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# Community-based LETSystems in Australia: Localised Barter in a Sophisticated Western Economy

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## Introduction

Modern domestic barter systems are operating throughout the world at both the community level and at the business-to-business level in countries which are at different stages of economic development and which have different social and cultural backgrounds (Birch, Liesch and Yau 1994). Beyond the domestic economy, at the international level, international countertrade is widely practised and thoroughly institutionalised as an international business operations mode. It is used voluntarily by firms and it is mandated by governments (Liesch 1991, 1993, Liesch and Palia forthcoming). Barter and other forms of reciprocal exchange appear to provide an alternative macro-marketing exchange system, particularly in times of low economic growth. The protracted economic recession in Australia, through the late-1980s and early-1990s, might have facilitated the institutionalisation of two distinct domestic barter systems. In 1993, in Australia, an estimated AUD60 million of business-to-business barter-style exchange was effected between at least 3,500 firms via a network of 30 highly sophisticated, computerised trade exchanges. This has grown to be in excess of AUD350 million traded among some 12,000 firms in 1996 (Birch and Liesch 1998). In addition, in 1998, over 250 community-based systems, *LETSystems*, facilitated the exchange of goods and services in Australia among individuals without the need for federal money (Birch and Liesch 1997).

Dalton (1982, p. 181) warned that "...in English, we use the treacherous term barter to mean two very different kinds of transactions: moneyless market exchange (market exchange in kind), and moneyless exchange of any sort (gift-giving, prestations, ceremonial exchanges such as potlatch, Kula and moka)". For the purposes of the following discussion on community-based *LETSystems*, the meaning of barter will be restricted to moneyless market exchanges. Barter implies an absence of money in the exercise of an exchange transaction between parties who might not have been willing nor able to transact had the exchange been monetised. Domestic barter, as practised within local and regional communities, in its most basic form, is simply the simultaneous transfer of goods and services agreed upon implicitly as being of equal worth and concluded under the one 'contract' (Birch and Liesch 1997). However, it need not be practised in this basic form, as centralised trading facilities have enabled unilateral (rather than direct reciprocal)

trades.

## Monetised Exchange and the Existence of Barter within Domestic Economies

The mere fact that non-monetised (barter-like) exchange systems have become entrenched in the Australian and other high income economies, where the liberal market-based price mechanism is primary, implies that market imperfections exist. It is suggested here that these imperfections represent primary conditions for domestic barter to exist simultaneously with federal currency monetised exchange. The focus here is with domestic community-based *LETSsystems*, although some brief mention is made of domestic business-to-business barter systems. The former domestic systems are characterised by exchange of consumption goods or services whereas the latter are characterised by exchange of intermediate inputs (Birch and Liesch 1997, Birch and Liesch 1998). Both domestic systems, however, provide a substitute system of credit that complements the formal financial markets.

**Community-based LETSystems** In Australia, the development of *LETSsystems* has been motivated by "... a desire to strengthen the local community, increase networking opportunities, utilise unemployed skills and overcome the limited resources and credentials of members" (Birch, Liesch and Yau 1994, p. 205). It is generally argued in the economics literature that the main advantage of monetised exchange over non-monetised exchange is that the former reduces transactions costs. These costs include costs associated with searching for exchange partners, the costs of bargaining over the appropriate rate of exchange of one good or service for another, the costs of enforcing contracts (for example, costs of redress when quality falls below that contracted either explicitly or implicitly in the exchange transaction) and information costs associated with determining the trustworthiness of trading partners (North 1990). However, there is a tendency to assume that barter is always and everywhere inferior to monetised exchange on transactions costs grounds. This can be mistaken because barter transactions are "... by no means difficult to achieve in a small community where everybody knows a great deal about everybody else's products and requirements" (Einzig 1949, p. 352). Transactions costs associated with exchange are low in close-knit social groups. Where *LETSsystems* reflect a desire to build community ties and increase networking opportunities, transactions costs may even be negligible. Thus, a primary motivation for monetised exchange may be absent in *LETSsystems*.

