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The Evolution of Money: A Story of Constitutional Nullification

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ARTICLES

THE EVOLUTION OF MONEY: A STORY OF CONSTITUTIONAL NULLIFICATION

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I. INTRODUCTION

The history of money in America demonstrates that even the United States Constitution could not dictate or preserve a singular conception of money.¹ The Constitution specifically provides that gold and silver coins will be the money of the United States and arguably prohibits the issuance of paper money.² Yet, gold and silver coins have vanished from the monetary market, even though the two metals are still important commodities and gold is still regarded by some as a possible hedge against inflation. Moreover, the coins that remain in circulation, including the Susan B. Anthony dollars, are made out of a complex

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² The Constitution allows Congress to coin money but supplies no definition of money itself. In 1787, English dictionaries defined money as metallic coin. See George Bancroft, A Plea for the Constitution Wounded in the House of its Guardians, app. at 82-83 (1886). The word “dollar," also not defined, appears twice in the Constitution. First, it appears in Article 1, § 9, clause 1:

The migration or importation of such persons as any of the states now existing shall think proper to admit shall not be prohibited by the Congress prior to the year one thousand eight hundred and eight, but a tax of duty may be imposed on such importation, not exceeding ten dollars for each person.

U.S. Const. art. 1, § 9. Second, the word “dollar" appears in the 7th Amendment: “[I]n Suits at common law, where the value in controversy shall exceed twenty dollars, the right of trial by jury, shall be preserved ...” U.S. Const. amend. VII. The two words, “money” and “dollar,” however, are not synonymous, nor is the concept of money limited to dollars.

³ See generally Woodruff v. Mississippi, 162 U.S. 291, 307 (1895) (Field, J., concurring). In speaking of the views of the framers of the Constitution, on the subject of money, it was said that “at that time gold and silver moulded into forms convenient for use, and stamped with their value by public authority, constituted, with the exception of pieces of copper for small values, the money of the entire civilized world ... From the earliest periods in the history of the world down to the present time. It was with “four hundred shekels of silver, current money with the merchant,” that Abraham bought the field of Machpelah, nearly four thousand years ago.

Id. at 314.
alloy of cheap metals, not gold and silver. Federal Reserve notes, popularly known as dollar bills, and printed on the familiar green paper in different denominations, now circulate as money. These paper dollars enjoy incredible prestige across the globe, becoming the most coveted "hard money" in international markets.

Over the course of American history, Congress used the force of law first to create money-substitutes that financed the deficit whenever the quantity of constitutional money was insufficient. It then invented a new official currency in Federal Reserve notes that completely replaced the constitutional coin. This transformation of money occurred without any amendment to the monetary clauses of the Constitution. These clauses have been gradually nullified by a simple urge to "do the right thing." The eventual triumph of paper dollars and the concomitant nullification of the monetary clauses have occurred over the entire life span of the Constitution, a journey that still seems unfinished. Along the way lie dramatic periods when the transition of money from metal to paper was politically resisted and constitutionally challenged. There were even a few setbacks. Ultimately, however, the campaign for paper dollars marched on, winning most battles.

Each of the three branches of federal government played a significant supportive role in bringing about the nullification of the monetary clauses. Congress, however, apparently bore the most responsibility. Innovative attempts to launch myriad forms of paper money, even when originated in the Treasury Department, could not become law without

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3. See 31 U.S.C. § 5112(b) (1994). The dollar, half dollar, quarter dollar, and dime coins contain three layers of metal. See id. The outer two layers are made out of an alloy of 75% copper and 25% nickel. See id. The inner layer is copper.

4. Historically, philosophers and writers viewed the creation of paper money as an evil. In Goethe's FAUST, completed in 1832, for example, when Chancellor introduces the idea of paper money, the Emperor remarks, "A most enormous cheat—a crime, I fear!" JOHANN WOLFGANG VON GOETHE, FAUST 58 (Bayard Taylor trans., Houghton, Mifflin and Co. 1881). But Mephistopheles, defending paper money, says, "Such paper, stead of gold and jewerly, So handy is." See id. at 60. In 2500 B.C., the Egyptians were perhaps the first to use metal rings as money. However, during the T'ang Dynasty (618-907 A.D.), the Chinese were the first to use paper money.

5. With gold and silver money as the point of reference, money-substitute means an instrument that represents gold and silver. Thus, money-substitute is by definition convertible into real money.

6. Constitutional money, for the purpose of this Article, means gold and silver. See A.J. Frame, Money and Wealth, 11 BANKING L.J. 152-33 (1894) ("What constitutes a sound circulating medium? My answer is gold and silver (the only real money) and an amount of paper promises to pay, in real money . . . .").

7. In contrast to money-substitute, official money in the form of Federal Reserve Notes neither represents gold or silver nor is redeemable in these metals.

8. The idea of constitutional nullification parallels the one in criminal law. See Jack Weinstein, Considering Jury "Nullification": When May a Jury Reject the Law to Do Justice, 30 AM. CRIM. L. REV. 1 (1993) (explaining that in criminal law nullification occurs when a jury, prompted by its own sense of fairness, does not follow the law and refuses to convict a guilty person).
congressional approval. Moreover, the Constitution grants Congress, not the Executive branch, the power to coin money and "the power to borrow Money on the credit of the United States." Invoking these and other enumerated powers, Congress asserted a sovereign right to control the quantity and quality of money soon after the adoption of the Constitution. The need to assert such a power became more urgent when the United States faced foreign and civil wars but had little gold or silver to fight them. In moments of crisis, paper money was an inferior but a reliable ally to prosecute wars and save the Union. Forms of paper money conceived in emergencies frequently lingered on even in peaceful times, as many were declared legal tender.

When the law adopts a certain form of money as legal tender, the adopted form acquires an official status that allows debtors to lawfully discharge their monetary obligations by tendering official currency. Money, as an officially accepted medium of exchange, facilitates commercial transactions as it passes freely from hand to hand without reference to the character or the credit of the person who offers it. Sellers accept official currency on a widely shared presumption that the money so obtained will continue to serve as a medium of exchange in the future. In different societies and in different times, metal coins, wampum, animal skins, whiskey, bullets, and tobacco functioned as official currency.

An official currency, though important, is not critical to the functioning of a monetary system. Even when the law authorizes a certain medium of exchange as official currency, the market continues to breed new substitutes because safety-conscious merchants prefer to deal in money substitutes rather than in official currency.

In over four thousand years of the history of money, "a public money system is of comparatively late origin while the device of legal tender is a still more

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9. See generally U.S. CONST. art. I, § 8, cl. 2. This clause gives Congress the power to borrow money. See id. Using this power, Congress authorized diverse forms of treasury notes and bonds. See id.

10. Id.

11. See discussion infra notes 23-41.


13. See Arthur Nussbaum, Basic Monetary Conceptions in Law, 35 MICH. L. REV. 865, 899 (1937). In Massachusetts, legal tender was born in 1631. See id. In other colonies, legal tender status was extended to various commodities such as bullets and tobacco. See id. Tobacco currency in Maryland was recognized as late as 1828. See Crain v. Yates, 2 H. & G. 332 (Md. 1828).

14. Over matters of money, a tension exists between the law and the market. This tension occurs because the law often lags behind the market in recognizing new forms of money. The law needs to define money so that it may be officially tendered to discharge debts. The market needs to define money so that commercial transactions may be executed efficiently. When the two definitions disagree, the law inevitably defers to the market's conception of money.
recent invention." Thus, money in the functional sense is not synonymous with legal tender or official currency. In a free economy, the market rather than the law dictates which form of money is used in commercial transactions. The law is still needed to recognize monetary conventions of the market and, sometimes, to clean up the mess the market leaves behind its monetary adventures. But rarely has the development of money been the pure artifact of governmental policy or political decision. Money is a living creature of the market and its form changes to facilitate commercial transactions in an ever more efficient, convenient, and safe manner. As such, most innovations in monetary practices are attributable to the decisions of the market.

The rise of paper dollars is thus a compelling story of interaction between law, war, and market. Economic necessity caused by wars forced lawmakers and judges to bend and evade the monetary clauses to deal with the shortage of gold and silver, the money of the Constitution. Law, most notably through the concept of promissory notes, provided the technical infrastructure to devise clever financing as well as to cloak and legitimize blatant deviations from the letter and spirit of the Constitution. This adaptation to the forces of market and war upset those most learned in the history and law of the Constitution, including Thomas Jefferson, John Marshall, and Joseph Story, all of whom insisted that the monetary clauses left no room for monetized paper.

Bankers and merchants, however, paid more attention to needs of the market just as Congress did to dictates of the battlefield. Gradually and steadily, market-driven money and war-driven law triumphed over the Constitution. Textualists and originalists, who demanded that law develop within confines of the constitutional text or its original meaning, begrudged that the jurisprudence of money could not be so contained.


16. See generally James B. Thayer, Legal Tender, 1 Harv. L. Rev. 73 (1887). The Constitution does not say that Congress may make coin a legal tender. See id. at 83.


The main purpose of this Article is to present a thesis that no legal text, not even the most authoritative, such as the United States Constitution, can fully predict how the future will discard some of the most obvious paradigms. The thesis illuminates the study of money—a construct that has defied prediction and annulled the reigning paradigm of each distinct period. The Article explains how the monetary clauses of the Constitution, which incorporated a universal truth at the time of their adoption, failed to halt the evolution of money. The hindsight analysis further clarifies that the historical context itself, which compelled the adoption of the monetary clauses, furnished irrefutable proof that money cannot be a mere creature of law, nor can its concept be fossilized in the paradigm of any age. Several authors have surveyed the legislative history of the monetary clauses, but each has failed to provide a comprehensive analysis of the forces that first shaped and then repudiated the monetary clauses. As such, this Article examines the legislative history and the constitutional developments of the monetary clauses in a new analytical light. A secondary, though no less important, purpose of this Article is to demonstrate how the promissory note, an instrument that merchants created to pay for commercial transactions, has supported the evolution of money from precious metal to paper dollars. This technical discussion is useful in understanding a genetic connection between paper money and promissory notes.

Furthermore, this Article will perhaps provide insights into the future evolution of money if the United States were to merge its economy with those of other nations in its region. Even if a regional merger fails to occur, the prevailing conception of money is already moving from paper to plastic and electronic accounting. Although this Article does not examine the regional monetary union or modern forms of money, such as credit cards and digital money, the reader is advised to keep current monetary practices in mind. While appraising the ensuing historical analysis, ask whether the law or the Constitution is likely to play a leading role in the future of money.

21. Ideally, this Article will benefit law students in a better understanding of Articles 3 and 4 of the Uniform Commercial Code (UCC). See generally U.C.C. Arts. 3-4 (1998).
22. See Peter L. Bernstein, A Primer on Money, Banking, and Gold 4-5 (1965).
With the growing complexities of the marketplace and of the methods of production ... [money] becomes more and more abstract, until it ... consists primarily of numbers ... [although we still use some currency (worth, in reality, no more than the paper it is printed on) and some coins, most of the money we spend moves ... through the writing of checks ... to debit one account ... and to credit another. Thus, most of our money has no real value or tangible existence: we can't see it or feel it or smell it.

Id.
Part I of this Article introduces the Article’s purpose. Part II examines the historical context in which Congress drafted the monetary clauses of the Constitution. This background is essential for understanding subsequent changes in the conception of money. Part III discusses banknotes, the money the market created to replace gold and silver coin. Part IV analyzes how Congress converted its power to borrow into a power to create payment instruments, including United States notes, popularly known as greenbacks. Part V explores major legal events that led to the monetary union of the United States. Part VI briefly examines the present monetary practices. The final part of the Article concludes the discussion.

II. FRAMING OF THE MONETARY CLAUSES

A. Bitter Experience of the Continental Congress

Upon waging a “just and necessary war” in the American Revolution, the Continental Congress had little money, that is, gold and silver, also known as specie. As the supply of specie was inadequate to conduct the war, Congress began to issue bills of credit, an instrument designed in the image of the familiar promissory note. A bill of credit was issued as a negotiable promissory note in a bearer form so that it could freely circulate as a money-substitute. Until the bill was converted into specie, it passed from person to person performing the function of a medium of exchange, that is, facilitating the buying and selling of goods and services. Thus, bills of credit, also known as “continental currency,” were the promise of the Continental Congress to pay the face value of each bill in silver coin to any holder on demand. To make the

23. In the eighteenth century, money in all major commercial nations was gold and silver.
24. On November 29, 1775, Congress considered the report of the Committee on the State of the Treasury and resolved to issue bills of credit in the amount of $3,000,000. The committee was authorized to consult with the printer and contract for proper paper. See generally 3 J. Continental Cong. 390 (1775). The bills were issued in equal numbers (83,334) of denominations ranging from one to eight dollars per bill. See id. at 398.
25. This negotiability is a shared characteristic of money and money-substitutes. If a negotiable instrument is in a bearer form, it can be transferred by mere delivery, and thus its ability to act as a medium of exchange is further enhanced. A non-bearer negotiable instrument, which must be signed and delivered for further negotiation, is somewhat cumbersome, though it still may be used as a money-substitute.
26. See 3 J. Continental Cong. 390, 407 (1775). The bill of credit had the following design:

<table>
<thead>
<tr>
<th>No.</th>
<th>Dollar</th>
</tr>
</thead>
<tbody>
<tr>
<td>CONTINENTAL CURRENCY</td>
<td></td>
</tr>
<tr>
<td>THIS bill is a bill of exchange for the value of (in) dollars, payable to bearer on demand, according to a resolution of Congress passed at Philadelphia, November 29, 1775</td>
<td></td>
</tr>
</tbody>
</table>

See id.
convertibility of paper bills credible, the confederated colonies created a fund to assure the redemption of bills into specie. The Continental Congress did not invent the bill of credit; it simply used a payment instrument that the market had designed to facilitate payments. Nor was the Congress the first to deploy these paper bills for public financing; the American colonies had already used such bills to finance wars, though with less than honorable market success.

Soon after paper bills were issued, Congress was notified that "a sundry person in this city [Philadelphia] have refused to receive in payment or give currency to the bills." A committee was formed to look into the matter and report to Congress. A few days later, Congress was informed that "several evil disposed persons, in order to obstruct and defeat the efforts of the United Colonies . . . have attempted to depreciate the bills of credit issued by the authority of this Congress." Moreover, nonacceptance and depreciation of paper bills were not the only problems. It was also reported that counterfeit bills had surfaced in the colonies, challenging the very authenticity of the bills of credit.

To save paper bills from utter disrespect and nonacceptance, Congress passed a toughly worded resolution declaring that any person who refused to receive bills of credit issued by Congress would be considered an enemy, precluded from all trade, and shunned by the community. Whenever the law forces people to transact in a certain currency—paper, corn, or tobacco—that currency becomes a legal tender. By invoking sanctions of law, the Continental Congress initiated
a pattern of clouding the distinction between metallic money and promissory paper.

