vix Pervenit* calls it, dishonest profit.

Speaking on usury is important because it is a sin against both charity and justice. It is, Usury, a sinful injustice that causes misery. The misery it causes has a dual effect; misery shackled to those receiving loans with interest from lenders is the first and most immediate misery. The second kind is a nationwide misery. This misery affects the entirety of the Nation and erodes the legitimacy of institutions within the state.



Justice, the giving to each what is owed to them, is totally and utterly abandoned. The Justice of Socrates is replaced with the fallacious justice of Thrasymachus.¹ Justice has become the advantage of the stronger and always, as if it is faithful as a clock, the banks tick on shelling out usurious loans to those in need of assistance. By charging interest on a loan the Usurer says, “your misfortune is my fortune, and your struggle is my victory.”

What is Usury?

Usury, that is, interest on a loan, is a sin against commutative and distributive justice. In *Vix Pervenit* Pope Benedict XIV’s letter to the Italian Bishops on usury, decrees “The sin [of usury] rests on the fact that sometimes the creditor desires more than he has given. Therefore he contends some gain is owed him beyond that which he loaned, but any gain which exceeds the amount he gave is illicit and usurious.”² *Vix Pervenit* further reads,³

By these remarks, however, We do not deny that at times together with the loan contract certain other titles—which are not at all intrinsic to the contract—may run parallel with it. From these other titles, entirely just and legitimate reasons arise to demand something over and above the amount due on the contract. Nor is it denied that it is very often possible for someone, by means of contracts

¹ Plato, *The Republic* Book I, 343c

² Benedict XIV. 1745 *Vix Pervenit* III.I Retrieved July 10, 2020
<https://www.papalencyclicals.net/ben14/b14vixpe.htm>

³ *Ibid.* III. III



differing entirely from loans, to spend and invest money legitimately either to provide oneself with an annual income or to engage in legitimate trade and business. From these types of contracts honest gain may be made.

Vix Pervenit leaves us with a clear authoritative teaching on what usury is and is not.

Current State of the Usury Debate

Unfortunately, in our time, there are some Catholic Christians who say that identifying the taking of interest on a loan as a sin is incorrect. Any attempt at upholding seasoned Church teaching is pushed away as nothing more than a nonsensical trope perpetuated by those who are unnecessarily backwards.

We can see a parallel to this unfortunate situation in the recent past. The reaction to Pope St. Paul VI and his Encyclical *Humanae Vitae* was split. One side of the split came from the Canadian Conference of Catholic Bishops (CCCB). The CCCB stated, in the Winnipeg Statement,⁴ that it was impractical for Catholics, however faithful, to live up to the expectations of *Humanae Vitae*. They wrote that in the modern world it is not possible for Catholics to live without contraception. This challenge on the impracticality of *Humanae Vitae* is strikingly similar to the opinions expressed by some pro-usury Catholics. It is echoing the same sentiment that it is impractical to suggest all usury (just as the CCCB mulled over the outlaw of all contraception) is

⁴ CCCB. The Winnipeg Statement, III. 8-10. Christian Conscience and Divine Law



sinful or that we can't live in a functioning world in the current year without interest-bearing loans.

The modern debate on usury has spawned from a separate issue in the socioeconomic discourse. With a rise in radical political philosophies, namely socialism, a sharp reaction by free market theorists and advocates has caused many still possessed by the false socialism vs capitalism dichotomy to double down on certain repugnant economic ideas; the first among these repugnant ideas is usury.

The worst part of the modern perspective on usury is its transmogrification from a sin into a virtue. The modern perspective does not treat the concept of usury as irrelevant. Rather, this perspective treats the taking of interest on loans to be a virtue, or at least a non-evil. The normalcy of usury has led to the acceptance of usury, and by this acceptance those who see no issue with it dissent from Church teaching.

Modern Interpretation of Aquinas & the Scholastics

To understand the problems with modern perspectives on usury, it is useful to lay out the modern interpretation of Aquinas and the Scholastics. This erroneous interpretation rests on a flawed understanding of a few key concepts related to usury. The following discussion lays out the flawed understanding of each concept in turn.