Better utilising unemployed and under-employed skills through *LETSsystems* hints at failures in the market for labour. Orthodox economics predicts that if unemployment emerges in an economy, then the wage rate will fall to such a level that all who wish to work can obtain a job at the 'going rate'. The fact that there are over 40 million people unemployed in the member countries of the Organisation for Economic Cooperation and Development (OECD) today, with many individual countries recording unemployment rates of around ten percent of their labour force, indicates that there is labour market failure on a massive scale. A number of perspectives on unemployment can explain this fact.

First, unemployment can be interpreted as the outcome of chronic deficient demand that induces businesses to lay off workers regardless of what is happening to wages. This interpretation is associated with the so-called Keynesian approach to the analysis of mass unemployment. If businesses perceive slack demand for their products, they may lay off workers rather than try to negotiate lower wages since there are costs associated with the process of negotiation. Furthermore, in most industrialised countries, wages are only a relatively small contributor to total costs of production, so very large reductions in wages would be necessary to maintain profitability of firms. Keynes (1936) also demonstrated that even if wages were to fall, a return to full employment could not be guaranteed because falling wages would be accompanied by further decline in demand for output, unless there was an export boom large enough to more than compensate for reduced domestic demand. Once people have been unemployed for some time they tend to lose their skills as workers and cannot easily be re-hired without training. This diminution of human capital has been implicated in the persistence or hysteresis of high rates of unemployment in OECD countries (McCallum 1986). In times of recession, businesses are understandably reluctant to fund training schemes for unemployed workers.

Second, the existence of trade unions might create 'insiders' and 'outsiders' in the labour market. Insiders are those who have jobs and outsiders are those who do not have jobs, but are seeking them. Continuously increasing unemployment rates might have very little moderating effect upon wages if the insiders do not take outsiders into account in wage negotiations. A variation on this is the existence of internal labour markets characterised by relative permanency of the relationship between employer and employee, promotion from within and few points of entry (Doeringer and Piore 1985). New entrants into the labour force might find it very difficult to shift from the external to the internal labour market. The existence of internal labour markets is well accepted by labour economists today and helps explain why unemployment often impacts very heavily upon the young who have never had employment experience. Whatever the causes of persistent unemployment, it is not surprising that unemployed people get together to trade their skills among one another. If they are locked out of the labour market, then the *Letsystem* becomes a substitute labour exchange that enables them to trade their own labour for consumption goods and services (Liesch, St.

Hill and Birch 1998).

Utilising *LETS* to overcome limited resources and credentials of members also implies failures in the capital market. Unemployed people may have very limited access to credit. They may have little to offer by way of collateral and the lack of regular paid employment may disqualify them for loans from banks and other formal, financial institutions. For people whose spell of unemployment is not expected to be permanent, this is a clear case of market failure because if capital markets were perfect, unemployed people would be able to borrow against expected future income. There might also be discrimination in capital markets based upon race, sex or some other group characteristic. In these instances, *LETS* provide what might be described as a parallel credit system for those locked out of the formal, financial markets. In *LETS*, individuals can run up debts (within limits) which are extinguished later by transactions in kind.

**Business-to-Business Barter Systems** The rationale for the rapid growth of business-to-business barter systems, the other prevalent form of domestic barter, might be different from that of the *LETS* and is deserving of mention here. The two systems are sometimes confused. Business-to-business barter systems can be construed as institutions specialising in reducing transactions costs and in providing a substitute credit market when interest rates are high. Business-to-business barter systems emphasise the importance of reputation, an ancient device used for minimising such costs, although they still rely upon legal remedies as last resort. If a member of a business barter system dishonours obligations, there is a price to pay in terms of reputation (usually signalled by expulsion from the system).

The threat to reputation may be a very powerful incentive to individual members to maintain integrity in their transactions. This means that business-to-business barter systems are cost-effective tools of debt management. All transactions are electronically recorded and the system manager acts as a clearing house for the netting out of transactions. An individual member firm only has to be concerned with its net credit or debit position in respect of the system as a whole. It can ignore the positions of all the specific buyer - seller dyads of which it is a member (Birch and Liesch 1997). (In passing, it is noteworthy that general practitioners and other professionals who are members of *LETS* probably find them a very effective mechanism for minimising bad debts).

