

MMT - the differences

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I am not sure what others have made of the discussions on modern monetary theory (MMT) that have dominated this blog during the last week or so, but I have found them useful because it has considerably helped the development of my own thinking around MMT

I had already summarised some of that thinking in my publication of an explanation of what I think MMT says. There are, however, those who follow MMT who dispute that my interpretation is correct. That I acknowledge. I would say in response that an idea that cannot change and develop is not one worth having. What I am suggesting that MMT does need to change and develop.

To summarise the differences between what might be called Founder's MMT, as explained by Warren Mosler, and what I would call Reformed MMT (or RMMT, as a commentator described it), these are, again in my opinion, as follows, with headings to help identify the issues.

This summary will be added to my explanation of MMT in due course.

To make this post easier to read for some for whom the following table will be hard to follow on a web browser a [PDF version is available here](#).

Founder's MMT Reformed MMT

What MMT does

MMT describes the role of money in the macroeconomy. It does so without recognising that there was any significant change in that role between the era of asset-backed currencies and the fiat currency era. MMT describes the role of money in a macroeconomy where a fiat currency is in use, subject to the condition that:

- a) The government of the jurisdiction in question has a central bank.
- b) That central bank issues the fiat currency that is in use as the only legal tender within that jurisdiction.
- c) The jurisdiction in question can borrow in its own currency and need not do so in any other currency.

MMT does not, and is not intended to, provide a history of money or an explanation of its role in any circumstance other than those noted above.

MMT is modern in the sense that the above conditions reflect relatively recent economic history

Purpose of MMT

To provide a theoretical explanation of the role of money in the economy over time as a largely academic pursuit. To provide an explanation of how money actually works in the economy now, largely as a guide to policy making.

Summary of MMT

Founder's MMT says a government can fund its spending using the currency of its choice using money created for it by its central bank without needing the prior settlement of taxes or the taking of loans. Reformed MMT says that a government can fund its spending using the currency of its choice using money created for it by its central bank without having to necessarily impose taxes take loans in advance of doing so

Ordering of spend and tax and the creation of a valuable currency

Taxes are imposed but not paid before the government can spend because that imposition provides money with its value in exchange. Without having imposed a tax first a government could not spend in its own currency because that currency would not be accepted within the economy. Taxes need not be imposed or paid before the government can spend. A government can always spend without raising a tax first by creating the money required to do.

A tax need not be imposed before a government spends in the currency it declares to be legal tender because it is that declaration and the requirement that all enforceable

debts be denominated in it that provides money with its value.

Founder's MMT says that a government will, to secure the use of its currency:
Reformed MMT says that a government will, to secure the use of its currency in an economy:

a. Impose a tax on its population that must be paid using the currency that it creates. This will be a poll tax of some form, payable irrespective of the availability of income to make settlement. a) Declare the money that it creates the sole legal tender of the jurisdiction in question.

b. The government imposing the tax will offer employment to its population, forcing them out of their existing employment and into the employment of the government. b) Refuse to uphold contracts in other currencies for domestic purposes, including (but far from exclusively) for the settlement of taxes.

c. The government will make settlement of the liability due to those it has forced into its employment that they will then in turn use for transactions within the economy for which that government is responsible, meaning that the currency in question is widely available for settlement of the tax previously imposed. c) Require that bankers use the currency in question for their domestic transactions, including their inter-bank settlements.

d. Payment of the tax due can then take place. d) Actually use this currency in the course of its own market interventions, and refuse any other, meaning it will only accept payment of tax in this currency.

Following this logic, money secures its value by being imposed, violently if necessarily, on society. Money secures its value from the enforced payment of tax. Following this logic, tax is imposed voluntarily on a society that has secured the benefit of government spending and is settled in the legal tender of the jurisdiction, which is used for all commercial transactions, from which it secures its value.

To achieve this outcome, Founder's MMT says that taxes are imposed before government spending can take place within an economy. As a result, Reformed MMT says that a government wishing to spend without having either imposed taxes or taken loans in advance of doing so is able to do so because it can secure loans in the currency it has created from its central bank because that currency is the only legally

enforceable currency in which contracts might be concluded in the jurisdiction in question, meaning that those wishing to transact must use it if they are desirous of being paid.

It is not tax in that case, but commercial contract law, that puts a currency into circulation and which provides money with its value, having said which if the value of tax payments owing to a government is a significant part of national income those in the jurisdiction have little choice but to transact in that currency to avoid exchange rate risks and costs when making tax payment.

In the view of Reformed MMT, tax is imposed by a legal government to uphold the rule of law, which rule of law is used with public consent as the basis for the reprimand of those refusing to comply with the communal requirement that they do so. There is a social contract in which tax plays a key role.

Purpose of tax

a) The primary purpose of tax is to create unemployment so that people are forced to work for the government and so accept its currency which they need to settle the taxes it has imposed before providing any other means to make settlement. a. Tax is primarily used to reclaim the money created by government spending from the economy to control inflation.

b) By forcing people into employment with the government so that they can earn the money require to pay their tax liabilities it is suggested that tax provides the government created currency with its value. b. By requiring payment of tax in the currency the government creates and, assuming such liabilities are sufficient in proportion to total income, the economy pragmatically adopts the government created currency for general use to avoid currency exchange risks that would otherwise arise when making tax payments.

c) The payment of tax destroys the money created by government spending, but never funds that spending. c. Tax is used to redistribute income and wealth, reprice market failure, to act as an instrument for the delivery of economic, fiscal and social policy and to promote democracy by representing the consideration in the social contract.

d. The payment of tax destroys the money created by government spending, but never funds that spending.