Neither the threat of law nor revolutionary patriotism, however, could cure defects in the issuance of bills of credit. The logic of the market was simple: if Congress had money, it would not issue bills of credit, and if it had no money, its promise to pay silver on demand was empty. The paper bills, therefore, were inherently risky instruments. As such, the people who refused to accept paper bills altogether believed that Congress had no silver to redeem them. The people who discounted their face value believed that Congress did not have enough silver to redeem all the bills it had issued. The fact that the Continental Congress had issued an oversupply of paper bills was no secret. The Committee on the Treasury itself reported that "so much paper money" had been issued that "its value [was] progressively declining." It recommended that the quantity of paper bills in circulation be considerably reduced "to prevent the discontents and mischiefs which must follow a further depreciation of the paper money." Learning a bitter lesson in inflation and realizing that no government could have more money by simply printing more of it, Congress limited the quantity of paper bills of credit to $200 million in 1779. Despite this cap on quantity, however, the bills of credit continued to fall in value. In 1780, Congress was informed that, despite all the efforts to support their credit, paper bills were trading "[a]t least 39-40ths below their nominal value ...." Instead of questioning the patriotism of the

33. "The state can give paper money or extremely debased coin debt-canceling power enforceable by the courts, but the experience of history proves that it is powerless to enforce it upon the community as a medium of exchange." Phanor Eder, *Legal Theories of Money*, 20 CORNELL L. REV. 52, 60 (1934).

34. A modern example would be junk bonds, particularly if individuals were forced to sell goods and services in exchange for these bonds.

35. See *The Wealth of Nations* 329 (James Thorold Rogers ed., 1869). Smith stated that:

A positive law may render a shilling a legal tender for a guinea, because it may direct the courts of justice to discharge the debtor who has made that tender. But no positive law can oblige a person who sells goods, and who is at liberty to sell or not to sell, as he pleases, to accept of a shilling as equivalent to a guinea in the price of them.


37. *Id.*

38. See 15 J. Continental Cong. 1053 (1779).

39. 16 J. Continental Cong. 263 (1780). It was brought to the attention of the Continental Congress that bills increasing in quantity beyond the sum necessary for the purpose of circulating medium, and wanting, at the same time, specific funds to rest on for their redemption, they have seen them daily sink in value, notwithstanding every effort that has been made to support the same . . . whereby the community suffers great injustice, and the public finances are deranged . . . [therefore] it is necessary speedily to reduce the quantity of paper medium in
people, Congress began to understand the message of the market: a bill of credit would fail to trade at its face value if the market was unsure about its full convertibility into specie. The paper bills were destined to depreciate as there was no specie to redeem them. In view of their falling value, Congress asked states to revise their laws that had made these bills a legal tender.40 Nothing worked, however, and paper bills continued their downward slide. By 1781, paper bills were worthless and ceased to circulate as either money or money-substitute, leaving behind a new adage in American vocabulary: "not worth a continental."41

B. Constitutional Convention on Money

1. The Purity of Gold and Silver

The consummate failure of continental bills of credit was well-known when the Constitutional Convention was held in the summer of 1787. Everyone recognized the evil of what they called "paper money," a popular name for bills of credit. On May 29, 1787, Edmund Randolph, a deputy from Virginia, opened the "main business" of the Constitutional Convention. In speaking of the defects of the Confederation, he pointed out how the authors of the Articles of Confederation, although deserving his high respect, had not foreseen the chaos caused by paper money.42 On the same day, Charles Pinckney, a deputy from South Carolina, laid before delegates the draft of a federal government called "Plan of a Federal Constitution." On monetary issues, Pinckney proposed that "the legislature of the United States shall have the power ... to borrow money, and emit bills of credit ... to coin money, and regulate the value of all coins."43 In addition to these monetary powers, Pinckney proposed monetary disabilities to the effect that no state shall "emit bills of credit; nor make anything but

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40. See J. Continental Cong. 269 (1780).
41. See I MITFORD MATHEWS, A DICTIONARY OF AMERICANISMS 383 (1951). The expression originated from the 1780 adage "not worth a Continental dam." OLIVER TAYLOR, HISTORIC SULLIVAN 97 (1909). A "dam" was an Indian coin of value less than one cent. See id.
42. See JONATHAN ELLIOT, DEBATES ON THE FEDERAL CONSTITUTION 126 (1861) [hereinafter DEBATES]. These debates in the Convention were held at Philadelphia in 1787. Published under the sanction of Congress, a diary of the debates of the Congress of the Confederation was maintained by James Madison, a member and deputy from Virginia. See id.
43. Id. at 130 (quoting U.S. CONST. art. VI).
gold, silver, copper, a tender in payment of debts . . . " On August 16, 1787, delegates debated monetary clauses of the draft constitution. No objection was made to making gold and silver the money of the new republic.

Long before the framing of the Constitution, precious metals were used as money in and among markets of the world. Cheaper metals and raw materials were used as money only when precious metals were unknown or scarce. In the late eighteenth century, money was still international in character as it had been for many centuries. Most communities shared a common tradition that nothing but precious metals should be the circulating medium in the markets. Nations engaged in international commerce were particularly under a market-driven constraint to adopt gold and silver as the transactional money. The idea that a nation could create its own fiat currency to replace gold and silver ran counter to the custom of the eighteenth century.

Gold and silver constituted the preferred money of the world primarily because supply was limited, a fact in conformity with the historically-tested monetary principle that an oversupply of money diminishes wealth, disrupts social order, and destabilizes the market. Oak leaves, scattered in abundance, as John Adams put it rather poetically, would most certainly fail to serve as a reliable form of money. Therefore, the natural scarcity of gold and silver was a virtue to be preserved in both law and economics. Even between the two metals, because gold has always been more limited in supply than silver, its status as money was both idealized and protected. However, both gold and silver, each in their respective capacity, served the market. Silver, cheaper than gold, was useful for small bargains, whereas gold was a more convenient medium to execute large and expensive transactions.

44. A committee, consisting of five members, called the Committee of Detail was appointed to prepare the text of the Constitution conformable to the proceedings of the Convention. See id. The draft constitution had the following monetary provisions: the legislature of the United States shall have the power to coin money; to regulate the value of foreign coin; to borrow money; and to emit bills on the credit of the United States. See id. at 381.

45. See id. at 434-35.

46. See Nusbaum, supra note 13, at 886.


48. See Bancroft, supra note 1, at 23.

The preference for silver and gold was rooted in the notion of "intrinsic value," the reigning paradigm of the age that a thing worthless in its own right could not qualify as money. Fierce opposition to paper money was motivated in part by the fact that a piece of paper had no inherent value. Gold and silver had market value as commodities, as they still do. Their market values may fluctuate against each other and with respect to other goods and commodities. Nations may differentiate gold and silver coins by engraving images of their kings and presidents or attributing different weights and units of account. Yet the underlying bullion, the pure grains of gold and silver, recognizable throughout the world, remain the same. For centuries this core value of gold and silver was the mainstay of metallic money.

The framers of the Constitution were familiar with the advantages of metallic money and knew the universal superiority of gold over silver. Therefore, at the urging of Alexander Hamilton, they adopted a bimetallic standard. Ironically, however, it was gold that was added last to the monetary clauses. Silver, the "ancient money" of the American colonies, had its status deeply entrenched in the consciousness of the people and realities of the market. During the years of the Continental Congress, a proposal was made to make silver the single money of the United States. It was therefore unthinkable to demonetize silver. Recognizing the preeminence of gold, emanating

50. The question whether the sovereign could debase the intrinsic value of coin generated copious scholarly comment. See B.A. Milburn, *Money and the Constitution*, 4 Law Notes 124 (1900-01) (Congress may have the power to coin money and regulate its value, but it does not follow that the mere stamping of a coin will fix its intrinsic or natural value as its face value.). Even William Blackstone commented on this topic: "[T]he king's prerogative [seems] not to . . . [debase or enhance] the value of coin, below or above the sterling value, though Sir Matthew Hale appears to be of another opinion." WILLIAM BLACKSTONE, *COMMENTS ON THE LAWS OF ENGLAND* 277 (Thomas M. Cooley ed., 3rd rev. ed. 1803)


52. At the time of adoption of the Constitution, Spanish, French, English, and Portuguese coins were in wide circulation and constituted the money supply of the United States. See Loughlin, supra note 49, at 10. Although some gold was current, silver coins alone were legally recognized in colonial times. Of all foreign coins, the Spanish milled silver dollar was, and for decades had been, the money of American markets. See also MAURICE MULLIN, *THE MONEY OF THE UNITED STATES* 18 (1894). The Spanish milled silver dollar was also the unit of common account. Accordingly, market transactions, exchange rates for other foreign coins, and contracts were measured in terms of Spanish dollars. As no national coins existed when the Constitution was framed, one may safely conclude that the dollar mentioned in the Constitution was a unit equivalent to the Spanish silver. The Act of 1792, which established the United States Mint, further clarified the Constitution by defining dollar as a unit of account in value and weight similar to the Spanish milled dollar. See Act of Apr. 2, 1792, ch. 16, 1 Stat. 246.

“from its intrinsic superiority, as a Metal, from its greater rarity, or from the prejudices of mankind.” Hamilton first advocated the adoption of gold as the single standard. However, his proposal was incompatible with the silver-driven realities of the American market. Nevertheless, as a compromise, gold was added to the monetary clauses.

The adoption of a bimetallic system was a pragmatic decision to create an adequate supply of money needed to develop a new country. There was simply not enough gold to support the emerging economy. The goods produced at the time were basic and inferior and therefore unable to fetch gold from foreign markets. The little gold available was insufficient to buy even the needed capital goods from Europeans who demanded gold. In contrast to gold, silver was a more suitable currency to complete a high volume of cheap transactions. Silver mines in South America further assured what Hamilton called “an extraordinary supply” of the metal through the conduit of West Indies, the important trading partners of the United States.

2. The Evils of Paper Money

The only monetary provision discussed at some length in the Constitutional Convention was the one regarding paper money, technically known as bills of credit. The draft constitution empowered Congress to emit bills on the credit of the United States. A similar power was previously given to the Continental Congress in the Articles of Confederation. A motion was made on the floor of the Constitutional Convention to strike out “and emit bills on the credit of the United States” from the draft constitution. Gouverneur Morris of Pennsylvania, who made the motion, warned that moneyed interests

54. _Nessi Report, supra note 51, at 577. Hamilton argued that gold was a more stable metal and even correctly predicted that the value of silver would fall against the value of gold. See id. at 577.
55. _Id. at 580. See also_ JOHN KENNETH GALBRAITH, _Money_ 12 (rev. ed. 1993). “San Luis Potosí, Guanajuato and the other rich silver mines of Mexico, some of which continue to operate to the present day, and their counterparts in Peru were the source of the American treasure.” _Id._
56. _See Art. of Confed. art. XII._ All bills of credit issued, monies borrowed and debts contracted by, or under the authority of Congress, before the assembling of the United States, in pursuance of the present confederation, shall be deemed and considered as a charge against the United States, for payment and satisfaction whereof the said United States, and the public faith are hereby solemnly pledged.
57. _See generally_ JAMES WILLARD HURST, _A Legal History of Money in the United States, 1774-1970_ (1973). Congress had no authority to lay taxes, either before or under the Articles of Confederation. See id. at 5. The states and Congress had concurrent authority to coin money under the Articles of Confederation. See id. at 8.
58. _Debates, supra note 42, at 434._
would oppose the new federal government if paper issuances were not prohibited. The delegates in favor of the motion highlighted the evils of paper money. James Wilson of Pennsylvania said that removing the possibility of paper money would "have a most salutary influence on the credit of the United States." Oliver Ellsworth of Connecticut spoke most eloquently and "thought this a favorable moment to shut and bar the door against paper money." The mischiefs of various experiments in paper money, he argued, had disgusted all the respectable parts of America.

No delegate vigorously opposed the motion. Virginia delegates, however, were unsure whether a total ban on the issuance of paper bills would be in the best interests of the nation. They argued that complete prohibition of paper bills would tie the hands of Congress in all emergencies. James Madison proposed that Congress should be authorized to issue bills of credit in emergencies, but without making them a legal tender. "This will remove the temptation to emit them with unjust views; and promissory notes, in that shape, may in some emergencies be best." Likewise, Virginia's George Mason expressed similar doubts on the subject, though "he had a mortal hatred to paper money." The revolutionary war, he pointed out, "could not have been carried on, had such a prohibition existed." Edmund Randolph, another delegate from Virginia, opposed a total ban on bills of credit, "as he could not foresee all the occasions that might arise." Despite these reservations, Virginia voted for the motion because Madison became satisfied that the motion to strike out the words from the draft constitution "would not disable the government from the use of public notes, as far as they could be safe and proper; and would only cut off the pretext for a paper currency and particularly for making the bills a tender, either for public or private debts."

58. George Reed of Delaware warned that, if the words were not struck out, they "would be as alarming as the mark of the beast in Revelation." Id. at 435. Pierce Butler of South Carolina reminded delegates that paper was not legal tender in any country in Europe and supported the motion for disarming the government of such a power. See id. Even John Francis Mercer of Maryland, "a friend to paper money," was reluctant "in the present state and temper of America" to approve the measure. Id.

59. Id.
60. Id.
61. See id.
62. Id. at 434.
63. Id.
64. Id.
65. Id. at 435.
66. See id. The vote was as follows: "New Hampshire, Massachusetts, Connecticut, Pennsylvania, Delaware, Virginia, North Carolina, South Carolina, Georgia, ay, 9; New Jersey, Maryland, no, 2." Id.
67. Id.
Although the delegates were unsure about placing a total ban on Congress's power to issue paper money, they were certain about denying states even a conditional power of issuance. The draft constitution allowed states to issue bills of credit with the consent of Congress. However, even this limited power was unacceptable to most delegates. On August 28, 1787 James Wilson of Pennsylvania and Roger Sherman of Connecticut moved to make the prohibition "absolute, instead of making the measures allowable ... with the consent of the legislature of the United States."\(^{68}\) Sherman did not want to leave a loophole for lobbyists. He argued that, "[i]f the consent of the [federal] legislature could authorize emissions of it, the friends of paper money would make every exertion to get into the legislature in order to license it."\(^{69}\) The motion was carried eight to one. \(^{70}\)

Thus, the final text of the Constitution enumerates monetary powers for Congress and accumulates monetary disabilities against states. Monetary powers, embodied in Article 1, section 8, are addressed to Congress.\(^{71}\) These provisions empower Congress to borrow money on the credit of the United States, coin money, and regulate the value of domestic and foreign coins. Monetary disabilities, embodied in section 10, are aimed at the states.\(^{72}\) They disable states from coining money, issuing bills of credit, making anything but gold and silver coin a tender in payment of debts, or passing laws impairing the obligation of contracts.\(^{73}\)

Several conclusions may be drawn from the brief remarks the delegates made at the Constitutional Convention. First, most delegates used the term "bills of credit" interchangeably with "paper money" even

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68. See id. at 484.
69. See id. at 485.
70. See id. at 435. Virginia voted against the motion; Maryland abstained. See id.
71. See U.S. CONST. art. I, § 8. The Congress shall have the power: "To borrow money on the credit of the United States" Id. cl. 2. "To coin money, regulate the value thereof, and of foreign coin, and fix the standards of weights and measures." Id. cl. 5. "To provide for the punishment of counterfeiting the securities and current coin of the United States." Id. cl. 6.