Business-to-business barter systems may also be a lower cost alternative for businesses requiring working capital. Arranging overdraft facilities through the banking system is costly because of interest and other fees charged. Acquiring inputs via barter can alleviate the need to maintain or extend overdraft arrangements. The transaction charge incurred through a business barter system is low, especially compared to today's market rates of interest. Furthermore, business barter might be the only mechanism that offers credit to some businesses in times of high interest rates owing to the phenomenon of 'equilibrium' credit rationing. Even if financial markets are working efficiently, at high interest rates, many businesses might be locked out because banks cannot distinguish between good and bad risks (Liesch, St. Hill and Birch 1998).

When interest rates rise, some borrowers will substitute low return - low risk activities with high return - high risk activities, but the problem for banks is that they do not have enough information to distinguish between the two types of business. Consequently, some firms which do not make the substitution will be denied access to loans (Stiglitz and Weiss 1981, 1992). Firms may then seek to offer goods through the barter system as a substitute for short term loans. Therefore, business-to-business barter systems can be seen as a non-monetised, market-based antidote to a failure of the formal financial system in times of high interest rates. Those businesses that would make the high return - high risk substitutions if they could get credit in the formal financial market would possibly be deterred from moving into the business-to-business barter system by virtue of its reliance on reputation as a sanction against risky or dishonourable behaviour (Liesch, St. Hill and Birch 1998).

## Background to *LETS* in Australia

In 1998, approximately 250 community-based barter systems, known as *LETS*, an acronym for Local Energy Trading (Local Energy Transfer, Local Employment Trading, Local Exchange Transfer, Local Exchange and Trading) System, have been established in Australia (Project *LETS* List, <http://www.pipcom.com/~sparky/letslist.htm>). *LETS* operate at the community level and are democratically organised, non-profit enterprises (Birch, Liesch and Yau 1994). The two main aims of these systems is: (1) to utilise more fully the skills and resources within the local community; and (2) to provide a mechanism by which the community can remain viable and self-sufficient. *LETS* are based on the premise that

... a community's wealth lies in its goods and services, the skills of its people, rather than the

amount of money available to it, and thus is not linked to traditional 'employment' which is heavily dependent on money (Jordan 1990, p. 1).

The first Australian *LETS* system was established in 1987 in Maleny, Queensland. Maleny is a small country town that appears to attract many people who are seeking an alternative lifestyle. In 1998, this system had over 900 members with an estimated growth rate of ten members per month. However, it is estimated that only 300 of these members are actively trading within the system (Doyle 1998). Members in the Maleny *LETS* system exchange a diverse range of goods and services using *LETS* units, called 'bunyas'. Each 'bunya' represents a cash federal dollar for the purposes of accounting for taxation and other state, institutional requirements, and all transactions are recorded for taxation and accounting purposes at a centralised *LETS* office. Every *LETS* system in Australia has a unique *LETS* unit of exchange, for example, 'keatings', 'bunyas', 'frasers' and 'ecos'. These units can only be traded within the community's own *LETS* system. One of the largest systems operating in Australia is the Blue Mountains *LETS* system in New South Wales. In 1998, this system had about 1300 members, half of whom were actively trading in the system. About 500 transactions valued at approximately 30,000 'ecos' were conducted each month in 1998 (Project *LETS* List, <http://www.pipcom/~sparky/letslist/htm>).

Unlike pure barter, there is no requirement for a direct reciprocal exchange of goods or services to be taken through a *LETS* system. Rather, members can acquire goods or services from a pool of members at one point in time and provide goods and services to other members of the system at a later time. The goods and services that can be provided by the members of the system are listed in a trading directory, and in Australia, these goods and services range from professional services such as veterinary care to the sale of home-made handicrafts. Transactions between members are recorded at the community's *LETS* office, and monthly statements are issued to members. The *LETS* office is staffed by *LETS* members, who are paid in *LETS* units rather than in cash dollars. New members pay a nominal joining fee and are charged a nominal annual fee to cover *LETS* office administrative functions.