Lucrum Cessans

Lucrum cessans (profit ceasing)⁵ refers to the idea that since money which is lent cannot now be used for investment and other profitable use, the lender is justified in charging that which he could have reasonably received had he not made the loan. While this idea is present in the speculative writings of theologians,⁶ it is not found in *Vix Pervenit* or any of the other authoritative teachings on usury. While *Vix Pervenit* does allow for parallel contracts, it stipulates that these must be “not at all intrinsic to the [loan] contract.” Since *lucrum cessans* only exists because of the loan contract in question, it is intrinsic to said contract. Thus, *Vix Pervenit* clearly prohibits charging interest on a loan and justifying it by *lucrum cessans*.

Mutuuum

Others, most notably the founder of the Zippy Catholic blog,⁷ have argued that *Vix Pervenit* only applies to what is called a *mutuum*: a loan with no collateral. So while a borrower cannot charge interest on consumer loans, it can still be charged on loans that are fully collateralized and without recourse to the borrower himself. This argument fails for two important reasons. First, it is based entirely and exclusively on

⁵ McCall, Brian Michael, Unprofitable Lending: Modern Credit Regulation and the Lost Theory of Usury (February 25, 2008). *Cardozo Law Review*, Vol. 30, No. 2, 2008, Available at SSRN: <https://ssrn.com/abstract=1098954> page 570

⁶ Aquinas responds to this objection in *Summa II-II* q78 a1: "the lender cannot enter an agreement for compensation, through the fact that he makes no profit out of his money: because he must not sell that which he has not yet and may be prevented in many ways from having."

⁷ <https://zippycatholic.wordpress.com/2014/11/10/usury-faq-or-money-on-the-pill/> Zippy FAQ Q4

the word choice in *Vix Pervenit*. While *mutuum* does refer to this kind of loan, it is not used exclusively for this and also refers to loans in general. Further, *Vix Pervenit* goes on to explain⁸

some will falsely and rashly persuade themselves ... that together with loan contracts there are other legitimate titles or, excepting loan contracts, they might convince themselves that other just contracts exist, for which it is permissible to receive a moderate amount of interest. Should any one think like this, he will oppose not only the judgment of the Catholic Church on usury, but also common human sense and natural reason.

Thus, the argument that non-*mutuum* loans can bear interest is not at all convincing given that the document excludes interest not just on *mutuum* loans, but even on other contracts. While they may be able to find theologians who make this exception, it is clearly not allowed given the stipulations laid out in *Vix Pervenit*.

A distinction must be made on this subject. A *mutuum* is that which, by its nature when lended, changes ownership. A *mutuum*, money or food, ceases to be the property of the lender once it is loaned out.⁹ For example, if Peter loans John \$5, the \$5 ceases to belong to Peter and ownership is transferred to John.

⁸ Benedict XIV. 1745 *Vix Pervenit* III.V. Retrieved July 10, 2020
<https://www.papalencyclicals.net/ben14/b14vixpe.htm>

⁹ Ederer, R.J. (2005) "Economics for Dummies" Review of *The Church and the Market: A Catholic Defense of the Free Economy*. Thomas E. Woods Jr. Lexington Books, 2005. Retrieved July 19, 2020 <http://culturewarsmagazine.com/2005/Ederer.html>



A *commodatum* is equivalent to what we call a rental today. Peter borrows a tool from John to fix his car and returns the tool to John. For the use of the tool, Peter pays John. Economist Rupert J. Ederer explains this distinction as follows:¹⁰

Among other things, Father Dempsey explained clearly what seems to present a problem to the author: the difference between a *mutuum* and a *commodatum*. The former (*meum-teum*) is the loan of something which of its nature must change ownership when it is loaned, because it is used up by the borrower (money, food). Therefore it is no longer the property of the lender. The *commodatum* involves a loan of something where the same thing is returned with compensation for use (a horse, tools). In the *mutuum*, only an equivalent amount must be returned to the lender barring the eventuality where he suffers some loss arising from the loan of, e.g., money (*damnum emergens*). He cannot be expected to pay for what by consumption or spending became his own.

Charging interest on a *mutuum* loan is equivalent to demanding compensation for that which the lender does not own. That is, by the nature of its definition, unjust. It is not giving to each what is owed to them. Upholding justice in all transactions and facets of a Christian world is essential.

