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978-1-107-03254-5 - Constitutional Money: A Review of the Supreme Court's Monetary Decisions

Richard H. Timberlake

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CONSTITUTIONAL MONEY

This book reviews ten Supreme Court cases and decisions that dealt with monetary laws and gives a summary history of monetary events and policies as they were affected by the Court's decisions. Several cases and decisions had notable consequences on the monetary history of the United States; some were blatant misjudgments resulting from political pressures. The cases included begin with *McCulloch v. Maryland* in 1819 and end with the Gold Clause Cases in 1934–1935. Three institutions were prominent in these decisions: the Supreme Court, the gold standard, and the Federal Reserve System. The final chapter describes the adjustments necessary to return to a gold standard and briefly examines the constitutional alternatives.

Richard H. Timberlake is an emeritus professor of economics at the University of Georgia and an adjunct scholar at the Cato Institute. His research specialties are monetary policy and the history of central banking. Dr. Timberlake's most recent publications include *Monetary Policy in the United States: An Institutional and Intellectual History* and *Money and the Nation State*, edited with Kevin Dowd. He received his Ph.D. from the University of Chicago in 1959.

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A Cato Institute Book



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To

*Those sovereign people of the Constitution who freely and unwittingly
contribute to the undesigned order of human affairs*

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Preface

Constitutional Money examines nine Supreme Court decisions that markedly affected the U.S. monetary system in order to determine how and why money in use today became what it is. The exposition requires attention to three institutions: the Supreme Court because of its interpretations of the Constitution's money clauses, the gold standard and its operations as sanctioned by the Constitution, and the central bank – the Federal Reserve System – and its operations and constitutionality in the presence of a gold standard. The Court decisions begin with *McCulloch v. Maryland* in 1819 and end with The Gold Clause Cases in 1934–1935.

Everyone who thinks critically about the monetary system is aware of the significant difference between the gold-and-silver standard that the Framers originally prescribed and today's central-bank-fiat-money standard. Article 1, Section 8, of the Constitution states: "The Congress shall have power ... To coin Money, regulate the value thereof, and of foreign coin, and fix the standard of Weights and Measures." Article 1, Section 10, declares: "No state shall ... coin Money; emit Bills of Credit; make any Thing but gold and silver Coin a Tender in payment of Debts." Those passages taken together imply, first, that any legal tender money can only be gold and silver "coin," and, second, that Congress's monetary power is limited to managing the gold and silver contents of those coins. The Constitution does not prohibit banks and other institutions from creating common money managed by "the people," but it clearly denies the states and the federal government, by implication, any authority to change the base of gold and silver.

Barter of goods and services preceded money. Manifestly, any barter-medium that "the people" might use before a general money-medium appears is already "acceptable." Anyone can swap eggs for butter, or labor services for land; no authority in a free society can prohibit barter in any form. Recognizing this principle, the Framers dealt only with the creation

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of money at the two levels of government – federal and state. The “people,” however, could deal with each other on any terms mutually agreeable. That was a significant element of Freedom of Contract.

In spite of these obvious homilies, in 1933 with President Franklin Roosevelt’s strong assent and signature, Congress passed a law prohibiting the private ownership of monetary gold. While this law was rescinded in 1974, gold and silver are nowhere to be found in today’s monetary system. Their use as money is still illegal. Entrepreneurs who promote them as money are prosecuted, and even persecuted, by U.S. government agencies. The precious metals have become monetary apparitions, futilely reminding Congress of its constitutional limitations and responsibilities.

The Supreme Court’s monetary decisions have become a casebook of primary material begging for examination and possible reinterpretation. While the decisions reviewed here are only a small fraction of the total judgments that the Court has rendered over this time span, they have special importance in the economic world of markets because every transaction for goods, services, and capital also includes a sum of money.

The Framers wrote the Constitution for the ages, and they provided for changes by means of simple amendment procedures. Since the Constitution arranges for its own correction, it has no reason to be interpreted differently for different ages, social conditions, or other human circumstances. Judicial decisions that change the original meaning to fit some current social norm are illicit; they violate the substance of the document and destroy its reason for being.

In this book I package an analysis of constitutional cases on money with a summary history of government monetary policies and events through the twentieth century. My account explains how the Federal Reserve System as a central bank has interacted with the later Court decisions to undermine the Framers’ monetary constitution, and in so doing has promoted continuous inflation and ongoing public uncertainty regarding the future value of money. I conclude with some suggestions for a constrained monetary system, including the possibility for the reinstatement of an authentic gold standard.