Unlike the cash-based system, prices within the *LETS* system are not pre-set and the price for each transaction is negotiable. Indeed, using the cash dollar price as a basis of valuation is discouraged (Liesch, St.Hill and Birch 1998). Contrary to the traditional monetised system, debt within the *LETS* system is encouraged and is considered to represent "...a commitment to put 'energy' back into the system at some time in the future" (Birch and Liesch 1997, p. 242). Further, interest is neither paid nor charged, and thus there is no value to be gained from hoarding *LETS* units as value can only be gained by trading. Moreover, because *LETS* units only have value within their own local system, the 'wealth' remains within the community.

Due to the relatively autonomous nature of Australian *LETS* systems, it is difficult to ascertain the exact number of systems or members from throughout the nation. However, a study conducted by Williams (1996) in 1994 revealed that there were approximately 24,700 *LETS* members in Australia, accounting for approximately AUD9.4 million annual turnover. Further, *LETS* systems in Australia had an average membership of 145, with an average annual trading volume of about AUD330 per member. However, over 70 percent of these systems reported less than fifty members (Williams 1996).

## **Espoused Motivations and Benefits from *LETS* Membership**

**Motivations** A survey of 57 *LETS* coordinators conducted in Australia in April 1995 revealed that there were three key reasons for the establishment of *LETS* in Australia (Williams 1996). First, *LETS* builds, strengthens, empowers and energises the local community. The *LETS* system fosters the development of closer relationships and stronger social networks within a community and thus develops a greater sense of community (Williams 1996). Second, the system reduces the reliance of the local community on goods and services sourced externally to that community, and thus the community becomes more self-sufficient with its 'wealth' remaining within that community. Third, *LETS* helps those in the community who are excluded from traditional employment to be involved in productive activity and to more fully utilise their skills. *LETS* systems encourage local initiative which in turn, helps the members of the local community, in particular the unemployed or under-employed to improve their self-esteem and quality of life (Greco 1994).

An empirical study of 371 *LETS* members in *LETS* systems from across Australia was conducted in late-1994 (Birch and Liesch 1997). One of the objectives of this research was to investigate the motivations for the establishment of *LETS* systems in Australia (Table 1). The principal motivations reported in the study included the ability of *LETS* to build a stronger community and encourage local initiative. Respondents reported that as a member of a *LETS* system, they have the opportunity to meet new friends and customers, and to get together with other people. Further, the *LETS* system was perceived to engender trusting, warm and more personal transacting and to encourage members to help

one another. Moreover, respondents agreed that *LETS* provide them with a sense of belonging and that they can become a member of what is perceived to be an extended family.

**Table 1: Motivations for Membership in *LETS*systems**

Motivations	Mean (SD)
<i>LETS</i> help to build a stronger community	4.33* (0.77)
<i>LETS</i> encourage local initiative	4.30*(0.71)
I can meet new friends/customers in the <i>LETS</i>	4.28*(0.67)
As a member of the <i>LETS</i> , I am able to help others	4.23*(0.72)
As a member of the <i>LETS</i> , I can get together with other people	4.05*(0.80)
<i>LETS</i> allow trusting warm, and more personal transactions	3.96*(0.90)
I can gain a sense of belonging by being a member of a <i>LETS</i>	3.66*(0.99)
I can become a member of an extended family	3.59*(1.00)

(Scale: 5 point Likert Scale: Strongly Agree (5) to Strongly Disagree (1))

(\* significant at  $p<0.05$ , one tailed test,  $H_0 \mu : 3.00$ ) ( $n=371$ ).

Hence, in Australia, the development of *LETS*systems appears to have been motivated by a desire to strengthen and empower the local community by building more cohesive associations among members. Other motivations include increased networking opportunities, utilising unemployed skills and overcoming the limited resources and credentials of members (Birch, Liesch and Yau 1994).

**Benefits** A wide range of economic, psychological and social benefits appear to be derived from membership in *LETS*systems. With respect to economic benefits, Williams (1996) found that *LETS*systems allow the unemployed to participate in productive activity within their community and to use and develop their skills. For these members at least, *LETS* fosters greater self-esteem and provides a better quality of life. Indeed, in the survey of 371 members of Australian *LETS*systems conducted by Birch and Liesch (1997), it was found that *LETS* membership appears to be most attractive to lower income groups.