Another passage from Aquinas¹¹ does permit profit above that which is lent. He mentions the example of money that is not consumed, but rather displayed, or used for safekeeping. This passage is limited in scope. When money is lent to purchase a

¹⁰ Ibid.

¹¹ Aquinas De Malo Q13A4ad15



consumer good or a durable asset, the money lent is used for something else. It fits neither of the examples used by Aquinas for which something above the principle can be demanded. Further, the argument ignores the nature of the sin of usury, which consists of selling ownership and demanding a charge for the use of the thing that was sold. It makes no difference what the money is used for. In Aquinas' examples, though, the money is not used, and ownership is still clearly retained by the lender.

The point is ultimately about transfer of ownership, not about the type of good (consumption or durable assets) purchased with the funds that are lent. As Fr. Bernard Dempsey, S.J., noted when summarizing Scholastic theologian Luis de Molina:¹²

It would seem that though Molina, with the Roman law, regarded a mutuum as practically concerned with consumption goods, nevertheless this is not the point which is, in principle, determining. The critical factor is the transfer of ownership, which is bound up with the fungibility.

It is apparent that much of the confusion among authors today with regard to usury is rooted in semantic issues that are not often discussed.

Time Value of Money

Libertarians like Thomas Woods¹³ and Trent Horn¹⁴ have argued that the nature of money has changed, and this change implies that interest is legitimate today. This

¹² Dempsey, B. Interest and Usury (1948) London. Dennis Dobson LTD. p. 144

¹³ Woods, T.E. The Church and the Market. Lexington Books. 2005.

¹⁴ Horn, T. and Pakaluk, C. Can a Catholic Be a Socialist? Catholic Answers Press. 2020.

view states that money is itself productive, whereas in the past it was viewed as a barren asset. Woods states that the time value of money, the notion that money today is worth more than the same amount of money in the future, all other things equal, makes interest legitimate. However, the Church addressed this argument during the papacy of Innocent XI. It condemned the following proposition as erroneous:¹⁵

Since ready cash is more valuable than that to be paid, and since there is no one who does not consider ready cash of greater worth than future cash, a creditor can demand something beyond the principal from the borrower, and for this reason be excused from usury.

Thus the time value of money cannot be used to justify interest. Any other attempt to describe why the changed nature of money now allows interest falls either into this error or the *lucrum cessans* error. Both are illegitimate and erroneous.

Finally, some will argue that since the Council of Lateran V allowed for interest to offset the cost of lending, that usury must not be wrong in principle. Some important notes must be considered here. This defense was written not for profit, but to offset the actual expenses of lending (sourcing funds, real work in drawing up contracts, etc.).

Further, this was written to defend the Montes Pietatis, which were set up to provide an alternative to usurious lending. They charged fees, which could be paid over time, to offset expenses: it was not profitable. This concept applied today certainly would

¹⁵ Pope Innocent XI by decree of the Holy Office, Various Errors on Moral Subjects (II), March 4, 1679. <http://patristica.net/denzinger/> Retrieved July 19, 2020

not permit even small interest rates. At best this would permit a flat, low interest rate, similar to closing costs in mortgages. It certainly cannot be used to defend annual compound interest.

Modern Interpretation of *Vix Pervenit*

One of the most important documents on usury is the 1745 letter from Pope Benedict XIV to all the clergy of Italy regarding the permissibility and justice of certain contracts entitled *Vix Pervenit*.¹⁶ In 1836, the Holy Office declared¹⁷ that this Encyclical applied to the whole Church.¹⁸ While *Vix Pervenit* provides striking clarity to some issues surrounding usury, parts of it have been used to justify contracts that are, in fact, usurious.

Vix Pervenit clearly states that usury is the taking of interest on a loan, that the amount of interest is not relevant to whether or not a loan is usurious, and that those who engage in usury are required to make restitution.¹⁹ The lack of clarity in modern discourse comes from the wording in paragraph III.III which states in part²⁰

¹⁶ Benedict XIV. 1745 *Vix Pervenit* Retrieved July 15, 2020
<https://www.papalencyclicals.net/ben14/b14vixpe.htm>

¹⁷ Vermeersch, A. 1913. *Usury Catholic Encyclopedia* ¶15 Retrieved July 10, 2020
[https://en.wikisource.org/wiki/Catholic_Encyclopedia_\(1913\)/Usury](https://en.wikisource.org/wiki/Catholic_Encyclopedia_(1913)/Usury)

¹⁸ Herbermann, Charles, ed. (1913). "Usury" . *Catholic Encyclopedia*. New York: Robert Appleton Company.