It is important to keep in mind that the Constitution does not prohibit: (1) the emission of bills of credit by Congress or individuals and corporations chartered under state laws; or (2) the creation of anything but gold and silver coin as legal tender. See Williams Watts Felwell, Evolution in Paper Money in the United States, 8 MINN. L. REV. 566 (1924).

72. See U.S. CONST. art. I, § 10. "No State shall ... coin Money; emit Bills of Credit; make any Thing but gold and silver Coin a Tender in Payment of Debts; pass any... law impairing the Obligation of Contracts." Id.

73. Even in this textual framework, monetary powers and disabilities are mostly asymmetrical. Only with respect to coining money is the power of Congress contrasted by a matching disability against states. No such symmetry exists with respect to other monetary clauses. For example, the Constitution prohibits states from making anything but gold and silver legal tender. No Congressional power has been correspondingly granted with respect to legal tender. Likewise, the Constitution is silent over whether Congress may issue bills of credit or impair obligations of contracts.
though the two concepts were not always identical in meaning. Second, delegates knew that bills of credit were not inherently legal tender, for otherwise Madison would not have suggested empowering Congress to issue non-tender bills. Third, the ban on state issuance of bills of credit was absolute. Fourth, Madison’s rationale that Congress would retain the power to issue bills of credit in emergencies was broadly shared on the floor of the Constitutional Convention. Finally, it can be said with “moral certainty” that the framers of the Constitution prohibited making any paper bills a legal tender money.74

What remains unclear from the Constitutional Convention and the Constitutional text and what has befuddled many generations of lawyers and judges is a simple question: Has the Constitution outlawed all forms of bills of credit? The constitutional phrase “to emit bills of credit” seems obtuse, as it is couched in language no longer used in the law or elsewhere; the word “emit” is now associated with odors rather than instruments of money. The term “bills of credit” has likewise lost its legal usage. Despite the obscurity surrounding bills of credit, most certainly for later generations, no delegate of the Constitutional Convention demanded a clarification of its meaning. The experience of the Continental Congress had proven beyond a doubt that nothing but specie ought to be the money of the United States. For many delegates, therefore, important technical definitions between tender and non-tender bills of credit and between public bills of credit and privately issued promissory notes were irrelevant.

Only Madison drew a timid but important distinction between tender and non-tender bills of credit, suggesting that a non-tender bill of credit was more like a “promissory note” that Congress should be able to issue in emergencies.75 This distinction would later become the most insightful comment made regarding the future of money. Otherwise, there was little disagreement over the proposed monetary provisions, in part because many delegates were not as interested in monetary provisions as they were in political issues. “On the whole, the monetary clauses of the Constitution seem to have won exceptional favor, offering what was objectionable to the fewest people and what was commendable to the most.”76 Thus, the Constitution discarded the concept of paper money from the U. S. monetary system, providing no clue whether the adoption of gold and silver as the constitutional money was designed to suppress all forms of bills of credit.

75. See DEBATES, supra note 42, at 435. For a discussion on how Madison’s distinction made sense in the contemporaneous law of negotiable instruments, see infra text accompanying notes 139-42.
76. BRAY HAMMOND, BANKS AND POLITICS IN AMERICA 103 (1957).
III. STATE-CHARTERED PAPER MONEY

If the Constitutional Convention had suppressed all forms of bills of credit, the irreverent market had stored a big surprise for the cheerleaders of the monetary clauses. In a dramatic reversal, the functional money of the United States began to depart from the monetary clauses soon after the adoption of the Constitution. The money used in most market transactions was neither metallic in form nor federal in creation. It was paper money in the form of promissory notes that originated from privately-owned state banks, known as bank bills or banknotes. As notes of the state-chartered banks became the dominant medium of exchange, they gradually began to serve the functions of money, which the Constitution had reserved exclusively for gold and silver coin.

Constitutional money, despite its initial synergy with the eighteenth century financial markets, began to present problems, the most serious of which lay in maintaining comparative value of the two metals. The nature of metallic money was such that it was weighed as it was counted. A dollar, for example, was not only a unit of currency but also contained a definite weight of pure metal from which it was struck. Obviously, a dollar coined in gold could not weigh the same as a dollar coined in silver. Ideally, the two coins were to be so struck in their respective weights that they carried an equal value, thereby allowing a dollar in gold to be freely exchanged with a dollar in silver. This required a constant monitoring of market fluctuations between exchange values of the two metals.

Thus, constitutional bimetallism introduced a perpetual tension between the law and the market. The Constitution fixed no exchange ratio between gold and silver coins. But if the law was to establish an official exchange weight between gold and silver coins, the question remained whether the market in bullion would honor the legal ratio. If the mint ratio between gold and silver coins varied from the market exchange value at the time of coinage or later, the more expensive coin would disappear leaving behind the cheaper coin—a market mechanism

77. The weight of the Spanish dollars varied, though they had the same nominal value. But the standard weight of a commonly used Spanish silver coin was 371.25 grains. See LAUGHLIN, supra note 49, at 17, 21.

78. Recognizing the force of the market as the driving principle behind any legally-set ratio between gold and silver, Hamilton, the first Secretary of Treasury, attempted to find a ratio as close as possible to the existing markets in the United States. He proposed, and Congress legislated, a ratio of 1 to 15. Accordingly, the U.S. silver dollar weighed 416 grains, containing 371.25 grains of pure silver. The equivalent gold dollar weighed 27 grains and contained 24.75 grains of pure gold. See id. at 21.
popularly known as Gresham's law. It would sometimes be gold, sometimes silver, depending entirely on the variations in the relative value of the two metals, simply because gold or silver, like every other commodity, fluctuates in value on account of its production cost. This bimetallic relativism was not a national but an international problem, as gold and silver bullion and coins of all nations moved across borders.

The market duel between silver and gold as the preferred medium of exchange was more relevant in international transactions. Domestically, however, gold and silver were used primarily as bank reserves rather than a medium of exchange. Although gold was lighter than silver, its physical transportation from buyers to sellers and debtors to creditors was cumbersome. Therefore, to avoid an actual exchange of metal, which imposed a high transaction cost, the markets across the globe had been searching for a convenient and more efficient substitute. Banks, which remained unmentioned in the Constitution, stepped in to serve

79. Sir Thomas Gresham (1519-1579), the financial adviser of Queen Elizabeth I, coined the phrase "bad money drives good money out of circulation." John K. Galbraith, Money: Whence It Came, Where It Went 10 (1975). Gresham's law, however, applies only when there is a fixed rate of exchange between two monies. See Milton Friedman & Anna Jacobson Schwartz, A Monetary History of the United States 27 (1963).


81. See 10 Cong. Deb., app. 269-71 (Gates & Sexton eds., 1834). Although the Constitution empowers Congress to coin money, it poses no barrier to the establishment of a monetary system under which national and foreign coins struck in gold and silver may lawfully be used in domestic transactions. The circulation of foreign monies was no assault on the sovereignty of the United States. Generally, the economic prosperity of a nation was not dependent on national coins. This report is an excellent study exploring the status of gold and silver coins, foreign and national, in the United States since the adoption of the Constitution. See id. Nations had risen to the highest rank in commerce and general prosperity without adopting a monetary system based exclusively on their national coins. See id. at 269. Many commercial communities, including Holland, Hamburg, Genoa, and China had "more or less freely received the coins of well-known mints at their intrinsic value." Id. The United States followed the example of these free monetary communities and allowed foreign coins to participate in the development of its national economy. Although Congress regulated the value of these foreign coins, as the Constitution had authorized it to do, the markets remained free to develop their own standards for evaluating foreign coins. See id. at 271. Market standards paid more vigilant attention to pure grains of metal than to national icons engraved on the coins. Even in Great Britain, where only national coins were a legal tender, foreign gold was "current at a trivial discount." Id. at 270.

82. See id. Banks were interested in specie, and it was unimportant to them whether reserves in their vaults consisted of national or foreign coins or bullion. See id. at 271. In 1793, a year after the establishment of the national mint, Congress granted legal tender status to the coins of Great Britain, Portugal, France, Spain, and their corresponding American dominions. See Act of Feb. 9, 1793, ch. 5, 1 Stat. 300. When the coinage of the U.S. silver dollar was discontinued in 1805, foreign coins from Spain, Mexico, Central America, Brazil, Chile, and Peru drove the monetary system of the United States. See Act of June 25, 1834, ch. 71, 4 Stat. 681; Act of Mar. 3, 1843, ch. 69, 5 Stat. 607.
the needs of the market with a new form of money derived from the concept of the promissory note. 83

The framers of the Constitution were determined to outlaw bills of credit issued by state and federal governments, but they overlooked state-chartered bank money. There is no evidence that the framers envisioned banknotes as the principal source of money supply.84 The market was enamored with bank money because constitutional money was rigid in form and incapable of adapting to the ever changing needs of the market; conversely, banknotes offered this flexibility. The consequence of this new development was serious: If the monetary clauses were conceived to bring the quality and quantity of money under federal control, state-chartered banknotes posed a direct challenge to any a priori legal monopoly over the meaning of money.

A. The Charm of Banknotes

In their design and function, banknotes were promissory notes issued in a bearer form, promising to pay to the holder gold or silver on demand.85 In many ways, they were strikingly similar to the prohibited

83. The mushrooming of state banks was an astounding phenomenon in both fact and theory, for it challenged not only the constitutional mandate against bills of credit but also the authority of the federal government to institute a uniform standard of money across state lines. In fact, the growth of state banking was directly tied to the establishment of the United States Bank, which Hamilton believed was necessary to assure both the quality and the quantity of money. The establishment of the United States Bank prompted the states to counter this controversial federal move by chartering state banks. During the 20 year life of the first United States Bank (1791-1811), more than 80 banks were opened in the 13 states. When the charter of the United States Bank was not renewed in 1811, due in large part to the clout of state banking supporters, state banking became an unshakeable part of the monetary system. See generally Folwell, supra note 71.

84. See HURST, supra note 47, at 142. See generally ALBERT GALLATIN, THE WRITINGS OF ALBERT GALLATIN 579 (Henry Adams ed., 1879) [hereinafter GALLATIN'S WRITINGS]. "The introduction of the banking system met with strenuous opposition on various grounds; but it was not apprehended that banknotes . . . would degenerate into pure paper money . . . ." Id. at 236.

85. See J. MILNES HOLDEN, THE HISTORY OF NEGOTIABLE INSTRUMENTS IN ENGLISH LAW 70-73 (1955). Even though bank money mushroomed in the United States with few restraints, it originated in the customs of Lombard Street in London and matured as a legal concept in the English common law courts. See id. as noted before, gold and silver comprised the money of the world, including England. See id. Around 1645, goldsmiths at the Lombard Street issued receipts for gold and silver deposits that they received from their customers. See id. The receipt was a promise to repay the deposited coin or bullion on demand. See id. The goldsmiths' promise to pay a specified amount of money on demand would give birth to two distinct payment instruments, bank notes and checks. See id. The depositors began to use goldsmiths' notes as a payment mechanism in commercial transactions. See id. Sellers were willing to accept these notes as a valid payment, particularly when the goldsmith's reputation for honoring his
bills of credit. Nonetheless, there were critical differences between the two instruments. Bills of credit were issued by governments, often as a legal tender. In contrast, banknotes were issued by private banks to serve as optional money; the market was free to accept or reject banknotes, at face value or at a discount. The idea of banknotes was built on convenience and redemption, two important factors that facilitated commerce and charmed the market.\(^\text{86}\) Dealing in hard money was cumbersome and risky, especially in big transactions that required a heavy amount of gold or silver to be transported to a distant place. In such transactions, paper banknotes provided a safe and convenient substitute with a considerably low transaction cost.\(^\text{87}\) The most attractive attribute of the banknote, however, was its promised redemption—a written undertaking to pay the specified money \textit{on demand}, which meant that the bank, the issuer of the note, would pay real money, gold or silver, when the note was presented. Albert Gallatin, the Secretary of Treasury, explained the redemption principle in the following words: "The substitution of a paper for a gold or silver currency is therefore admissible only on the express condition that it shall always be equal in value to the legal coin of which it is the representative . . . ."\(^\text{88}\) Any deviation from this principle, he further stated, "is a violation of existing contracts . . . and impairs private and public credit."\(^\text{89}\) This assurance of redemption further convinced issuance had been established in the market. \textit{See id.} Thus, the concept of money-substitute was born. \textit{See id.} The transition from goldsmith to bank was relatively easy. \textit{See id.} It was a shift in size and organization of the operation rather than concept.

\(^{86}\) Another and perhaps more substantial benefit of "the substitution of paper to gold and silver . . . brings into activity an additional circulating capital equal to the difference between the amount of paper and that of the reserve in specie necessary to sustain the par value of that paper." \textit{GALLATIN'S WRITINGS, supra} note 84, at 337.

\(^{87}\) In \textit{Ontario Bank v. Lightbody}, 13 Wend. 101, 110-12 (N.Y. 1834), the New York Court of Appeals, court articulated the market significance of banknotes in the following words:

\begin{quote}
It is admitted that bank notes, as the circulating medium of the country, have acquired the denomination of money, from their convenience as a substitute for gold and silver, and their utility in promoting the objects of trade, and in exchanging the products of industry; but after a bank has failed, its notes are deprived of those characteristics of money which entitled them to that appellation by the custom of trade, while they continued at a value equivalent with specie, or nearly so. Their convertibility into specie being lost, and their power of circulation having departed, not one of the ingredients of money remains, and they can be legally defined only as unpaid promissory notes. . . .
\end{quote}

\textit{Id.} at 110-12.

\(^{88}\) \textit{GALLATIN'S WRITINGS, supra} note 84, at 379. Albert Gallatin, the Secretary of Treasury (1801-14) under Presidents Jefferson and Madison, was a principal figure in the economic development of the United States.

\(^{89}\) \textit{Id.}
merchants that notes, rather than specie, ought to be the medium of payment in commercial transactions.90

Thus, banknotes originated as non-governmental promissory notes. Gradually, however, they acquired the attributes of paper money. Following the example of foreign banks, state banks with large specie holdings began to issue banknotes in a more organized manner. Often, these paper notes were printed and issued in different denominations. Unlike coins which were made in the unit of currency and its fractions, banknotes were issued in higher denominations of ten, twenty, or one hundred times the unit of currency, in this case, the dollar. The notes of creditworthy banks began to circulate from person to person and even from town to town. When merchants concluded that the notes of a certain bank could be converted into real money on demand, no one was interested in their redemption.91 As their circulation became more common, banknotes were no longer considered specific property of the person to whom they were issued. Both in the market and the law, banknotes became "money with no ear-mark"92 and could not be recovered after they had passed in currency.