Thirty-one percent of the respondents reported an annual household income of less than AUD10,000, with only 22 percent of the respondents reporting a household income of AUD30,000 or more. Thirty-one percent of the respondents were unemployed with another 42 percent of the respondents reporting that they were either part-time or casual employees. Only 27 percent of the respondents reported being in full-time employment in the orthodox, formal sector of the economy. Hence, *LETS*systems in Australia predominantly consist of either unemployed or under-employed people earning below average incomes. In his study, Williams (1996) also found that *LETS* coordinators estimated that over one-third of *LETS*ystem members (34.1 percent) were unemployed.

Birch and Liesch (1996) revealed that respondents agreed the economic benefits of membership in a *LETS*ystem included feeling more generous with their *LETS* units than with cash dollars and their gaining interest free credit (Table 2). Further, respondents agreed that membership of a *LETS*ystem provides a number of psycho-social benefits which include creating wider horizons, providing greater opportunities and facilitating a better lifestyle (Table 2). In particular, the social benefits of *LETS*systems membership include the ability to network and establish closer personal and business relationships (Williams 1996). Other benefits include a better quality of life, greater freedom, increased self-esteem, greater control over one's life and more opportunities for members to use their skills (Birch and Liesch 1997).

**Table 2: Benefits of Membership in *LETS*ystems**

Benefits	Me
I feel more generous with my <i>LETS</i> units than with cash dollars	4.06
In the <i>LETS</i> , I can have interest free credit	3.98
The <i>LETS</i> has allowed me to widen my horizons	3.81
The <i>LETS</i> allows me to have a better lifestyle	3.73
The <i>LETS</i> has created new opportunities for me	3.72
I buy goods and services in the <i>LETS</i> that I otherwise would not be able to afford	3.70
Being a member of a <i>LETS</i> makes me feel more valuable	3.59
In the <i>LETS</i> , I can better use my skills	3.57
The <i>LETS</i> allows me to have a better quality of life	3.55
Membership in the <i>LETS</i> makes me feel more secure	3.22
I have experienced personal growth since I became a member of the <i>LETS</i>	3.19
I have more customers since I joined the <i>LETS</i>	3.07
I feel more wealthy since I became a member of the <i>LETS</i>	3.06
As a member of the <i>LETS</i> , I have more power over my life	3.02
I have acquired new skills by being a member of the <i>LETS</i>	2.95
As a member of a <i>LETS</i> , I feel more in control of my life	2.91
My self esteem has improved since I became a member of the <i>LETS</i>	2.90
I feel more free and liberated since I joined the <i>LETS</i>	2.90

(Scale: 5 point Likert Scale: Strongly Agree (5) to Strongly Disagree (1))

(\* significant at  $p<0.05$ , one tailed test,  $H_0 \mu : 3.00$  (n=371).

## Limitations of *LETS* Exchange

Despite the numerous benefits of *LETS*ystems, a number of limitations or disadvantages of membership in *LETS* have been reported (Birch and Liesch 1997; Williams 1996). In particular, it was noted at the 1995 National Australian *LETS* Conference that there are problems with *LETS* in Australia that need to be confronted and overcome if these exchange systems are to survive and prosper (Williams 1996). For example, membership problems concern low levels of trading, fear of debt, difficulties in attracting new members, and a limited range of goods and services available within the system (Jupp 1994). Further, in Australia, some *LETS*ystems have terminated after a short history, and in some systems there has been a high turnover of membership of management committees and of system membership generally.

A key limitation of *LETS* systems uncovered in the study undertaken by Birch and Liesch (1997) included the limited functionality of the *LETS* unit, in terms of not being able to use the *LETS* unit to pay federal taxes or to replenish stock (Table 3). Further, respondents agreed that there are limited goods and services available in the *LETS* system and this limits opportunities for reciprocity. Respondents also confirmed that trading within the *LETS* system can be more difficult due to: (1) out of date trading directories; (2) the need to be more tolerant when trading; and (3) the higher level of effort required to trade with *LETS* units rather than with cash dollars. However, most respondents disagreed that they are treated like a second rate customer when they pay with *LETS* units or that they have difficulty in spending their *LETS* units.