¹⁹ Benedict XIV. 1745 *Vix Pervenit* Retrieved July 15, 2020
<https://www.papalencyclicals.net/ben14/b14vixpe.htm>

²⁰ *Ibid.* III.III

By these remarks, however, We do not deny that at times together with the loan contract certain other titles—which are not at all intrinsic to the contract—may run parallel with it. From these other titles, entirely just and legitimate reasons arise to demand something over and above the amount due on the contract.

Many cite this statement in an attempt to justify the taking of interest on some loans. Zippy, the proprietor of the popular Catholic blog, states throughout his exhaustive FAQ that the prohibition on usury is applied only to a specific type of loan contract known as a *mutuum*.²¹ This distinction, explained in full in the preceding section, has been used to argue that lending at interest in some cases is allowable. Fortunately, other research on this topic provides clarity.

Law professor Brian McCall provides a brief summary of the Scholastic theory of usury in a 2008 law review article. This is especially useful since the Zippy blog leans heavily on the work of St. Thomas Aquinas to justify lending at interest in some circumstances. McCall claims that there are two broad categories of instances in which it is acceptable for one person to pay back more than the amount that is given to him in a transaction.

The first category is “loans of money pursuant to which damages are due.”²² McCall explains that the lender is owed something beyond the principal value of the loan if he

²¹ Zippy Catholic. 2014. “Usury FAQ, or, money on the Pill”
<https://zippycatholic.wordpress.com/2014/11/10/usury-faq-or-money-on-the-pill/#5>

²² McCall, Brian. 2008. “Unprofitable Lending: Modern Credit Regulation and the Lost Theory of Usury” *Cardozo Law Review* 30-2, pp 570.



incurs actual damages.²³ McCall's example is late payment; if Peter lends money to John with the stipulation that John return the principal to Peter on a certain date, Peter is justified in requiring John to pay him damages.

While some might argue this situation can be referred to as interest, in modern finance, this is simply a fee or a penalty for late payment. The excess payment above the original principal is warranted because the borrower failed to hold up his end of the agreement.

The second category is made up of a range of contracts "which to a modern jurist may appear similar to a loan in effect but which according to the scholastic theory did not constitute a loan."²⁴ McCall goes on to explain four such types of contracts. Three of these contract types can in no way be considered a loan in the modern sense. Thus, the earnings that result from them are not interest, but a payment of profit due to shared risk. This shared risk is the essence of what we call today an *equity stake* in an investment, which is clearly not a loan.

The first type of contract McCall mentions is a partnership investment. Given that the partners both receive compensation in accord with the success of the business, such compensation is not interest on a loan but just reward for the profit earned through the productive use of the capital invested.

²³ These damages are called *lucrum cessans*, profit ceasing, and *damnum emergens*, damage emerging.

²⁴ McCall, Brian. 2008. "Unprofitable Lending: Modern Credit Regulation and the Lost Theory of Usury" *Cardozo Law Review* 30-2, pp 571.



The second is an annuity, which is a stream of payments over time from a financial institution to the beneficiary after an initial deposit from the beneficiary to the financial institution. The stream of payments over time exceeds the initial investment made by the beneficiary. However, McCall states that this arrangement was only just if the stream of payments was based on what the Scholastics called a “fruitful base”²⁵ That is, the initial payment from the beneficiary of the annuity to the financial institution was required to have been invested in a productive venture.

The third category is government bonds. McCall claims that the Scholastics found that excess payment of government bonds over and above the principal (McCall calls this a gratuity) is justified based on the power of the government to tax. Since taxation is morally licit, payments exceeding the principal of a government bond are justified.

Finally, McCall discusses future sales or sales on credit. After briefly outlining the Scholastic notion of the just price, McCall explains that it is morally allowable to charge more for sales on credit since the just price may fluctuate over time and thus doubt may arise as to the future price of the good when payment is made to the seller by the buyer. In cases where such doubt is unlikely, McCall states, paying more for a credit transaction would constitute usury. Further, a credit transaction in which the credit price clearly exceeded the bounds of the just price was also prohibited.