The proliferation of banknotes in the United States was consistent with the common law of negotiable instruments as it developed in England. In 1758, three decades before the adoption of the United States Constitution, Lord Mansfield, a celebrated common law judge in England whose reputation was contemporaneously well-established in

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90. See J.S. Waterman, The Promissory Note as a Substitute for Money, 14 MINN. L. REV. 313, 313-41 (1930). "Paper money, in order to possess the economic quality of general acceptability, should, it seems from history, be readily convertible on demand into a definite amount of metallic media, if such redemption is desired by the holder." Id. at 315.

91. See Allen Ripley Foote, The Currency Problem, 11 BANKING L.J. 257, 260 (1894). If it is perfectly certain that a man can pay his note at maturity, he can renew it as many times as he likes, but let a doubt exist as to his ability to pay, and payment is demanded of him at the first opportunity, and a proposal to renew is regarded as a confession of bankruptcy.

92. For a discussion regarding the origin of the term "money has no ear-mark," see 2 FREDRICK POLLOCK & FREDERIC WILLIAM MAITLAND, THE HISTORY OF ENGLISH LAW 151 (2d ed. 1898). In the 18th century, the United States suffered from persistent legal confusion regarding bank liability for deposits of specie. The depositors viewed the bank as a safe warehouse for keeping gold and silver coins and wished to draw out the same coins they had deposited. Even Alexander Hamilton, the Secretary of Treasury, believed that the specie deposited in a bank was earmarked property of the customer. The banks resisted this view of liability by adhering to the concept of bailment. They preferred the counter legal doctrine under which depositors were the bank's creditors. This view, which finally prevailed, changed the notion of money from earmarked property to the amount of money deposited. In Thompson v. Riggs, 72 U.S. 663 (1866), the United States Supreme Court upheld the view that, when money is deposited in the bank, the title to the money passes to the bank and the latter becomes the debtor of the customer in that amount. See id. at 680.
American colonial legal circles, authored the opinion in *Miller v. Race*, a case that legally entrenched the free circulation of banknotes. In an action of trover of a banknote, Lord Mansfield wrote: "[Bank notes] . . . are treated as money, as cash, in the ordinary course and transaction of business, by the general consent of mankind. . . . They are so much money as guineas themselves are . . . ." Lord Mansfield used spirited words, perhaps inflated words, to underscore the commercial significance of banknotes. Even in his time, banknotes were not money but rather promissory notes, and their market acceptability continued to depend on whether they would be redeemed into real money. However, even as promissory notes, banknotes proved an important creation, functionally replacing the circulation of heavy metal. The concept of redemption of banknotes on demand into a specific weight of grains of pure metal offered a preferred alternative to the worn-out, often clipped, and sometimes counterfeit coins in actual circulation.

**B. Constitutionality of Banknotes**

The constitutional text that no state shall issue bills of credit was short and clear. Its meaning, however, was uncertain and became more so.

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94. Id.
95. The Bank of England, a privately-owned institution, did not issue notes until it was incorporated by the government in 1694. Waterman, supra note 90, at 321. However, in 1718, the bank was transformed into a "Royal Bank" and its notes were made legal tender. The notes of the Bank of England, without being legal tender, gained a high reputation during the same period. See id. at 323-24.
96. Even the case law began to state the significance of paper money. See, e.g., Ware v. Street 39 Tenn. (2 Head) 609 (Tenn. Apr. Term 1839).

The supposed commercial interests of our country and the general convenience of our people, have produced a course of legislation by which the bank paper has become the circulating medium and the standard of value, instead of specie. True, it has not been made a legal tender, and cannot be without a change of the constitution. But by almost universal consent it has become the medium of exchange and the representative of property it has taken the place of precious metals, and is regarded as money. This, however, is by consent and not by law. No man is bound to receive it in payment of debts, or for property.

*Id.* at 612. In *F. and M. Bank v. Joseph White*, 2 Sneed (Tenn. 1855) 482, 484:

Bank notes differ essentially from promissory notes and other negotiable securities for money. They are not, properly speaking, evidences of debts or securities for money, but are treated as money, in the ordinary course and transaction of business, by the general consent of the community. They are transferable by delivery and issued and put in circulation with the avowed intention, that they shall pass from hand to hand and circulate as money . . . .

*Id.* at 483-84. See also *Gwin v. Breedlove*, 43 U.S. (2 How.) 29, 38 (1844). "[I]f the debtor pays bank-notes, which are received by the creditor in discharge of the contract, the payment is just as valid as if gold or silver had been paid." *Id.* This case, however, was decided after the constitutionality of bank notes had been upheld. See id. Later, the Supreme Court recounted the pivotal role of banknotes: "As bills of credit were thus entirely abolished, the paper money of the State banks was the only currency or circulating medium to which this prohibition could have had any application, and was the only currency, except gold or silver, left to the States." *Veazie Bank v. Fenno*, 75 U.S. (8 Wall.) 533, 552 (1869).
when state-chartered banking grew and began to dominate the money supply. To fully understand the victory of bank money, one must look beyond the tangle of federalism, which, on the surface, dominated the political and constitutional debate over the issue. Bank money was the creation of the law merchant and the needs of the market. Its entrenchment in the legal system was the reaffirmation of a simple monetary tradition: the market creates, modifies, and recreates the concepts of money. The law simply recognizes the changes, often ex post facto.

The common law acceptance of banknotes was more than a hundred years old when their constitutionality was challenged in 1837. In 1820, Kentucky established a bank “in the name and behalf of the Commonwealth of Kentucky.” The bank, the exclusive property of the Commonwealth, was authorized to issue the common form of banknotes in which the bank “promised to pay the bearer, on demand, the sum stated” on the face of the note. John Briscoe obtained a loan from the bank in the form of notes. The bank instituted a suit when Briscoe refused to pay back the loan. Briscoe contended that the loan was void because it was given in banknotes, which were bills of credit issued by the state of Kentucky, an act prohibited by the Constitution. In a hotly-contested decision, the United States Supreme Court upheld the constitutionality of the bank and the banknotes.

The irony of the Briscoe case lay in its timing. It was first heard by the Supreme Court in 1834, barely four years after Craig v. Missouri, a case in which Chief Justice John Marshall stated in lucid terms that the “certificates” issued by the State of Missouri were unconstitutional, emphasizing that the Constitution could not be evaded by giving “a new name to an old thing.” Speaking in a sweeping language, the Chief Justice explained that “[t]o ‘emit bills of credit,’ conveys to the mind the idea of issuing paper intended to circulate through the community for its ordinary purposes, as money, which paper is redeemable at a future day.” He further explained that “[i]f the prohibition means any thing, if the words are not empty sounds, it must comprehend the emission of any paper medium by a state government, for the purposes of common circulation.” It is unclear whether the Chief Justice included banknotes issued by private banks in the definition of prohibited bills of

97. The notes of the Bank of England were made legal tender in 1833. See Waterman, supra note 90, at 317.
99. See id. at 329 (Story, dissenting).
100. 29 U.S. (4 Pet.) 410, 433 (1830).
101. Id. at 432.
102. Id.
credit. Given Lord Mansfield's seminal holding in *Miller v. Race*, decided about seventy-five years before *Craig*, it is highly unlikely that Justice Marshall proposed to ban the notes of all banks. If he did, the opinion posed a direct challenge to the very existence of state-chartered banks. The *Briscoe* case was finally heard in 1837, after the death of John Marshall in 1835.103 Several new members of the Court were appointed by President Andrew Jackson, a determined foe of the central bank and an ally of state-chartered banking.

The *Briscoe* Court repudiated the opinion of John Marshall through the art of distinguishing rather than by the blow of overruling. Justice McLean, a former member of President Jackson's cabinet, wrote and read the opinion of the Court. By no means a gem of constitutional rhetoric, the opinion nonetheless made a spirited defense of banknotes. It derived its most powerful arguments from the context of the market rather than from the text of the Constitution. If paper money issued by state-chartered banks was totally prohibited by the Constitution, such a "startling" doctrine would administer "a fatal blow against the state banks; which have a capital of near four hundred millions of dollars, and which supply almost the entire circulating medium of the country."104 Instead of examining the constitutionality of state-owned banknotes, the Court lumped together the circulation of all banks, private and state-owned. Though flawed in its precision, the argument brought home the point: a payment instrument that had deeply penetrated the market could not be declared unconstitutional. Regarding a state's power to incorporate banks, the Court relied upon another *fait accompli*. It pointed out that states had exercised this important power "for half a century; and this, almost without question . . . ."105 Again, the argument was built on fact rather than law. These reality-based arguments were made with a touch of stinging sarcasm as the "questionable" central bank had failed to survive, only a year prior to the decision.106

Justice Story wrote a studied dissent that, in a way, more vividly affirmed the constitutionality of banknotes. With a solid understanding

103. The case had to be postponed because two of the seven judges were physically unable to attend, the other five were divided three to two. At the time, the Court was composed of only seven judges.
105. Id. at 318.
106. In his message to Congress, President Andrew Jackson said: "Both the constitutionality and the expediency of the law creating this Bank are well questioned by a large portion of our fellow citizens; and it must be admitted by all that it has failed in the great end of establishing a uniform and sound currency." HAMMOND, supra note 76, at 374. The Second United States Bank ceased to exist when its charter expired in February 1836. The *Briscoe* case was decided in January 1837. See *Briscoe*, 36 U.S. at 257.
of the law of negotiable instruments, Justice Story examined the heart of the matter. Analyzing the bill of credit as found in the British laws, and citing Lord Mansfield’s decision in *Miller v. Race*, Justice Story concluded that there was “no mystery” about bills of credit, as they were “negotiable paper, intended to pass as currency, or as money, by delivery or indorsement.” Bills of credit “are not ... in a legal or exact sense, money; but, for common purposes, they possess the attributes, and perform the functions of money.” In light of this definition, Justice Story then declared: “The constitution does not prohibit the emission of all bills of credit, but only the emission of bills of credit by a state: and when I say, by a state, I mean by or in behalf of a state, in whatever form issued.” Justice Story was not opposed to banknotes in general. His dissent criticized a limited type of banknotes, the ones issued by a wholly state-owned bank. Thus, the Supreme Court, Justice Story included, upheld state-chartered private banking and its issuance of banknotes. Consequently, state banks flourished, and banknotes became the functional money of the United States, a development that the framers of the Constitution never anticipated.

After *Briscoe*, the monetary clauses acquired a new meaning. The Constitution does not mandate that all transactions be conducted only with gold and silver coin. Even paper money, as an optional medium of exchange, is constitutional provided it is redeemable in constitutional coin. The twin attributes of a money-substitute, redemption and optionality, would later become the constitutional recipe to prepare new forms of money. For example, although banknotes were the functional

107. Justice Joseph Story, the youngest man ever appointed to the Supreme Court, is one of the greatest scholars of American law. Justice Story authored a book that was a great contribution to the law of negotiable instruments. See generally COMMENTARIES ON THE LAW OF BIllS OF EXCHANGE (4th ed. 1860). Justice Story’s understanding of bills of credit was superior, and his articulation of the issues in the *Briscoe* case was illuminating. See *Briscoe*, 36 U.S. at 328 (Story, J. dissenting). Yet, by this time, the concept of money had already moved away from a plain-meaning textual view of monetary clauses of the Constitution.

108. Id. at 330 (Story, J., dissenting).
109. Id. (Story, J., dissenting).
110. Id. at 348 (Story, J., dissenting).
111. See id. at 349 (Story, J. dissenting). Justice Story even conceded that a state could be part owner of the bank. See id. at 349 (Story, J., dissenting).
112. In May 1813, Secretary Albert Gallatin left the Department of Treasury. See HENRY ADAMS, LIFE OF ALBERT GALLATIN 653 (1879). In 1836, “the bank-paper mania has extended itself so widely that I despair of its being corrected otherwise than by a catastrophe.” Id.
113. A later commentator summed up the significance of state banks in the following words:

There is no sound economic reason why there should not be in every village, town and county in the country, one or more banks of issue, the notes of which shall always be good at par in gold values, and in sufficient supply promptly to effect all legitimate exchanges of the products of labor desired by the people . . . .

Footes, supra note 91, at 258-59.
money of the market, the idea of redemption maintained intact the constitutional paradigm that nothing but gold and silver coin shall be the real money of the United States. The additional factor that banknotes issued by state-chartered banks were merely optional money that creditors may lawfully refuse did not assault a key provision of the Constitution, namely that no state is allowed to make anything but gold and silver coins a tender in payments of debts. Though the market successfully created a constitutional money-substitute in the form of banknotes, it remained to be seen whether the federal government could do the same.

IV. TENDER PROMISES OF WAR AND PEACE

If the market paved the way for state banks to successfully use the concept of the promissory note to launch banknotes, the nation's wars forced the cash-strapped federal government to invent its own paper money. The creation of federal notes initially was based on the same constitutional recipe as banknotes: redemption and optionality. The route to this simple project, however, was strewn with political and constitutional barriers. Furthermore, the market was unlikely to receive federal notes with enthusiasm, particularly if the government lacked the resources to redeem them into precious metal. A constitutional crisis was bound to occur if the federal government decided to make its paper notes a legal tender.

The silence of the Constitution on federal banking became a formidable barrier to the retention of a central bank, which, during its intermittent existence, served as a perfect vehicle to create federal banknotes. Though the constitutional battle over the central bank was fought in terms of federalism, the underlying conflict concerned the role and meaning of money. In December 1790, when the Constitution entered its second year, Alexander Hamilton, the first Secretary of

114. The success of banknotes carries a simple truth that the promissory note, a debt instrument, was on all counts the genetic ancestor of paper money. In common law, negotiable promissory notes emerged in the early 17th century, though non-negotiable debt documents are of great antiquity. For the history of development of promissory notes, see generally HOLDEN, supra note 85.

115. The framers of the Constitution were aware of banking, though only three banks operated in the United States when the Constitution was adopted. The successful operation of the Bank of England was also a guiding influence. To some framers, the usefulness of a central bank was obvious. Others were skeptical about the whole enterprise of banking. Some wished to keep banking within the domain of state sovereignty. Some thought the "subject was too touchy." HAMMOND, supra note 76, at 105. These issues aside, the framers had no clear vision that banks, which were not addressed in the Constitution, would become the ultimate custodians and creators of paper money. See id. at 105-06.