In summary, the limitations or disadvantages of membership in the *LETS* systems are limited trading opportunities due to the limited range of goods and services available in the system, trading difficulties due to trading directories being out of date, the higher level of effort required to trade with *LETS* units than with cash, and the need to be more tolerant when trading within the *LETS* system. Further, respondents indicated that the *LETS* unit has limited functionality, in terms of its not being useful for paying tax nor replenishing stock.

Table 3: The Limitations of Membership in *LETS* systems

Limitation	Mean
<i>LETS</i> units cannot be used to pay tax	3.78*
There is a limited range of goods and services available in the <i>LETS</i>	3.60*
<i>LETS</i> units cannot be used to replace stock	3.51*
Some of the listings in the trade directory are out of date	3.32*
You need to be more tolerant when trading in a <i>LETS</i> than when trading with cash	3.23*
It takes a fair degree of effort to trade within a <i>LETS</i>	3.02
I have found some members of the <i>LETS</i> to be unreliable and unprofessional	3.00
<i>LETS</i> units cannot be used to pay wages	3.00
I have difficulty spending my surplus <i>LETS</i> units	2.57
You are treated like a second rate customer if you are paying with <i>LETS</i> units	2.15

(Scale: 5 point Likert Scale: Strongly Agree (5) to Strongly Disagree (1))

(\* significant at  $p < 0.05$ , one tailed test,  $H_0 \mu : 3.00$  (n=371).

## Implicit Pricing in *LETS* Exchange

Exchange values in barter systems appear to deviate at times from market prices in the conventional money-based exchange system. Therefore, it was informative to determine how prices are determined within the *LETS* system. Interviewees in the pilot exercise to the Birch and Liesch (1997) study revealed that they feel more free and generous with their *LETS* units and therefore, depending on the nature of the transaction and the relationship between the transactors, they may be prepared to pay other than the equivalent cash market price. This study also set out to explore whether, and to what extent, prices within the *LETS* system vary from market prices in the cash, money-based system. In addition, it was investigated whether prices within the *LETS* system vary from market prices in the money-based system to an extent which depends upon the particular trading situation.

The preliminary pilot inquiry also indicated that close relationships, based on trust and goodwill among members are

central to the continuity and integrity of the *LETS* system. Williams (1995) argues that *LETS* trading facilitates the development of closer relationships and allows the establishment of stronger social networks in the community. Hence, the Birch and Liesch (1997) study sought to address whether the coordinating mechanism within the *LETS* system is trust stemming from the ability to establish and maintain good trading relationships, or whether the price mechanism (which mediates conventional exchange in money-based systems) was somehow employed in *LETS* exchange.

The study also sought to determine whether 'pricing' within the community-based barter system varies from pricing within the cash system. The researchers were interested to determine whether the *LETS* unit was valued similarly to a cash dollar, and whether the 'price' varied across trading situations. Respondents were asked whether the 'price' they pay for goods within the *LETS* system was above, at, or below the cash price. The results are presented in Table 4. The results indicate that most of the respondents (67.6 percent) stated that they pay the cash price, with another quarter (25.7 percent) stating that they pay less than the cash price, and only a few (6.7 percent) reporting that they pay above the cash price.

**Table 4: Price Paid for Goods and Services in the *LETS* system**

Price paid	Frequency	Percentage
At the cash price	242	67.6
Below the cash price	92	25.7
Above the cash price	24	6.7
<b>Total</b>	<b>358</b>	<b>100.0</b>

Respondents were also asked whether the 'price' they received for goods and services in the *LETS* system was above, at, or below the cash price. The results are presented in Table 5.

**Table 5: Price Received for Goods and Services in the *LETS* system**

Price Received	Frequency	Percentage
At the cash price	241	66.0
Below the cash price	108	29.6
Above the cash price	16	4.4
<b>Total</b>	<b>365</b>	<b>100.0</b>

Once again, most respondents (66 percent) stated that they received the cash price, with another 29.6 percent stating that they receive less than the cash price, and only 4.4 percent stating that they receive more than the cash price for their goods and services. Hence, there is a tendency for 'prices' within the barter system to be perceived to be equivalent to the cash dollar price.