²⁵ Ibid. pp 574

McCall's work brings breathtaking clarity to the modern application of the commands in *Vix Pervenit*. Except in cases discussed above, some of which are not loans at all, the charging of interest on a loan is clearly unjust and gravely so.

Economic Concepts

Those who defend a more liberal interpretation of the Church's condemnation of usury often appeal to advances in the field of economics to justify their interpretation. In this view, economics is purported to be a science like physics or chemistry. The implication is that new developments in the field are in some sense independent of the teaching of the Church and the Church's teaching must be adapted to account for scientific advances in the field of economics.

In this section we examine five important economic concepts and points of confusion that are particularly relevant to understanding usury and its application to business loans. As we will see, it is clear that modern economics in no way changes the Church's clear condemnation of usury as the payment of interest on a loan.

Time Value of Money

One of the fundamental components of finance theory is the time value of money. This is the theoretical, intuitive basis for interest and returns on any invested capital. In the Austrian School of Economics, it forms the basis of interest theory.

Investopedia provides a succinct definition:²⁶

The time value of money (TVM) is the concept that money you have now is worth more than the identical sum in the future due to its potential earning capacity. This core principle of finance holds that provided money can earn interest, any amount of money is worth more the sooner it is received.

Though this definition implies that time value of money is a fundamental law of nature, it is nothing of the sort. It is merely the ethical assumption that the passage of time without the use of money one has title to should entail some return.

Thus, this is not an economic justification for interest. It is merely an ethical view that one may reject, and indeed Catholics should reject it. Money is not fertile like wheat seeds are. It is merely a medium of exchange; it is inert. It's possible to create a system in which it seems to be fertile, but this is an illusion. Business activity can be fruitful, but the money invested in it is merely a representation of the scarce resources employed.

Inflation

Inflation is another claim used to justify charging interest. Since the value of money declines over time, the lender can charge for the value that is lost to inflation in order to keep himself from loss. While it is true that inflation is a real phenomenon in

²⁶ Chen, J. *Time Value of Money* Retrieved July 16, 2020
<https://www.investopedia.com/terms/t/timevalueofmoney.asp>



modern economies, the moral claim that the lender is justified in charging interest is not proven simply by the existence of inflation.

While inflation does cause real damage to the borrower, this is not sufficient grounds for charging interest. The decreased value of money is not the fault of the borrower, but rather the fault of the one in charge of the money supply. This is an evil exogenous to the contract, and thus cannot be used to justify an additional charge to the borrower. The damage would have been realized with or without the loan. Any real damage should be rectified by the one who caused the decrease in the value of money. Or, as the Scholastics argued, the existence of an evil cannot be used as a source of gain.

Opportunity Cost

A common justification for charging interest on loans is opportunity cost. In modern economics, opportunity cost is a subjective concept. It is the highest valued, next best alternative to the choice made. An example is useful to illustrate this concept.

Suppose Peter is faced with three choices to occupy the next hour of his time: 1) reading a book, 2) watching TV, or 3) taking a walk. If Peter ranks the choices from best to worst as follows: 1) taking a walk, 2) reading a book, 3) watching TV, and he chooses to take a walk, the opportunity cost of taking a walk is reading a book. Thus, the cost of spending the next hour of his time going on a walk is reading a book.



This concept undergirds neoclassical economic theory, but like time value of money, is not a law of nature that obligates borrowers to compensate lenders. That interest is owed on loans is an ethical judgment, a judgment clearly condemned by the Church. In his article on usury law, McCall states that *lucrum cessans* and *damnum emergens* referred to actual damages incurred by the lender at the fault of the borrower.²⁷

These two concepts, *lucrum cessans* and *damnum emergens* are sometimes construed by contemporary writers as equivalent to opportunity cost. This is false. As McCall states, these concepts refer to real damages that are caused in some way by the borrower. Further, Zippy, author of the popular Usury FAQ, has argued²⁸ that opportunity costs are not ontologically real and thus cannot be related to *lucrum cessans* and *damnum emergens*. Opportunity cost might be a useful fiction for economic analysis, but this does not make it morally relevant to the question of usury.