116. Commercial and monied classes supported the idea of a central bank, while agrarian classes distrusted banking in general and central banking in particular.
Treasury, submitted a plan to incorporate a central bank. To Hamilton, a man most familiar with the success of the Bank of England, the proposed central bank was an indispensable institution for the new federal government as a reliable source of loans to the U.S. Treasury.117 The opposition was fierce and political in nature, waged by such icons of American history as James Madison and Thomas Jefferson.118

In periods of monetary stress, however, a cash-strapped federal government was more likely to embrace pragmatism, not dysfunctional idealism. During the periods when the federal government lacked a central bank and money, Congress converted its power to borrow money into a power to create paper money. The monetization of this new debt instrument is a story of clever financing by mimicking banknotes. The story is both political and technical in nature. Politically, the shortage of specie in time of war gave Congress a stable footing to turn debt into paper currency. The fetching part of the story, however, belongs to technical maneuvering of the promissory note, thereby turning a debt instrument into paper currency. To understand this technical cunning, a brief overview of Congress’s constitutional power to borrow is essential.

The Constitution grants Congress the power to borrow money on the credit of the United States.119 This power may be exercised by using diverse legal techniques. In the early years of the Republic, Congress borrowed money by means of ordinary contracts. Congress often authorized the Department of Treasury120 to issue “evidences of indebtedness.” Nevertheless, regardless of the legal device used,

117. See CLINTON ROSSITER, ALEXANDER HAMILTON AND THE CONSTITUTION 5, 9 (1964). Alexander Hamilton met fierce opposition from agrarians who mistrusted banking. See id. at 9. Born in the West Indies, Hamilton was treated as an “exotic” and an “alien” who said: “Every day proves to me more and more that this American world was not made for me.” Id. at 14. Despite this hostility, Hamilton was determined to teach agrarians that their future was bound up in ships, banks, canals, and factories. See id.

118. The First Central Bank was established in 1791 for a period of 20 years. Due to fierce opposition, its charter was not renewed in 1811. There was no central bank between 1811 and 1816, a period during which the British declared war on the United States. The Second Central Bank was chartered in 1816 for 20 years. Soon after its establishment, its constitutionality was challenged. The Supreme Court upheld the power of Congress to establish a central bank in a seminal case that, for the first time, translated silence of the Constitution into power of the central government. See McCulloch v. Maryland, 17 U.S. (4 Wheat.) 316 (1819). Despite this constitutional victory, the Bank was defeated politically, and its charter was not renewed in 1836. Like in the War of 1812, the federal government had no central bank during the Civil War. As a result, there was no institution to offer loans when the federal government was financially most vulnerable.

119. See U.S. CONST. art I, § 8, cl. 2.

120. The Department of Treasury was established in 1789 to prepare plans for the improvement and management of the revenue, to execute services relative to the sale of the lands belonging to the United States, and to perform all such services relative to the finances. See Act of Sept. 2, 1789, ch. 12, §§ 1 & 2, 1 Stat. 609.
borrowing money had certain fixed attributes. A traditional loan generally was obtained for a fixed period of time. All lenders charged interest that could be paid either in installments, as it accrued during the existence of the loan, or paid as a lump sum amount at maturity. Likewise, the principal was paid either in periodic installments or in a lump sum when the loan expired. 121 Most lenders demanded security, a pledge of valuable property to protect the loan against default. Though most loan contracts were assignable, they were not freely negotiable. Thus, a traditional debt instrument incorporated the following essential ingredients: an amount of principal, an interest rate, a description of the collateral, and a maturity period. 122

Invoking its constitutional power to borrow money, Congress first sought loans through traditional debt instruments. In war emergencies, however, it created a new debt instrument in the image of a promissory note, a flexible payment instrument that may or may not contain all the attributes of a traditional loan. A promissory note typically is drawn as

121. In contrast to the traditional loan, a revolving loan is granted for a pre-determined amount against which the borrower is required to make a periodic minimum payment that includes part principal and part interest.

122. The first major domestic loan, which originated in 1790, had all the traditional attributes. The debt was embodied in the form of certificates issued "consistently with good faith and the rights of creditors; which can only be done by a voluntary loan on their part." Act of Aug. 4, 1790, 1 Stat. 138. § 2. The certificates paid interest on the amount of money borrowed. A period was fixed to pay the interest and the principal amount. To assure the payment of interest and principal amount, Congress pledged the faith of the United States. Congress also pledged monies secured under the revenue laws. To make the monetary pledge more credible, Congress assured creditors that a separate and distinct account would be kept so that monies set aside for the payment of the loan might not be used for any other purpose. As if the security was still insufficient, Congress further promised that the proceeds of the sale of lands in the western territory would be appropriated toward discharging the debt. Moreover, the certificates were not negotiable. Each certificate was registered in the name of the subscriber. The subscriber could assign his certificates. For a proper assignment, however, the subscriber was obligated to request a transfer in a register maintained by an appointed state commissioner. See id.

Even foreign loans were obtained with all the attributes of a traditional debt. In 1803, President Thomas Jefferson purchased the Louisiana territory from France. To finance this transaction, Congress authorized the Secretary of Treasury to issue debt certificates in favor of the French Republic for the sum of $11,250,000, the amount for which the territory was bought. The certificates paid an interest of 6% per year starting from the day of the possession of the territory, in conformity with the Treaty of April 1803. To secure the loan, the faith of the United States was pledged for the payment of both interest and principal. The period for the reimbursement of the principal was fixed in the 1803 Treaty, with a prepayment provision. Accordingly, the Secretary of Treasury was authorized, with the approval of the President, to shorten the period fixed for the reimbursement of the principal. See Act of Oct. 31, 1803, ch. 1 & 2, 2 Stat. 245. The acquisition of the Louisiana Territory, for about $15 million, doubled the size of the United States. For many, this purchase was an act beyond the Constitution, as nothing in the Constitution gave the federal government the power to incorporate foreign territory into the Union. On the supposed unconstitutionality of the purchase, President Jefferson said: "[T]he less we say about the constitutional principles . . . the better . . . and that what is necessary for surmounting them must be done sub silentio." 1 Bradford Perkins, The Cambridge History of American Foreign Relations 117 (1993).
an order paper that passes from person to person by indorsement and delivery. But nothing in the law prevents it from being a bearer instrument that passes by mere delivery. Most often, a promissory note is an interest-bearing instrument, as the lender wants to make money by charging interest on the principal amount for the period it is lent. However, the law does not require the imposition of interest on a promissory note. Most often, a promissory note is an evidence of debt by which the borrower defers payment at a future date. Again, the law does not require that the money promised on a note be paid in the future. A note can be a simple promise to pay a stated amount of money on demand. Each taker of the note would be willing to sell goods and services if payment on the note is assured. But no person is under any legal obligation to accept a promissory note to part with goods and services. The marketability of each promissory note depends on the creditworthiness of its maker.

Here it is important to bear in mind the critical distinctions between a promissory note and paper money. Unlike a promissory note, which may or may not be in bearer form, paper money is always in bearer form and passes from person to person by mere delivery. Likewise, while a promissory note may offer interest on its principal, paper money is not an interest-bearing instrument. Rather, it is exchanged at face value. Two important additional factors distinguish promissory notes from paper money. First, paper money in itself is money, whereas a promissory note is one step removed from money. The second most important distinction relates to the issue of legal tender. Creditors may be lawfully forced to discharge debt upon the presentation of paper money. No creditor, however, must accept a promissory note. The debt will stand if the creditor refuses to accept even the most creditworthy promissory note.

Bear in mind that the transformation of a federal debt instrument into paper money did not occur overnight or in a single legislative leap. Although the first step towards paper money was taken during the War of 1812, Congress took more than fifty years to let its promissory notes evolve into paper money. Many judges and legal scholars did not accept this evolution without intellectual resentment. Many others accepted the fait accompli with resignation or blissful ignorance. Moreover, some still argue for restoration of the constitutional coin of silver and gold.
A. Paper Defense of 1812

The War of 1812, the first serious post-constitutional war, came at a difficult time.123 The American embargo of 1807 had choked the foreign trade of the United States. In 1811, the first Central Bank of the United States, a bank that had acted as fiscal agent of the Treasury and had effectively supported the federal government's borrowing needs, ceased to exist.124 The war threw the economy into confusion, bred treason, and nearly tore the Union apart.125 With the Central Bank gone and the war raging, the federal government, with little specie in the treasury, faced the task of raising money without issuing prohibited bills of credit. This formidable challenge called for legal creativity, if not outright constitutional nullification. By 1812, promissory notes were a secure fixture of private banking, law merchant, and financial markets. However, to introduce monetized paper into public financing was tantamount to blurring the distinction between prohibited bills of credit and constitutionally permissible debt instruments.126

To no one's surprise, Congress decided to issue paper notes, invoking its power to borrow money. Following the suggestion of Albert Gallatin, the Secretary of Treasury,127 Congress authorized the Secretary "to borrow, from time to time, not under par, such sums as the President may think expedient, on the credit of such notes."128 These paper notes were called treasury notes—a debt instrument which is still systematically issued to borrow funds at home and abroad. The notes had many of the attributes of a traditional debt instrument. For

124. In 1798, Congress authorized the President to borrow from the United States Bank a sum of $2 million at a maximum of 6% interest. Congress pledged the faith of the United States, and the anticipated direct tax to be collected within the United States was offered as security. This law, however, provided that the "principal shall be reimbursed at the pleasure of the United States." Act of July 16, 1798, ch. 84, § 2, 1 Stat. 609.
125. The embargo spawned massive resistance within the Union. Violations and evasions of the embargo were rampant. On June 18, 1812, President James Madison signed the war bill. Thus "with a tiny navy, an unrecruited army, no financial plan, the United States set off to war." PERKINS, supra note 122, at 137.
126. The difference between bills of credit and debt instruments is elusive. If notes were convertible into real money and bills were not, the difference was real. But if both were convertible into gold and silver, time and interest factors distinguished the two forms of instruments: bills of credit did not promise any payment of interest, notes did. Moreover, bills were redeemable on demand, whereas notes could be converted into real money only after the proscribed period of time had passed. Though notes gave the government time to accumulate real money, they were more expensive than bills of credit because the government had to pay interest on them.
127. See STUDENSKI & KROOSS, supra note 83, at 75-77.
128. Act of June 30, 1812, ch. 111, § 4, 2 Stat. 766, 767. This Act was passed authorizing the issuance of Treasury Notes. See id. The President was authorized to raise the debt up to $5 million.
example, they were interest-bearing instruments. The principal was to be reimbursed within one year of the date of issue. To offer security for the satisfaction of these notes, Congress pledged a portion of the existing redemption fund for the payment of interest and principal. The notes were not legal tender for the discharge of private debts. However, they were to be "received in payment of all duties and taxes laid by the authority of the United States, and of all public lands sold by the said authority." Public creditors and other persons were free to receive these paper notes in payment of supplies or debt owed by the United States.

The important feature that distinguished the 1812 treasury notes from traditional debt certificates was their negotiability. Unlike debt certificates, treasury notes required no registration with the Treasury or state commissioners. Instead, the notes were made negotiable by endorsement; that is, the notes were transferable by delivery and signature of the person named on the face of the note. Thus, the 1812 notes were cast in the image of a promissory instrument that passes from one named person to another. Such notes may not circulate as freely as paper money, yet they are closer to paper money than traditional debt certificates.

Three years later, in 1815, the form of treasury notes further changed bringing them even closer to paper money. Most of the attributes of a traditional debt instrument were dropped. Unlike the 1812 paper notes, which were interest-bearing, the 1815 paper notes bore no interest. The cumbersome technical requirement that 1812 notes be transferred with indorsement was also dropped, and the new notes were issued in a bearer form so that they could circulate by mere delivery. To further make the 1815 notes in the image of paper money and to assure their circulation in ordinary consumer transactions, notes were issued in smaller denominations. Furthermore, the 1815 notes contained no maturity period for their redemption. In fact, they were not redeemable into constitutional coin. However, the idea of

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129. See id. § 2. The interest was 5 7/8% per year. See id.
130. See id. § 8.
131. Id. § 6.
132. See id. § 5.
133. The Secretary of Treasury was authorized to issue treasury notes up to $25 million.
134. The Secretary of Treasury was given the option to make notes of higher denomination ($100 and above) bearing an interest of 5 7/8% per year.
135. See Act of Feb. 24, 1815, ch. 56, 3 Stat. 213 (1815). Notes less than $100 were to be payable to bearer, transferable by delivery alone, bearing no interest. Notes of $100 or higher could be issued at the discretion of the Secretary, either as order papers bearing interest or as bearer papers bearing no interest. See id. § 3.
redemption was not totally rejected, as the holder of the notes could convert them into interest-bearing certificates. The faith of the United States was pledged to establish sufficient funds for the ultimate reimbursement of these certificates into specie.\footnote{See id. \S 4.}

Thus, due to their circuitous, though uncertain, redemption into specie, the 1815 paper notes evolved beyond the concept of the promissory note, which promises direct and certain redemption. A fundamental distinction between the 1815 treasury notes and what would have been a new official currency was nonetheless retained. The 1815 paper notes were not legal tender in private debts, though they could be tendered in payment of services, supplies, or debts of the United States to such persons who were willing to accept them in payment.\footnote{See id. \S 8.} As such, distinguishing the 1815 paper notes from prohibited bills of credit effectively was reduced to a matter of opinion.

Perhaps because the nation was in danger, no one questioned the constitutionality of the 1815 paper notes, even though Justice Marshall, who would later declare the Missouri certificates to be unconstitutional, was sitting on the Supreme Court.\footnote{Craig v. Missouri, 29 U.S. (4 Pet.) 410, 431 (1830).} There was yet another historical conjunction. The issuance of 1815 paper notes took place under the watchful eye of President James Madison, who indicated in the Constitutional Convention that non-tender bills of credit constituted a permissible form of paper money that Congress could issue in emergencies.\footnote{See supra note 62.}

Even if the 1815 paper notes amounted to prohibited bills of credit, they ceased to exist after the war ended, and a central bank was established.\footnote{Act of Apr. 10, 1816, ch. 44, 3 Stat. 266.} Congress reverted back to borrowing money from the central bank, and, therefore, no treasury notes were issued.\footnote{In 1837, after the charter of the Bank of the United States was not renewed, Congress reverted to issuing treasury notes, but this time many of the attributes of a traditional loan were preserved in the issuance of these notes. Accordingly, Congress authorized the President to cause treasury notes to be issued up to a sum of $10 million and of denominations of not less than $50. The notes were redeemable after one year. The Secretary of the Treasury was authorized to determine the rate of interest to be paid at the time of issuance of the notes. The faith of the United States and some monies were pledged for the assurance of the creditors. The notes could be transferred by delivery and indorsement. Until 1861, every issuance of treasury notes followed traditional terms.} In 1817, Congress passed a law to repeal the authority of the Secretary of Treasury to reissue treasury notes. As if their continued circulation was constitutionally dubious, the 1815 notes received in payment and
offered for reimbursement were destroyed or canceled.\textsuperscript{142} Thus, Congress, mostly on its own initiative, restored constitutional money. However, in view of the success of the 1815 notes, the Madisonian principle that Congress could issue paper money in emergencies acquired a new respectability. Whether the Madisonian principle would also muster constitutional legitimacy was tested decades later when Congress reissued paper money during the Civil War.