The role of the central bank

a) To create the currency used by the government by lending it into existence for that government to spend. a. To create the currency used by the government by lending it into existence for that government to spend.

b) To administer the central bank reserve accounts through which the money created by the central bank for the government is injected into the economy via the commercial banks that have such accounts. b. To administer the central bank reserve accounts through which the money created by the central bank for the government is injected into the economy via the commercial banks that have such accounts.

c) To receive payment of tax from commercial banks via the central bank reserve accounts, using such funds to cancel the sums owed by the government to the central bank when money was created to facilitate its spending. c. To receive payment of tax from commercial banks via the central bank reserve accounts, using such funds to cancel the sums owed by the government to the central bank when money was created to facilitate its spending.

The money in which tax is paid

Tax is paid using government-created money. Tax is paid using commercial bank-created money because government-created money does not circulate within the tax-paying economy that only has access to commercial banking facilities.

The commercial banks have the task of translating that commercial bank-created money used by their customers to pay tax into sums due for settlement via their central bank reserve accounts, which accounts have been pre-loaded with government-created money as a result of government spending preceding the payment of tax.

The cause of unemployment

Unemployment is created by the government spending insufficiently to put to use the resources (people) it has made unemployed as a result of having imposed taxes on the economy.

Governments do not deliberately create unemployment, although they can tolerate a level of unemployment created as a consequence of the inefficiencies found within any

economy because of failures to communicate and consequent timing differences in required actions arising between the state and private sectors, both of which sectors can as a consequence contribute to the creation of that unemployment as a result of the inevitably imperfect actions of each of them.

The remedies for unemployment

The Job Guarantee prevents unemployment.

The guarantee of work to anyone who wants it is financed centrally and administered locally.

The work is paid at a basic rate which is, however, intended to set a floor on the acceptable pay rate within markets below which employers cannot drop and still secure the services of employees.

Since government action in taxing before spending necessarily created unemployment increasing spending by making payment to cover the cost of the Job Guarantee necessarily restores the full employment which it was assumed existed before any tax was imposed.

A government that can spend without necessarily having to tax can pursue a policy of full employment in the economy for which it is responsible.

If there are unemployed resources and people in that economy then full employment can be delivered without risk of inflation arising meaning that no additional taxation to match the spending made is required.

If there are labour but not physical resources underemployed in the economy for which a government is responsible a government has to decide if the cost in terms of a declining exchange rate can be justified to deliver full employment.

Central management and forecasting of the economy is essential to reduce the timing issues within economic cycles that can result in periodic unemployment because of failed market signals on supply and demand.

A job guarantee might address the consequences of failed market signals.

The cause of inflation

A currency itself is a public monopoly and monopolists are necessarily “price setters.”

As a consequence, the price level is necessarily a function of prices paid by the government's agents when it spends, or collateral demanded when it lends.

The government is, therefore, solely responsible for the rate of inflation within the economy.

Inflation has multiple causes within a market-based economy without any necessary involvement of government, whether that is due to price speculation, excessive profit taking, the exploitation of monopoly power, deliberate disruption of supply chains, or imbalances of power within the marketplace, e.g. between monopsonist employers and employees denied union representation.

The government as a major employer and purchaser of resources can exaggerate these inflationary tendencies.

The government can also fuel inflation by taxing insufficiently.

Because the government is not a monopoly creator of credit, the majority of which is the result of commercial banking and trade transactions, it cannot be suggested that the government has sole control of a currency. As such it cannot be solely responsible for inflation.

A government can tackle inflation. Taxation is the only effective tool available to it to do so.

The role of government 'borrowing' and government 'debt'

Governments need not borrow. They are the sole creator of currency and as such cannot ever need to borrow it back from the economy into which they have injected it by taxing less than they have spent. The government is not the sole creator of money since it can be created by commercial sector banks. This will always mean that the total money supply of a jurisdiction will be in excess of the net difference between cumulative government spending and taxation levied.

The government need never borrow since it can always create the funding it requires to fulfil its mandate. However, as a consequence of the historical legacy structure of the world's major financial markets governments need to:

- a) Issue bonds that can be used as security for lending within financial markets.
- b) Provide a long-term savings facility to pension funds and others who need it and wish for the implicit guarantee that saving with the government provides.

c) Provide a savings facility to the public who also wish to avail themselves of a facility that has no risk regarding repayment.

The provision of such a facility is a banking arrangement. It is not borrowing, although those who have deposited funds are creditors of the government.

There is no need for a government to balance sums held on these deposit accounts with the cumulative difference between sums it has expended and tax charged (the inappropriately called 'national debt'). The sum ion deposit may be less, equal to or more than that supposed debt. The difference will be reflected in balances with the central bank.

The government can use this desire on the part of savers to deposit sums with the government to advantage. In the absence of markets providing any useful social purpose for savings by turning them into a source of capital for investment the government might do that instead. As such these savings could be used to deliver full employment within an economy though their use as financial capital that could stimulate full employment in times when that does not happen.