Interest vs Rent

It is necessary to clarify the distinction between interest and rent or the payment for the use of a factor of production. In economic theory, rent has several definitions, but here we take it to mean the payment for the present use of a durable consumer good (such as a home) or a durable asset used in the production of other goods (such as a drill press or other machine). According to modern economic theory, rent is justified

²⁷ McCall, Brian. 2008. "Unprofitable Lending: Modern Credit Regulation and the Lost Theory of Usury" *Cardozo Law Review* 30-2, pp 570.

²⁸ Zippy Catholic. 2014. "If we don't raise taxes that's a 'tax cut'" Retrieved July 15, 2020. <https://zippycatholic.wordpress.com/2014/05/03/if-we-dont-raise-taxes-thats-a-tax-cut/>

by the value of the services provided by the durable asset for the period of time it is used. This use also results in the asset wearing out over time, which means that it requires maintenance and repairs. The cost of maintenance and repairs is part of the rent.

Sometimes the concept of rent is confused with interest. In fact, according to basic financial theory, the two concepts are distinct. Interest represents the time value of money or the opportunity cost of funds. One way to illustrate the distinction between the two is with an example where both are used. For instance, a basic model to compute the asset value of land would take into account the rental value of the land on an annual basis and the going rate of interest used to finance the purchase of the land.

The distinction outlined above ensures that there is no confusion when it comes to evaluating the justice of lending at interest. The argument that confuses the two concepts is as follows: renting property is similar to a loan in that a property is borrowed and must be returned at the end of the agreement, and the Church has stated that this kind of passive income is just.

In response to this argument, a distinction must immediately be made: this example is not a loan, it is a rental agreement. A few notes will distinguish the two transactions. In a loan, the borrower has full right to the thing that is lent, while the lender only has a claim to it at a later time. In a rental agreement, ownership is not transferred, rather it is kept by the landlord. This entails risk of real damage and real depreciation. Neither of these occur in a loan.



If borrowed money is spent frivolously, the lender is not damaged unless the borrower is unable to repay. Of course, failure to repay a loan is also unjust, but it is not an intrinsic feature of the loan itself. In a rental agreement, if damage is done to the property through normal use, the tenant is not liable, while the landlord must absorb the cost. Malicious treatment of the property is certainly not justified by this argument. Thus, the claim that lending is just another kind of rental agreement is not substantiated, as it is based on a misunderstanding of the risk burden and ownership. Profit from renting property is licit (within the bounds of just price), while no profit from lending is ever justified.

Interest vs Return on Equity

An important distinction in finance is the difference between debt and equity. Both are sources of funds for a business to invest in productive assets the business uses to generate profit. Among the many differences between these two sources of funds is the bearing of the risk of the business itself.

Under the current legal structure of our financial system, a lender has a legal right to be paid over and above the amount of money lent to the business. This legal right is typically specified over a period of time and guarantees the lender a specified return unless the business fails. If the business fails, the lender is first in line to receive the funds they lent, plus the interest agreed upon, from the liquidation of the firm's assets.

It is not so for the equity holder. An equity holder is an owner of the business and, in the current system, is compensated for his investment in the company by an increase in the value of the stock of the business in the case of a corporation and/or by regular payments made out of the profits of the business. The equity holder has a legal right to the profits of the business, but these profits are net of the interest paid to the lender.

Thus, the lender's payment is an expense of the business paid prior to computing the profit of the business, which is the property of the equity holders. In the event of bankruptcy, the equity holder is not guaranteed any payment whatsoever when the firm's assets are liquidated. The equity holders are last in line behind lenders to receive these funds.

Equity, then, is the only source of funds that is subject to the risk of the business. While lenders face a risk of nonpayment, this is distinct from sharing in the risk of the business itself. Interest paid to the lender is considered, in the present system, a normal expense. The equity holder (owner) does not receive this level of guarantee.

Fr. Heinrich Pesch, S.J. makes this point succinctly in his discussion of usury. Discussing Canon Law, Fr. Pesch tells us²⁹

It was taken for granted that Christians were supposed to grant loans for consumer purposes to their neighbors in need whenever they were able to do so, out of simple charity, *nil de sperantes*.³⁰ Also, there was no difficulty in

²⁹ Pesch, Heinrich. 2004 (1918). *Ethics and the National Economy*. IHS Press. pp. 84

³⁰ [Footnote in original] "Hoping for nothing thereby." Cf. St. Luke vi:35

recognizing that one was entitled to earn a profit from a capital investment to the extent that the investor was himself involved as a partner, in any case as sharing in the risk.