\textbf{B. Civil War Greenbacks}

The Civil War not only ended slavery, but it also, by necessity, brought the end of constitutional money. Unquestionably, the Civil War was an emergency without parallel in the history of the new Republic. It threatened the overthrow of the government and the destruction of the Constitution itself. It demanded the equipment and support of large armies and navies, and the employment of money beyond the capacity of all ordinary sources of supply.\ldots \textquoteleft \textquoteleft \textquoteleft \textquoteleft The public treasury was empty, and the credit of the government \ldots \textquoteleft \textquoteleft had become nearly exhausted.\ldots Taxation was inadequate.\ldots \textquoteleft \textquoteleft The necessity was immediate and pressing. The army was unpaid.\textsuperscript{143}

Therefore, in 1862, Congress passed a bill, signed into law by President Abraham Lincoln, that changed the nature of federal debt.\textsuperscript{144} The law authorized the Secretary of Treasury to issue, on the credit of the United States, 150 million paper dollars, officially known as "United States notes." As these paper notes were printed with green ink, the public began to call them greenbacks.

By issuing greenbacks, Congress dropped the key concepts of redemption and optionality and leaped well beyond the 1815 treasury notes, which offered some form of redemption and were not legal tender. Technically, greenbacks were bearer instruments transferable by mere delivery, as they carried no interest.\textsuperscript{145} Moreover, because greenbacks were not redeemable into gold or silver, no period was stated for their redemption. They were "receivable in payment of all taxes, internal duties, excises, debts, and demands of every kind due to the United States."\textsuperscript{146} They were also made "legal tender in payment of all

\textsuperscript{142} See Act of Mar. 3, 1817, ch. 85, 3 Stat. 377, 378.

\textsuperscript{143} Knox v. Lee, 79 U.S. 457, 458 (1870).

\textsuperscript{144} See Act of Feb. 25, 1862, ch. 33, § 1, 12 Stat. 345.

\textsuperscript{145} See id. § 1.

\textsuperscript{146} Id.
debts, public and private, within the United States, except duties on imports and interest [upon bonds and notes].  Thus, greenbacks were no longer promissory notes redeemable into constitutional money. Rather, they were designed to circulate as the new official currency.

Though greenbacks were not redeemable in constitutional coin, Congress was still unwilling to discard the entire concept of redemption, a key concept that preserved the spirit, if not letter, of the monetary clauses. Giving an unusual meaning to the concept of redemption, Congress introduced the concept of "investment" of greenbacks, thereby presenting holders with two investment choices. For long-term investment, holders could convert greenbacks into bonds, which were "redeemable at the pleasure of the United States after five years, and payable twenty years from the date thereof." For short-term investment, holders could convert greenbacks into certificates of deposit (CDs). The principal amount of CDs could be redeemed only in greenbacks, not coin. With respect to bonds, the government retained several options. The Treasury could buy back these bonds at any time, at their market value, for coin of the United States. This option could be exercised beneficially if the bonds had significantly depreciated. The authority to buy back bonds, however, could be exercised even by tendering U.S. notes, a legal tender in all debts, private and public.

The Act of 1862 introduced a cycle of monetized paper. The greenbacks could be converted into interest-bearing investment paper, that is, government bonds and certificates. The bonds and certificates were redeemable, but only in greenbacks. In this cycle of conversion, paper for paper, the constitutional coin disappeared.

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147. Id.
148. See id.
149. Id. The distinction between "redeemable" and "payable" is unclear, unless it meant that the bonds would be converted into gold and silver coin but the metal would not be paid until the expiration of 20 years.
150. See id. § 2. The bonds paid 6% interest in coin every six months. See id. The certificates of deposit (CDs) paid 5% interest, provided notes were deposited for at least 30 days. See id. § 4.
151. See id. § 2.
152. See id.
153. Congressional debates on the constitutionality of the Act of 1862 were conducted in a state of panic, frustration, and passion, a set of sentiments not good for cold reasoning. Nonetheless, the arguments for and against the bill were made with sophistication. See CONG. GLOBE, 37th Cong., 2d Sess. 765 (1862). Some proponents of the bill invoked the argument of emergency and necessity caused by the civil war, a justification for the proposed law. See id. at 692. Some were unsure whether revenues could be raised in a timely fashion through taxation. See id. at 683. Some invoked the inherent power of Congress to issue legal tender notes. See id. at 637. The opponents emphasized the dangers of paper money, namely its massive depreciation, inflation, and other evils that follow. See id. 765. One representative called the bill a "dangerous departure" and the beginning of a "new financial system in the United States." Id at 663.
The most troubling characteristic of this "new official money" was neither the substitution of paper for coin nor the manipulation of the idea of redemption. The mischief lay in making greenbacks legal tender, thereby subordinating the Constitution to ordinary law. The opponents of paper money had three arguments against the greenbacks. First, greenbacks betrayed the principle of fairness embodied in the concept of a traditional loan under which debt instruments must conform "consistently with good faith and the rights of creditors; which can only be done by a voluntary loan on their part." Second, greenbacks were unconstitutional because the text of the monetary clauses must be strictly construed. Third, the framers of the Constitution left no authority for Congress to make federal debt instruments a legal tender, which ultimately forced creditors to accept much depreciated greenbacks and discharge debts they contracted to be paid in specie. This new state of affairs was challenged before the Supreme Court in the Legal Tender Cases.

**C. Constitutionality of Greenbacks**

The legal tender cases challenged the constitutionality of greenbacks on various grounds. The first two cases challenged the constitutionality of greenbacks issued during the Civil War. In the first case, *Hepburn v. Griswold*, decided in February 1870, Chief Justice Salmon P. Chase framed a rather narrow issue and ruled that Congress lacked the power to make greenbacks "legal tender in payment for pre-existing debts," that is, the debt contracted before the issuance of greenbacks. Chief Justice Chase declared greenbacks unconstitutional, even though, as President Lincoln's Secretary of Treasury, he facilitated their issuance. In the second case, *Knox v. Lee*, decided a year later, the Supreme Court overruled *Hepburn* and held that legal tender greenbacks were constitutional with respect to both prior and subsequent obligations.

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155. 75 U.S. (8 Wall.) 603 (1870).
156. Id. at 619, 625, 626.
158. 79 U.S. 457 (1870). This case was decided along with *Parker v. Davis*. See id.
159. These cases have been criticized on various grounds, including the charge of court packing. Around two months before the *Hepburn* decision, the membership of the Court was increased from eight to nine. Before the second case was decided, two new justices were appointed. These two new justices, Strong and Bradley, voted for the constitutionality of the notes in *Knox v. Lee*, which was decided five to four. *See Knox* 79 U.S. at 528. *See also Dam, supra note 20, at 377.*
In response, Justice Chase wrote in his diary: "It is I think a sad day... for the cause of constitutional government."

In *Knox*, the argument for the constitutionality of greenbacks invoked the Madisonian principle that Congress could not be disabled from issuing "promissory notes" during emergencies. Justice Strong, writing for the majority, stated that if "Congress has no constitutional power, under any circumstances, or in an emergency, to make treasury notes a legal tender... the government is without those means of self-preservation..." Of course, Justice Strong employed the Madisonian principle with less than total candor. No reader of the Constitutional Convention would fail to recognize that, though Madison supported the view that the government should be allowed to issue "promissory notes" during an emergency, he was also determined not to give any additional power to the government to make these notes legal tender.

Of all the legal tender cases, *Juilliard v. Greenman* was the most important from a doctrinal viewpoint. The context in which the case arose was different from the first two cases. Despite the constitutional victory in *Knox*, Congress decided in 1875 to redeem greenbacks in coin on demand. Upon redemption, the notes were canceled or retired. Three years later in 1878, however, Congress changed its mind and authorized the Secretary of Treasury to reissue and keep the greenbacks in circulation. Though legal tender, the 1878 greenbacks were distinguishable from the 1862 greenbacks in that the former were redeemable into constitutional coin on demand. This law was challenged in *Juilliard*.

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160. NIVEN, supra note 157, at 440.
162. In a letter to John R. Tucker, Justice Chase wrote that the dissenting justices, himself included, had relied on Madison's observation that the government could issue promissory notes but could not make them legal tender. See NIVEN, supra note 157, at 526 n.31.
163. 110 U.S. 421 (1884).
165. In 1873, Congress dropped the constitutional "Spanish-milled dollar" from the list of national coins, an act known in monetary literature as "the Crime of 1873." The same year, Congress also changed the unit of currency from silver to gold coin and relegated silver coin to minor transactions of $5 or less. See BRECKINRIDGE, supra note 95, at 98. This was the end of silver money as well as of constitutional bimetallism. Since the discovery of gold in 1850s, the market had already relegated silver to a limited use. Thus, the fall of silver was not brought about by the 1873 law. Rather, it was a market decision that the law simply had to recognize. In the next several decades, silver advocates tried to re-institute silver as national money. Laws were passed to keep silver alive through coinage and silver certificates. However, silver as money was functionally dead. The market opted for gold and diminished silver to a mere commodity. The United States, like the rest of the world, became monometallic. The demise of bimetallism was obtained not by constitutional amendment but through laws passed by Congress, approved by the President, and dictated by the market. See LAUGHLIN, supra note 49, at 95.
The 1878 greenbacks were issued under no emergency; thus, the re-authorization of greenbacks lacked the Madisonian rationale. In *Juilliard*, therefore, the critical question hinged on the power of Congress to issue paper money of legal tender quality in peace times. The Supreme Court upheld the constitutionality of the new greenbacks, finding that the power to issue paper money was inherent in the concept of sovereignty.  

In a vigorous dissent Justice Stephen Field argued that the federal government did not possess the authority “to alter the condition of contracts between private parties” by forcing creditors to accept a form of money for which they had not contracted.  

"If there be anything in the history of the constitution which can be established with moral certainty, it is that the framers... intended to prohibit the issue of legal tender notes both by the general government and by the states...."  

Moreover, the greenbacks, Justice Field noted, had lost one half of their face value. If paper money was to be lawful, he remarked, there was no sense in paying “interest on the million of dollars of bonds now due, when Congress can in one day make the money to pay the principal.”  

Despite its bold holding, *Juilliard* was not an unqualified victory for paper money. The holding of *Juilliard* rested on the key fact that the greenbacks issued under the 1878 Act were redeemable into coin.  

The holding in *Juilliard* that the federal government may issue paper money as legal tender presupposed the doctrine of redemption. Greenbacks were no more than legal tender promissory notes that could be redeemed into specie on demand. However, this doctrine of redemption was lost in the broad stroke of the holding, which crudely suggested that Congress may lawfully print paper money even in peace times and make it legal tender with no obligation to redeem such paper into specie. The point was also lost because, although Congress promised the redemption of new greenbacks, the market did not believe the federal government had enough specie to redeem all

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166. See *Juilliard v. Greenman*, 110 U.S. 421, 451 (1884). The Court also relied upon a host of constitutional clauses including the "necessary and proper" clause, a clause that always carries the potential of delivering just about any power to the federal government. See id.

Whereas the abolition of slavery was secured beyond a doubt by amendments to the Constitution, the monetary system was changed by the acts of Congress confirmed by the Supreme Court. See generally Foote, supra note 91. At the time, it seemed to many that the monetary system might regress to pre-Civil War days. See id. This concern was "a factor of doubt, a cause of distrust, and want of confidence in our entire currency and banking system." Id. at 258.


168. Id. (Field, J., dissenting).

169. Id. at 470 (Field, J., dissenting).

170. See id. at 437.
outstanding greenbacks. Accordingly, greenbacks depreciated in value, just as the promissory notes of any unreliable issuer would.

V. THE DUEL OVER OPTIONAL MONEY

During the Civil War, the federal government not only issued the failed greenbacks, it also undertook a number of measures to create a new national currency. If legal tender greenbacks were issued to raise money for the federal government during the Civil War, the new optional currency was aimed at permanently replacing the notes circulated by state-chartered banks. By issuing greenbacks, the federal government challenged the Constitution, and, by issuing a new optional currency, the government entered the turf of the market. Historically, the creation of optional money had been the sovereign domain of the market, a domain that the market loathes to share with any other authority. Accordingly, the market was bound to resist the federal government’s efforts to deny state banks the freedom of creating new forms of optional money. In fact, by the time the federal government was planning to launch a new optional currency, the market was already moving toward the adoption of a new money-substitute, which was potentially much superior than the promissory note that had held together the entire enterprise of banknotes. Therefore, from the starting gate, a duel was set in motion between the government and the market.

The federal government began this duel by launching an offensive to demolish state banking and to monopolize both the quantity and quality of optional money through the construction of a national banking system. Instead of installing a single central bank, an institution that had failed twice since the inception of the Constitution, the federal government chose an alternative route to bring forth a network of national banks. In President Lincoln’s administration, Salmon P. Chase, who was then the Secretary of Treasury, vigorously advocated the cause of national banking. Following the concept of free-banking popular in many states, National Bank Act of 1864 prompted the establishment of national banks in all communities, small and large, across the United States. Though chartered under the federal law, these national banks were established as private businesses. Moreover, the law of 1864 provided incentives for existing state banks to re-charter

171. See Niven, supra note 157, at 300.
172. See Act of June 3, 1864, ch. 106, 13 Stat. 99, 100 (codified primarily at 12 U.S.C. § 21 et seq.). The law set up different capital requirements: $100,000 for ordinary banks; $200,000 for banks established in communities with population exceeding 50,000 persons; $50,000 for communities less than 6,000 inhabitants. See id. at 101.
themselves under the new federal law and become national banks. Though some state banks re-chartered themselves under the federal law, the conversion was by no means massive. Rather, state banks resisted the National Banking Law, fearing, among other things, that the federal government might lose the Civil War.

A. The Overthrow of Local Notes

An important first step toward creating a new currency was the destruction of state banknotes. The proposal was driven by a desire to overthrow "the whole system of state banks." Senator John Sherman of Ohio, the chief advocate of a national banking system, argued that the state banking system was incompetent and unconstitutional. Although state banks provided the bulk of the money supply in the form of banknotes, the system was nonetheless chaotic if not damaging to the economy. Even the market disapproved of the proliferation of the unreliable banknotes of state banks. Volatile fluctuation in the value of banknotes was the most unsettling aspect of the monetary system. Although the notes of some state banks were stable in value and were exchanged at par, many rural banks, located far away from big cities, issued notes with little or no specie to support them. Consequently, many local notes circulated at highly depreciated value. According to one estimate, by the time of the Civil War, more than sixteen hundred state banks chartered under the laws of twenty-eight different states were engaged in supplying, managing, and monitoring the money supply.

Driven by sentiments to strengthen the Union and perhaps taking hints from the market that unreliable local notes ought to be suppressed, the federal government attempted to fix the problem. On the prompting of Secretary Chase, Congress passed a law that imposed a ten percent tax on state banknotes, which was levied both on the

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173. Seven hundred new national banks were chartered before the first conversion of a state bank into a national bank. See HAMMOND, supra note 76, at 732.