Attempts have been made in the past to treat monetary affairs with some reference to the Constitution. First, Bray Hammond in his book, *Banks and Politics in America* (Princeton University Press, 1957), did a comprehensive study of the operations of the Second Bank of the United States and its struggle to remain in existence after Andrew Jackson became president. Hammond was a historian who spent most of his professional life on the staff of the Federal Reserve Board in Washington. His account is well

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written and engrossing, but flawed by his misunderstanding of the Framers' monetary constitution and its limits on the monetary powers of Congress. Furthermore, his uncritical acceptance of, and apology for, a central banking institution – The Second Bank of the United States – is highly questionable. The best that can be said for Hammond's work is that it provides a starting point for serious inquiry on the constitutionality of central banking.

Gerald Dunne's short book, *Monetary Decisions of the Supreme Court* (Rutgers University Press, 1960), followed Hammond's work, but did not challenge any of Hammond's analysis or assumptions. Dunne was the legal counsel for the Federal Reserve Bank of St. Louis and a law professor at St. Louis University. His work properly brought the monetary decisions of the Supreme Court into focus for the first time. However, he was not an economist, and he did not question the Court's authority or its clear violations of constitutional monetary precepts in the cases he reviewed.

Much the same is true of James Willard Hurst's work, *A Legal History of Money in the United States, 1774–1970* (University of Nebraska Press, 1973). Hurst, too, was a legal scholar, not an economist. Early in his work, he stated that his research was limited to legal history. He did not try to make “independent judgments that call for expertness [sic] in other than legal matters,” and he did “not purport to write an economic history of money in the United States.” However, anyone who examines the legal history of monetary decisions must be able to interpret the monetary conditions under scrutiny in order to evaluate the validity of the judicial decisions. Hurst's work therefore lacks economic substance.

A more recent work, *Pieces of Eight*, by Edwin Vieira, Jr. (Devin-Adair, 1983), has much worthwhile legal material in it and addresses critically and validly many of the Court's decisions on monetary affairs. However, Vieira is a legal scholar, so his excellent legal analysis understandably includes only a limited account of the economic events and institutions of the times. Nonetheless, his conclusions correlate highly with my own, even when we emphasize different issues.

A work that focuses primarily on the prohibition of gold ownership in 1934, *The Gold Clause* by Henry Mark Holzer, addresses the constitutionality of gold as the basis of the monetary system, especially with reference to gold clauses in contracts. Holzer's analysis is very useful but limited to the set of circumstances that accompanied the Roosevelt administration's campaign against gold and the resulting Court decision in the Gold Clause cases.

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I have also benefited significantly from my experience with The Independent Institute in Oakland, California, in editing (with Kevin Dowd) the book *Money and the Nation State: The Financial Revolution, Government and the World Monetary System* (New Brunswick, N.J.: Transaction Publishers). Many of the articles therein, especially those by David Glasner, Leland Yeager, and Frank van Dun are especially relevant to material covered in this book. Van Dun's "National Sovereignty and International Monetary Regimes" is especially useful to the Supreme Court's discovery of "sovereignty," and its decisions in the legal tender cases. I also refer to my own article in that volume, "Gold Standard Policy and Limited Government," when discussing the evolution of the gold standard

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through the nineteenth and into the twentieth centuries. Other articles in that work are germane to an understanding of the state's relationship to the creation and production of money, and can be read with profit.

Several economist friends and legal counsels have done yeoman service in editing earlier versions of this text. George Selgin and Jim Dorn have been unstinting, unselfish, and constructive critics. I owe each of them a great debt. Others who have contributed corrections to my text and offered constructive comments include: David Boaz, William Beranek, Kevin Dowd, Roger Garrison, Tom Humphrey, Roger Pilon, Richard Salsman, Walker Todd, Larry White, and Leland Yeager. I also thank my good friend and financial analyst, Tom Wilkins, for suggesting useful references and for his stimulating discussions while the book was in progress. My thanks as always to my wife Hildegard for her constructive criticisms and constant encouragement. Finally, I want to thank my grown-up children, Tommy, Chris, Megan, Dave, and Dick, for reading various sections; for their skeptical review of some arguments; and for nagging me to finish. I also thank my brother Allen for one especially important observation on past Court decisions.