Fr. Pesch's summary is quite clear and is consistent with the work of McCall.³¹ As long as the investor shares in the risk of the business, he is allowed to earn a return on his investment in the business. This is distinct from interest, which is clearly condemned as usury.

Implications for Today

Having laid out the errors made in modern discourse on usury and explained the relationship of modern economic concepts to the moral teachings of the Church, we can make some policy suggestions that will move us toward a just system. We do not argue that any of the policy suggestions below will be neutral in terms of their impact on gross domestic product or on the material wealth of citizens. However, we believe it is likely that the implementation of these policies will result in more economically just outcomes for the poor and the middle class.

An economically just society is superior to an economically unjust society, regardless of gross domestic product or the material wealth of citizens. A full empirical analysis of similar policies is beyond the scope of this paper; our purpose now is to further the discussion on the most preferred policies. However, continuing on this road to

³¹ McCall, Brian. 2008. "Unprofitable Lending: Modern Credit Regulation and the Lost Theory of Usury" *Cardozo Law Review* 30-2

serfdom is treacherous and bound onto the causeway of injustice and it will continue to bring about the evil it has consistently procured.

Modern Loans Are Usurious

It is clear from the discussion in this paper that business loans made today are nearly always usurious. Whenever profitable interest is paid by the borrower to the lender and the lender does not share in the risk of the business, that interest is usurious. In the modern system, business loans do not expose the lender to the risk of the business. The types of contracts that paid “interest” in the parlance of the middle ages are now referred to as partnerships. They are equity arrangements, not debt arrangements.

Thus, a ban on business loans would make the business world more just, but it would certainly cause some problems that would need to be solved. Since debt is a means of allocating financial capital to investment projects, this role would have to be taken over by other means of allocating capital.

As stated above, *montes* (government lending) does not fall under the definition of usury. This is because the sovereign can justly tax the public to finance the implementation of its policies. Government loans can be used to allocate capital. Though it would not be sensible or just for the government to allocate all capital, it is justified in determining some investments.



Equity investment would likely replace most of the usurious debt financing under a ban on usury. As argued above, equity investment is fundamentally different from lending in that the equity investor takes on the risk of the underlying business. Investment banking would still occur under a ban on usury, as would retail investors. Debt is often a cheaper means of financing for businesses, but being less expensive does not justify its use.

Consumer loans are all usurious. Credit cards, personal loans, car loans, student loans, and mortgages all fall within the bounds of usurious lending laid out by *Vix Pervenit*. All are loans of money in which profitable interest is charged. Some of these are more profitable than others, but since all are undeniably loans of money, whatever that money is used for does not change the nature of the underlying transaction. Further, *Vix Pervenit* clearly condemns all usurious loans no matter the size of the profit made.³² When money is lent, all that can be demanded is the amount the lender gave and no more.

We Need a Modern Montes Pietatis

Montes Pietatis, Latin for “mount of piety”, were credit institutions that sought to carry out just lending. Lending money with little or no interest, these institutions aimed to shelter the needy borrower from usurers. Essentially, a person in need of a loan would leave a valuable item in pawn as a security for the loan and in return would

³² Benedict XIV. 1745 *Vix Pervenit* III.I Retrieved July 18, 2020
<https://www.papalencyclicals.net/ben14/b14vixpe.htm>

borrow money. The borrower would cover the actual costs of lending the money, but no profitable interest was allowed.

A modern, widespread *Montes Pietatis* would be a just and valuable alternative to the current arrangement of consumer lending. Though in the past they operated as charitable institutions lending to those in woeful circumstances, today the scope of their apostolate may be expanded in order to more actively present an alternative to usurious banks and lenders.

To reify these ideas, actions must be taken so as to reorient our financial world to a truly Just disposition. A modern *Montes Pietatis* is one way to do this. Reifying orthodox Catholic ideas in our society would allow the Justice of Socrates to flourish and the justice of Thrasymachus to be repudiated.