174. See JOHN SHERMAN, REFLECTIONS OF FORTY YEARS 282-84 (1895). The lure of national banking and its note circulation as privileged national money gave birth to many new nationally-chartered banks.

175. See id.

176. In a famous case, Chief Justice Chase made the following remark: "At the beginning of the rebellion [civil war] the circulating medium consisted almost entirely of bank notes issued by numerous independent corporations ... of various degree of credit ... administered often with great, and not unfrequently, with little skill, prudence, and integrity." Veazie Bank v. Fenno 75 U.S. (8 Wall.) 533, 536 (1869).

177. See SHERMAN, supra note 173, at 289. See also HAMMOND, supra note 76, at 726. Not all state banks issued the circulation notes.

issuer of the notes and on any person, bank, or corporation paying them. The tax caused the extinction of state banknotes. Later, Chase, as the Chief Justice of the Supreme Court, upheld the constitutionality of this prohibitive tax. The elimination of state banknotes was supposed to pave the way for national banks to monopolize the money supply.

B. The Reign of National Banknotes

By supporting a more reliable currency, the forced switch from local to national banknotes was the law’s effort to control the quality of money. The national banknotes were issued in different denominations ranging from one dollar to one thousand dollars. The Comptroller of the Currency approved the design of plates and special dies used in the printing of national banknotes. Despite their uniform look, the notes still identified the issuing national bank. Each note contained on its face an explicit promise of the issuing bank to provide constitutional coin on demand. This promise to pay was guaranteed by a further notation on the face of the note that it was “secured by a pledge of United States bonds.” To vest them with even more marketable quality, the notes were engraved with the seal of the Treasury. In their legal format, therefore, national banknotes were secured promissory notes issued by privately-owned banks.

Despite the promise and security printed on the face of national banknotes, it was initially unclear whether notes would be redeemed in constitutional coin or in greenbacks. In 1870, a new federal law clarified the situation, mandating that the promise written on the face of national banknotes bear a commitment that upon presentment the issuer would redeem the notes in gold coin of the United States.
Thus, the status of national banknotes as promissory notes to be paid in constitutional coin on demand was explicitly restored. Once the doctrine of redemption was embossed on their face, no one questioned their constitutionality.

To further enhance the quality of national banknotes, the law required each national bank to create a reserve of credible assets.\(^{188}\) Before starting business, each issuing bank was obligated to purchase U.S. bonds in the amount of at least one-third of its capital stock and deposit them, as a reserve, with the Treasury. In fact, each national bank was entitled to circulate notes equal in an amount to ninety percent of the "current market value of the United States bonds" deposited with the Treasury.\(^{189}\) By creating a direct linkage between government bonds and circulation notes, the federal government linked the money supply to the federal debt. This relational restraint on the quantity of circulation notes was in addition to the limit placed on the total amount of notes that the national banking system could collectively issue.\(^{190}\) This limit on the total supply of money was designed to curb inflation.

It is important not to confuse the new paper currency with greenbacks. The federal government issued greenbacks, whereas federally-chartered banks issued national banknotes. Greenbacks were legal tender in both private and public debts, whereas national banknotes were an optional currency in private transactions.\(^{191}\) However, national banknotes held a new governmental approval that state banknotes lacked. The national banknotes were lawfully receivable at par in payment of taxes, excises, public lands, and all other dues to the it, except for duties on imports.\(^{192}\) The federal government could also lawfully tender national banknotes to pay salaries and other debts that it owed to individuals and corporations within the United States. The federal government could not, however, tender the notes to pay interest on public debts or to redeem greenbacks.\(^{193}\)

\(^{188}\) Following the New York free-banking law, the Act of 1864 allowed the establishment of national banks in all communities, small and large, across the United States. See Act of June 3, 1864, ch. 106, 13 Stat. 99, 100.

The law set up different capital requirements: $100,000 for ordinary banks; $200,000 for banks established in communities with population exceeding 50,000 persons; $50,000 for communities with less than 6,000 inhabitants. See id.

\(^{189}\) Id. § 21.

\(^{190}\) See id. § 22. This Act fixed the aggregate amount of national banknotes to $300 million. See id. The limit was raised to $904 million in 1870. The Resumption Act of 1875 eliminated all restrictions on the emission of notes.

\(^{191}\) See id. § 23.

\(^{192}\) See id.

\(^{193}\) See id.
Thus, during the Civil War, the federal government launched two distinct forms of paper money: legal tender money in the form of greenbacks and optional money in the form of national banknotes. When the Union was in utter chaos, the redemption of any paper currency into specie was uncertain. This lack of redemption was perhaps constitutional under the Madisonian principle of emergency. After the Civil War, Congress restored the constitutional doctrine of redemption, restoring the status of both greenbacks and banknotes as promissory notes redeemable in constitutional coin, and, as Congress reverted to borrowing money through traditional loans, depreciated greenbacks began to fade away from the market. The national banknotes served as optional money, but they failed to destroy the state banking system as the federal government intended.

C. Market's New Darling

While the federal government was launching a new national currency and suppressing state banknotes, the market already had introduced a competing optional money—the check,\textsuperscript{194} the market's new darling that not only rescued state banks from extinction but also caused their further proliferation. Instead of issuing tax-prohibitive banknotes, state banks began to open deposit accounts against which customers could draw checks. For state banks, the checking account method of lending money turned out to be more profitable than the issuance of banknotes. For customers, the checking account simplified transactions: if banknotes were more convenient than coins, checks were even more convenient than banknotes. One check could transfer a large amount of money that otherwise had to be counted and transported. Moreover, the check was safer than banknotes, as a check could be issued to a named payee, whereas the banknote was bearer paper. "Thus, the market frustrated the federal government's determination to destroy the whole system of state banks."\textsuperscript{195} In fact, the checking account posed a direct threat to the very existence of national banknotes, let alone their domination. Enamored with the convenience and safety of the check, the market gradually paved the way for the eventual elimination of national banknotes, as even national banks preferred the superior efficiency, safety, and profitability of the checking account.

\textsuperscript{194} See Hurst, supra note 47, at 35. "Checks were in substantial use in principal commercial cities by the beginning of the nineteenth century." Id.

\textsuperscript{195} See Niven, supra note 157, at 297-98.
The concept of check was perfectly compatible with the monetary clauses of the Constitution, as interpreted in Briscoe. Just like the promissory note, the check is a negotiable instrument that the market created to transfer value. Though a form of paper money, the check is optional in character because no creditor is under any legal obligation to accept it in payment of debts. Most importantly, the check was inherently compatible with the reigning constitutional doctrine of redemption. Like the banknote, the check was no more than a money-substitute to be redeemed in constitutional coin.

Despite its unquestionable constitutionality, the check shifted the burden of redemption from banks to customers, a burden that the banknote placed totally and exclusively on issuing banks. Thus, a critical conceptual difference was interposed between the banknote and the check, even though both instruments were eventually to be redeemed at the banks. The banknote carried the credit of the issuing bank. It was the bank's undeniable responsibility to convert the note into specie on demand, regardless of the nature of the person seeking redemption. A check, in contrast, carried the credit of the person who issued it. The bank on which the check was drawn had no obligation to redeem the check until acceptance, for the redemption of a check could be lawfully refused for a host of reasons ranging from forgery, theft, or alteration of the check itself to insufficient funds in the account. This shift of burden, though important, failed to solve the problems of redemption that plagued the monetary system and the banking industry.

VI. A MORE PERFECT MONETARY UNION

It has never been a secret that all banks lend more money than they receive from their depositors. This expansion of money supply, though potentially a cause for inflation, is often needed for a growing economy. The practice of lending more money than a bank has in its possession hinges on a wishful expectation that not all customers will seek redemption at the same time. When creditors seek redemption in unison, the banking paradise often collapses. Given the redemption

196. See supra notes 97-106.
197. However, the bank was under a duty to accept a properly drawn check.
198. Notwithstanding the monetary clauses, the market knew the dangers of redemption because, to preempt wholesale redemptions, the market cultivated the stratagem of bank reputation. A bank could preempt wholesale redemption, it was theorized, by showing a complete willingness and ability to redeem on demand its notes and properly drawn checks. If the note or account holders were assured that the bank has the means to redeem its paper on demand, they would not rush to seek redemption. Though such psychological strategies aided large banks, they proved ineffective to halt the panics of redemption because even a well-reputed bank sank swiftly when the holders of its notes and the owners of its checking accounts
panics of post-Civil War decades, the market was prepared to totally discard the constitutional doctrine of redemption, but the law was not. Congress attempted to fix the problem of panics by resurrecting the idea of a central bank, an institution that had failed twice since the inception of the Constitution.

A. Federal Reserve Notes: Paper Dollars of the Twentieth Century

In 1913, six years after the devastating panic of 1907, Congress established the Federal Reserve Board, the so-called central bank, "to furnish an elastic currency . . . and to establish a more effective supervision of banking in the United States." Additional reasons, not articulated by Congress, supported the launching of a new currency, if not a central bank. Due to the market triumph of the check, national banks were losing interest in the issuance of banknotes. Even though the check was a reliable payment instrument for transferring large amounts of value, the nation nonetheless required some form of tangible currency, at least for consumers unfamiliar with the checking account or engaged in transactions involving smaller amounts. Furthermore, the growing presence of the United States in international markets accentuated the need for a national currency for "global invoicing, payments, and reserve purposes." The lingering national banknotes, embossed with the individual obligation of a thousand different banks, failed to present the dollar as the single, unified currency of the United States.

Dictated by domestic and international markets, Congress retired national banknotes and created a new national currency in the form of Federal Reserve notes. Uniform in size, color, look, paper quality,

all ran simultaneously to redeem their holdings. Consequently, the banks frequently failed in legions, causing extreme jolts to the monetary system.

199. Federal Reserve Act, ch. 6, 38 Stat. 251 (1913) (codified in scattered sections of 12 U.S.C.). The central bank, now called the Federal Reserve System, consists of 12 regional banks and is governed by a Board of Governors (BOG). The nation is divided into 12 regions, each with its own Federal Reserve Bank (FRB). Each FRB is a corporation whose stock is owned by commercial banks in the region. Each national bank must join the regional FRB, whereas state banks have an option to do so. See 12 U.S.C. § 282 (1994). The 12 regional FRBs are supervised by the BOG, which is a seven member committee whose members are appointed by the President with the advice and consent of the Senate.


201. Three successive steps were designed to achieve this purpose. First, Congress set up a 20 year period from December 15, 1915 to retire national banknotes. Second, Congress authorized FRBs, the 12 regional federal banks established across the United States, to issue Federal Reserve bank notes with the security of United States bonds. Third, and most important, Congress introduced a new form of money called Federal Reserve notes to be issued directly by the Central Bank. See Federal Reserve Act, ch. 6, § 16, 38 Stat. 251, 268 (1913).
and notations and available in different denominations, Federal Reserve notes are the paper money we now use in "cash" transactions. The notes are issued at the discretion of the Federal Reserve Board only to regional federal banks. Therefore, no person, corporation, state bank, or national bank can directly procure the notes from the Central Bank. The procedure of obtaining Federal Reserve notes empowers the central bank to control the amount of notes in circulation. Most important, Federal Reserve notes are the obligation of the United States and not the regional bank that obtained them by supplying the appropriate collateral. This transfer of obligation from private banks to the federal government distinguishes Federal Reserve notes from national banknotes, which were the direct obligation of the procuring bank. Thus, for the first time in the history of the United States, a new optional currency was issued as a direct obligation of the nation as a whole.

Despite their unprecedented national stature, Federal Reserve notes still constituted banknotes embodying the twin characteristics of redemption and optionality. Maintaining the idea of redemption, Congress created Federal Reserve notes in the image of private banknotes: they were promissory notes bearer in form, negotiable by delivery alone, and convertible in gold on demand. In 1913, the law specifically provided that Federal Reserve notes "shall be redeemed in

Linguistic confusion aside, the difference between Federal Reserve bank notes and Federal Reserve notes was real. Federal Reserve bank notes were genetically related to national banknotes. They were essentially banknotes bearing the number of the FRB that issued them. Just as national banks procured notes from the Comptroller of the Currency against a deposit of United States bonds, FRBs followed the same procedure to procure their notes. Just as national banknotes were obligations of the issuing bank, the Federal Reserve bank notes were obligations of the specific FRB that issued them. Moreover, like national banknotes, Federal Reserve bank notes were not legal tender in private transactions. In 1933, however, they were made legal tender. The purpose of Federal Reserve bank notes was to consolidate the currency at the regional level. Despite their name, national banknotes were "local" in the sense that the name of the issuing bank was printed on notes, which were obligations of the named bank. Whether they would be redeemed in gold or silver depended directly on the financial soundness of the named bank. In contrast, Federal Reserve bank notes were "regional" in character. It was hoped that myriad national banknotes, already in the process of retirement, would be replaced with "regional" banknotes, that is, Federal Reserve bank notes.

203. See id. § 412 (1994). Only a FRB may "make application" to receive these notes by offering an appropriate collateral security. The Central Bank, however, retains the discretion not to issue notes even if proper collateral is provided. This explicitly delegated discretion is designed to establish the control of the Central Bank over money supply.

In the Federal Reserve Act of 1913, the collateral security was limited to notes and bills accepted for rediscount. Under current law, the concept of collateral security has been expanded to include "drafts, bills of exchange . . . bankers' acceptances . . . gold certificates, or Special Drawing Right certificates, or any obligations . . . of . . . the United States or any agency." Id.

204. See id. § 411.
gold on demand at the Treasury Department of the United States, in the
city of Washington, District of Columbia, or in gold or lawful money at
any Federal reserve bank.\textsuperscript{205} The notes themselves carried on their face
a written legend that they were "redeemable in gold on demand." This
legal promise retained, at least facially, the historically understood
meaning of the Constitution that the real money of the United States
shall be none else but silver and gold. Furthermore, Federal Reserve
notes were also not a legal tender in private debts.\textsuperscript{206} Thus, the issuance
of Federal Reserve notes was to a large extent consistent with the notion
embodied in the monetary clauses that nothing but gold and silver shall
be the legal tender money of the United States.

The Great Depression of 1930s, however, changed the nature of
Federal Reserve notes, driving a wedge between money and the
Constitution. The Central Bank, created to halt redemption panics,
proved to be an utter failure. The trauma of Great Depression precipitated a record number of bank failures, a phenomenon that the
Central Bank could neither prevent nor halt.\textsuperscript{207} The message of the
market was clear: repudiate the idea of redemption! Realizing that
metallic money was no longer compatible with realities of the market
and perhaps invoking the Madisonian emergency principle, President
Franklin Delano Roosevelt, as part of his New Deal initiatives, outlawed
all redemption. The Joint Resolution of 1933 declared that obligations
that require payment in gold "obstruct the power of the Congress to
regulate the value of money of the United States . . . ."\textsuperscript{208} All
obligations, private and public, requiring payment in gold, the so-called
gold clauses, were held to be against public policy.\textsuperscript{209} The Gold Reserve
Act of 1934 provided that no currency of the United States would be
redeemed in gold.\textsuperscript{210} It also amended section 16 of the Federal Reserve
Act and deleted its gold redemption provision,\textsuperscript{211} thereby dramatically

\textsuperscript{205} Federal Reserve Act, ch. 6, § 16, 38 Stat. 251, 265 (1913).