Most respondents tended to agree that when they sell (mean = 3.43,  $p < 0.05$ ) and buy (mean = 3.49,  $p < 0.05$ ) goods and services within the system, the price they receive may vary depending upon the particular trading situation (Table 6). Hence, 'prices' within *LETS* systems may vary from market prices in the cash, money-based system to an extent which depends upon the particular trading situation.

**Table 6: Variations in Price Across LETS Transactions**

Statement	Mean (SD)
When I <b>sell</b> a particular good or service throughout the <i>LETS</i> , the price I receive may vary between sales depending upon the particular trading situation (eg., the person with whom I am dealing).	3.43* (1.21)
When I <b>buy</b> a particular good or service throughout the <i>LETS</i> , the price I receive may vary between sales depending upon the particular trading situation (eg., the person with whom I am dealing).	3.49* (1.00)

(Scale: 5 point Likert Scale: Strongly Agree (5) to Strongly Disagree (1))

(\* significant at  $p<0.05$ , one tailed test,  $H_0 \mu : 3.00$  (n=371).

### **LETSsystems, Income Taxation and Social Security in Australia**

The existence of domestic barter systems (both community-based and business-to-business) frequently incite concerns regarding their legality and integrity in the context of possible personal income taxation avoidance. In addition, *LETSsystems* are sometimes alleged to provide an opportunity for members to abuse social security unemployment benefits programs. While transactions in *LETSsystems* are recorded at the *LETSoffice* for accounting and taxation purposes, some transactions might be overlooked, while others might be understated. Nonetheless, each *LETS* unit is taken to represent a federal cash dollar equivalent for taxation (personal and business) purposes. It is clear, however, that while transactions are negotiable, and use of the federal cash system for making valuations is discouraged, creative accounting is both possible and likely.

In Australia, for the purposes of personal income taxation, *LETS* trading is not taxable unless the 'income' is earned from skills which are directly applied in the member's formal occupation in the monetised economy. For example, a medical practitioner is unable to deliver medical services through the *LETSsystem* without incurring a personal income taxation liability on these transactions, even if they are denominated in 'bunyas'. However, this same member can offer her artistic skills at painting portraits, and valued in 'bunyas', for exchange for other goods and services through the *LETSsystem*, without incurring a personal income taxation liability.

Income Taxation Ruling IT 2668 titled "Barter Transactions / Countertrade Transactions" provides guidance on taxation matters. In summary, for *LETSsystems* (identified as countertrade in the ruling), exchange is taxable if it falls within Subsection 25(1) of the Tax Act. For example, for a self-employed member, any 'bunya' consideration exchanged for services rendered in that person's normal course of endeavour is taxation assessable. For persons filing a taxation return with business income listed, the federal cash dollar value of any *LETS* currency must be included. The Act states that "... consideration which is merely the proceeds of a hobby, pastime, domestic or social arrangement, or the receipt of a windfall gain would not fall within the concept of income in Subsection 25(1). It is noted that a large proportion of transactions made through community-based countertrade organisations would not fall within the concept of income in Subsection 25(1)" (Para. 11, Taxation Ruling IT 2668).

For taxable business income that is received through *LETS* trading, expenditure incurred in earning that income can be offset against income, resulting in a net *LETS* position (profit or loss) valued in federal cash dollar terms for taxation assessment purposes. The Taxation Office accepts 'fair market value' for the valuation of *LETS* units for business purposes, where the cash equivalent of the goods is accepted unless it can be demonstrated that the trades are consistently at a level that is different from that comparable in the cash economy. In addition, business employers who pay their employees in 'bunyas' are likely to be liable for fringe benefits taxation (Pam 1992, <http://www.glasswings.com.au/GlassWings/utopia/lets.html>).

For the purposes of social security unemployment payments, the Australian Government has exempted *LETS* participation in the income tests for social security payment assessments. This provision has been officially sanctioned in the Deahm Amendment to the Social Security Act (Williams 1995). Hence, in effect, it is each member's responsibility to disclose truthfully income earned, both to the Taxation Office and the Social Security Department, when required. This is not a responsibility of the *LETS* organisation. Nonetheless, each member's net balance and transaction turnover is publicly available through the *LETSoffice* if so requested.