\textsuperscript{206} Initially, in 1913, Federal Reserve notes enjoyed a limited legal tender status and were lawfully receivable "for all taxes, customs, and other public dues." \textit{Id.}

\textsuperscript{207} See \textit{GALBRAITH, supra note 55, at 194.} "In 1929, 659 banks failed . . . . In 1930, 1352 went under and in 1931, 2294." \textit{Id.}

\textsuperscript{208} Joint Res. of June 5, 1933, ch. 48, 48 Stat. 112.

\textsuperscript{209} See generally \textit{id.}


\textsuperscript{211} See Gold Reserve Act of 1934, ch. 6, § 2, 48 Stat. 337, 338. Furthermore, the Act mandated that all gold coin be withdrawn from circulation and converted into gold bars. \textit{See id.} § 5. The Act also prohibited the Treasury from holding gold coins. \textit{See id.} § 6.
changing the legal status of notes. In 1913, notes were redeemable in gold and were not legal tender. By 1934, they could not be converted into gold and were declared legal tender for all debts, public and private.\footnote{At one point, gold coins, gold certificates, silver dollars, silver certificates, Federal Reserve notes, and treasury notes all were legal tender in private and public debts. \textit{See generally} George Nebolsine, \textit{The Gold Clause in Private Contracts}, 42 \textit{Yale L.J.} 1051 (1933).} To conform with this new public policy, the printed promise on the face of notes that they are redeemable in gold was erased.\footnote{Despite their lack of redemption in constitutional coin and despite their new status as legal tender, Federal Reserve notes were still redeemable into lawful money. Their new status was printed on the face of all Federal Reserve notes of all denominations: "This note is redeemable in lawful money at the United States Treasury, or at any Federal Reserve Bank." If the notes could not be converted into constitutional coin, the question remained, indeed a nagging question, how the notes could be redeemed in lawful money. To remove this irritant, the federal government erased the promise of redemption from the face of notes.} Thus, the New Deal repudiated both redemption and optionality, creating a new official money of the United States.

When challenged, the Supreme Court upheld the constitutionality of the Joint Resolution.\footnote{\textit{See generally} Norman v. Baltimore, 294 U.S. 240 (1935) (stating that huge volume of existing obligations with gold clause could be considered by Congress in determining whether existence of such clause substantially obstructed its monetary policy). \textit{See also} Nortz v. United States, 294 U.S. 317 (1935) (law forcing redemption of gold certificate in paper currency rather than gold was constitutional). However, the Court ruled that Congress may not lawfully repudiate its own obligation to pay in gold. \textit{See} Perry v. United States, 294 U.S. 330 (1935).} Instead of limiting its analysis to the monetary clauses, the Court invoked the "full weight of the constitution"\footnote{Listing several enumerated powers, the \textit{Norman} court found that Congress has broad and comprehensive national authority over the subjects of revenue, finance, and currency. \textit{Norman}, 294 U.S. at 303. I have articulated the concept of "the full weight of the Constitution" in another context, arguing that the Court should apply the entire Constitution, even if it is not argued in the briefs or courts below, when the existence of a fundamental right is asserted or disputed. \textit{Ali Khan}, \textit{The Invasion of Sexual Privacy}, 25 \textit{San Diego L. Rev.} 957, 974-76 (1986).} to conclude that Congress, acting under its aggregate powers, is empowered to provide a stable and uniform currency for the United States.\footnote{\textit{See Norman}, 294 U.S. at 304.} State courts were equally reluctant to find faults with the new national currency.\footnote{In several states, interesting cases have challenged the constitutionality of Federal Reserve notes and their lack of redemption in specie. \textit{See e.g.}, Brand v. State, 828 S.W.2d 824 (Tex. Ct. App. 1992) (stating that Congress has the power under the Constitution to establish national paper currency, has delegated that power to the Federal Reserve System, and has designated Federal Reserve notes as legal tender). Hence, Texas statutes imposing fines payable with Federal Reserve notes for traffic violations are constitutional. \textit{See also} May v. Bailey, 693 S.W. 2d 246 (W.D. Mo 1985) (stating that a Missouri statute, declaring United States silver coins to be legal tender for payment of public and private debts contracted in Missouri, must yield to federal law establishing Federal Reserve notes as legal tender; hence, dentist could not lawfully demand medicaid payment exclusively in United States silver coins). \textit{See} Milam v. United States, 524 F.2d 629 (9th Cir. 1974) (holding that the holder of a Federal Reserve Bank note, although entitled to redeem his note, was not entitled to do so in precious metal).} In jurisprudence, this episode was a clear triumph of legal positivism: the law is what the ruling institutions say it is. The
move to abolish the doctrine of redemption was well-intentioned, and the outcome was perhaps beneficial. Nonetheless, the New Deal monetary policies underscored the point that important provisions of the Constitution can be nullified, for better or worse, when the Legislative, Executive, and Judicial branches join hands in stressful times.\textsuperscript{218}

Although the federal and state courts upheld the suspension of the doctrine of redemption, it was unclear whether Congress intended to abandon the doctrine for good. However, once the trauma of Great Depression dissipated and the Madisonian rationale no longer supported deviation from the monetary clauses, Congress revived the doctrine of redemption, just as it resurrected the redemption of greenbacks at the end of Civil War. To not to do so would have been a blatant nullification of the monetary clauses. This time, however, the idea of redemption was housed in a labyrinth of twisted detours. Even after a careful reading of the following section, most readers would conclude that Congress has completely obfuscated the concept of redemption through the mysterious notion of “lawful money.”

\textbf{B. The Mystery of Redemption}

Although the current Federal Reserve notes promise no redemption on their face, the law in the books still does. The current law, codified in the Federal Reserve Act, maintains that Federal Reserve notes “shall be redeemed in lawful money on demand at the Treasury Department of the United States, in the city of Washington, District of Columbia, or at any Federal Reserve bank.”\textsuperscript{219} Thus, the law makes a distinction between Federal Reserve notes and lawful money. But what is lawful money? Is it gold or silver coin? Is it greenbacks? Is it something nonexistent?

Is gold coin the lawful money referred to in the Federal Reserve Act? The gold coin, first adopted a unit of currency in the Coinage Act of 1849, though debased twice in its content of pure grains, remains the lawful money of the United States.\textsuperscript{220} The current law states that the gold dollar “nine-tenths fine” consisting of the weight determined under

\textsuperscript{218} Cf. Korematsu v. United States, 323 U.S. 214 (1944) (sustaining a military order excluding Americans of Japanese origin from designated West Coast areas). See LAWRENCE TRIBE, AMERICAN CONSTITUTIONAL LAW 1000 (1978) (noting the nefarious impact that war can have on institutional integrity).
\textsuperscript{220} In 1933, Congress authorized the President “to fix the weight of the silver dollar in grains nine tenths fine at a definite fixed ratio in relation to the gold dollar.” Emergency Farm Mortgage Act of 1933, ch. 25, sec. 991, § 43(b)(2), 48 Stat. 51, 52-53.
the provisions of this title "shall be the standard unit of value." In reality, however, Congress has prohibited the Treasury from minting one dollar gold coins. The Secretary of Treasury may mint and sell gold coins for numismatic purposes, but Federal Reserve notes cannot be redeemed at par in these coins. To this extent, therefore, lawful money exists in the form of gold coins but not for the stated redemption.

Similarly, the silver coin cannot be the lawful money mentioned in the Federal Reserve Act. In 1933, Congress authorized the issuance of silver certificates and the conversion of silver into "standard silver dollars" to meet any demands for the redemption of such silver certificates. Standard silver coins, however, were not to be circulated as money but "retained" in the Treasury for the payment of such certificates on demand. Subsequently, Congress passed a law to terminate the redemption of silver certificates in "standard silver dollars." In theory, the standard silver dollar is still the lawful money of the United States. But just like the standard gold dollar, the standard silver dollar is no longer minted. Like numismatic gold coins, Congress has authorized the Treasury to mint numismatic one dollar silver coins of definite size, weight, and design. This numismatic silver dollar, however, is not the same as the Susan B. Anthony dollar. Nor is it the same as the standard silver dollar referred to in the Constitution. The public may use Federal Reserve notes to buy numismatic silver coins but Federal Reserves notes cannot be redeemed at par in these coins. Similar to numismatic gold coins, silver coins are both legal tender and lawful money. Thus, lawful money in the form of numismatic silver coins exists but not for the redemption of Federal Reserve notes.

Finally, we are left with greenbacks as the possible lawful money. As discussed earlier, these notes, when first issued during the Civil War, lacked any promise of redemption into specie. A few years later, they were made convertible into the constitutional coin, a key fact upon which the Supreme Court relied in upholding the constitutionality of

221. Act of Mar. 4, 1900, ch. 41, § 1, 31 Stat. 45, 45.
222. See 31 U.S.C. § 5112(a)(7-10) (1994). These numismatic gold coins are sold at a price equal to the market value of the bullion at the time of sale. These coins are both legal tender and lawful money.
223. See id. § 5118(b). However, a person lawfully holding gold coins may present the coins to the Secretary of the Treasury in exchange (dollar for dollar) for Federal Reserve notes, an exchange that no economically rational person would request.
224. Act of May 12, 1933, ch. 25, 48 Stat. 53 § 45(c).
226. See 31 U.S.C. § 5112(b). These numismatic silver coins are sold to the public at a price equal to the market value of the bullion at the time of sale, plus the cost of minting, marketing, and distributing such coins, including labor, materials, dies, use of machinery, and promotional and overhead expenses.
these notes. Thus, if Federal Reserve notes are redeemable in greenbacks and if greenbacks are redeemable in gold, one could simply conclude that Federal Reserve notes are redeemable in gold. However, this simple logic failed in 1933 when Congress prohibited the conversion of any currency into gold. Moreover, in 1945, Congress passed a law terminating the authority of the President and the Secretary of Treasury to issue greenbacks.

In summary, it is possible to reach only one conclusion, namely that lawful money for the redemption of Federal Reserve notes is nonexistent. The distinction between paper money and lawful money was unimpeachable when lawful money consisted of gold and silver coin. State banknotes, national banknotes, greenbacks, and initially even Federal Reserve notes were all myriad forms of the promissory note, convenient substitutes for constitutional money. A money-substitute performs many functions of money, including that of a medium of exchange for transferring goods and services. Even when redemption of money-substitutes into constitutional coin is temporarily suspended during unexpected emergencies, the distinction between lawful money and money-substitutes remains. A money-substitute may even constitute legal tender provided it still can be converted into real money. But when paper money is convertible only into another form of paper money, the monetary clauses lose their normative as well as historical meaning.

C. No Coin, No Paper

The creation of Federal Reserve notes is by no means the final victory of official currency. The elimination of state or national banknotes

229. One insight into the status of greenbacks is captivating. In 1933, Congress authorized the President "[t]o direct the Secretary of the Treasury to cause to be issued . . . United States notes [greenbacks] . . . in the same size and similar color of the Federal Reserve notes." Emergency Farm Mortgage Act of 1933, ch. 25, sec. 991, 48 Stat. 51, 52. This striking similarity between the two types of notes renders the concept of redemption of Federal Reserve notes into greenbacks an exercise in playful futility. See id. Even if United States notes are under the control of the Secretary of Treasury and not the Federal Reserve System and even if they are not "in the same size and familiar color" as Federal Reserve notes, these factors will convince few that one set of notes are "lawful money" while the other set is "redeemable in lawful money." Id.
231. See SUBCOMMITTEE ON FINANCE, HOUSE COMMITTEE ON BANKING AND CURRENCY, A PRIMER ON MONEY 19 (1964) (stating that Americans holding Federal Reserve notes cannot demand anything other than that they be exchanged for other Federal Reserve notes).
232. Despite a concerted effort to monopolize the creation of official money, private banking, whether state-chartered or federally-charted, continues to thrive. In fact, banking is becoming international in scope as foreign banks are allowed to operate in the United States.
has contributed little to the domination of Federal Reserve notes because the efficiency-driven market continues to breed new forms of optional money, that are simple to use and more easily portable, just as it created banknotes to replace coins, checks to replace banknotes, and credit cards to perhaps replace checks. The market is now headed toward creating "e-money." Even today, the official currency in the form of Federal Reserve notes and coins is used only in small transactions. Large transactions involving huge amounts of money are executed with checks or by electronic means. Increasingly, consumers prefer to use credit cards and debit cards to buy goods and services and rarely pay their bills in Federal Reserve notes or coins. Employers often pay salaries by direct electronic transfer of funds to employees’ individual accounts. Businesses transfer billions of dollars across interstate and international borders without ever handling a single Federal Reserve note or coin.

In short, money is no longer a physical entity. For the framers of the Constitution, the money was not only a medium of exchange but also a physical entity. Even if they understood that the market would create new forms of optional money, they intended that official money be embodied in nothing but gold and silver coin. This constitutional conception of physical money is lost as the embodiment of money changes from metal to paper. In the continuing evolution of money, it appears the dollar will eventually become an abstract unit of currency with no specific embodiment in metal or paper. This shift towards an abstract currency will become even more complex through the evolution of regional and global markets. It is unclear whether a regional monetary union under the North America Free Trade Agreement will ever occur, but if the United States enters such a monetary union, its money will venture into a brave new world, further mystifying an already intriguing story of the monetary clauses of the United States Constitution.

VII. CONCLUSION

From a constitutional viewpoint, the story of money in the United States contains a fascinating interplay between war, law, and the

234. Despite its prominence and worldwide acceptance, the dollar as a unit of currency has no fixed value in money markets of the world. In an emerging global economy, the dollar, as a unit of currency, fluctuates against other currencies, making a direct impact on international trade and domestic finance. Right now, the dollar is the most reliable unit of currency, though its exchange value with other currencies of the world is related to a host of complex factors. No one can predict the future strength of the dollar.
market. The outcome of this complex interaction has shifted the monetary system away from both the text and original intent of monetary clauses. When Congress prohibited the convertibility of paper money into gold and silver on a seemingly permanent basis, the distinction between money and money-substitute became confusing. The concept of lawful money is deceptive. Theoretically, Congress has two clear options to dispel this deception. It may declare the dollar a mere unit of currency, foreclosing the idea of redemption and the concomitant concept of lawful money. This option appears quite reasonable but it would run contrary to the historically understood meaning of the monetary clauses. As a second option, Congress may revive the concept of redemption, rehabilitating gold and silver coin. This option is problematic because precious metals have repeatedly failed to provide a stable monetary system in the United States and in other countries. In fact, nations all over the world are severing their currencies from all precious metal.\textsuperscript{235} Of course, Congress may do nothing and let the money evolve as it has in the past centuries.