It does seem to be the view of the *LETS* membership generally, however, that 'bunyas' do not have physical existence and, thus, have no value of themselves within the federal system. Rather, they only record a member's net obligation to their community system; this is the member's obligation to return 'energy' to the community. In the context of the federal social security system, it also seems likely that the member's uptake of 'employment' in the *LETS* system is disguising an element of hidden unemployment that would otherwise be recognised in the formal economy. If this is the case, the real level of formal unemployment could indeed be higher than officially recorded, and its diminution through the *LETS* system might be sanctioned somewhat by the Australian Government for the political reason of expediency.

## The Future of *LETS* in Australia

At first glance, barter might appear to be more attractive in periods of economic recession and higher levels of unemployment. Hence, membership of *LETS* systems, and the aggregate level of trading through them, may be expected to be lower in a period of improved economic conditions and reduced levels of unemployment. This argument gains support from the relatively high percentage of *LETS* membership who are either unemployed or under-employed. However, in addition to the economic benefits of *LETS* trading, there appears to be significant non-economic benefits to be derived from membership in *LETS* systems. For example, close relationships, based on trust and goodwill among members are reported to be central to the continuity and integrity of the *LETS* regime (Williams 1996).

Indeed, respondents in the survey conducted by Birch and Liesch (1997) agreed that *LETS* systems would continue even in the light of an improved economic climate and that they would continue to trade despite improvement in the broader economic climate. Respondents to this survey reported that their trading within the *LETS* system had been successful because they had been able to establish and maintain good trading relationships with other members, rather than being able to simply obtain the most attractive price. For these members, sound trading relationships would appear to provide a more sustainable competitive advantage and possibly higher switching costs than would a low price. Hence, despite an upturn in the general economic climate, trading within the *LETS* system may be expected to continue, and to possibly develop further.

Williams (1996) found that the more established *LETS* systems have larger memberships, which infers that the overall membership of *LETS* systems will expand as younger systems mature. In addition, the protracted recession in the late-1980s and early-1990s in Australia appears to have made barter-style transacting more attractive and thus has facilitated the institutionalisation of these systems across Australia. Hence, to some extent, members' trading patterns and buying behaviours have changed and switching back to the orthodox, cash-based regime may prove unsatisfactory. Moreover, the significant psycho-social benefits which appear to be associated with membership in these systems may create strong exit barriers. These systems may continue irrespective of the economic climate or an improvement in the current level of unemployment in Australia.

## Conclusions

This paper reports on community-based *LETS* systems in the Australian context. Community-based *LETS* systems are operating throughout Australia and appear to have become institutionalised, as has business-to-business barter. Despite the macroeconomic cycle, they are likely to remain and could develop further. This suggests widespread imperfections in markets, particularly in markets for credit and for labour. These barter-based systems function alongside, and complement, the orthodox formal exchange regimes. The community-based *LETS* systems are characterised by trading in consumption goods and services, whereas the business-to-business systems trade predominately in intermediate inputs.

Fundamental to *LETS* systems is the premise that the local community's wealth rests with the local stock of goods, services, skills and association of people rather than the store of money available to the community. To lubricate trading, *LETS* systems create an exchange medium which, of itself, has no worth outside of the particular community. However, there are circumstances when these 'currencies' are deemed to be equivalent to federal cash dollars. The Australian Taxation Office and the Social Security Department have ruled officially on these circumstances.

A range of economic, psychological and social motivations and benefits have been identified from survey research in the Australian context. However, these systems are limited because of their lack of scope economies and the restricted functionality of the exchange units outside of the particular community. While these systems attempt to disassociate *LETS* trading from exchange in the cash-based economy, it does seem that the majority of participants relate their trading to an equivalent trade in the cash-based economy. Generally, the respondents to the Australian survey assert that in both purchasing and selling, the exchange 'price' they negotiate is at or about the comparable cash price,

although it can vary across trading situations.

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