The U.S. Constitution and Monetary Powers:
An Analysis of the 1787 Constitutional Convention
And How a Constitutional Transformation of
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Abstract: 

The monetary powers embedded in the U.S. Constitution were revolutionary and led to a watershed transformation in the nation’s monetary structure. They included determining what monies could be legal tender, who could emit fiat paper money, and who could incorporate banks. How the debate at the 1787 Constitutional Convention over these powers evolved and the path the founding fathers took that led to the specific powers adopted is presented and deconstructed. Why they took this path rather than replicate the colonial system and why they codified such powers into supreme law rather than leave them to legislative debate are addressed. 

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In 1787, three years after the Treaty of Paris recognized U.S. independence, the founding fathers met from May 25th through September 17th in Philadelphia to craft a new national constitution to replace the Articles of Confederation.¹ This new U.S. Constitution, ratified by the States and then adopted by Congress in 1789, profoundly altered the nation’s monetary structure. It was nothing short of revolutionary. Before the U.S. Constitution, the principal “inside” paper money in circulation was issued directly by government legislatures and backed not by specie (the “outside” money of the times) but by the issuing government’s future taxes. Very few banks existed—none before 1782 and only three by 1787. After the U.S. Constitution, governments were prohibited from issuing paper money. Instead, publicly chartered, but privately run, banks proliferated—numbering 76 by 1805—and filled the inside paper money void by issuing banknotes backed by fractional specie reserves. By banning its chief alternative competitor, the U.S. Constitution established the legal framework that allowed for the ascendance in the U.S. of what we now recognize as the modern bank-based financial system.²

The Constitutional monetary powers of interest here are defined narrowly as 1) the power to emit bills of credit (paper money), 2) the power to determine what money is legal tender, and 3) the power to charter banks. Other monetary powers in the Constitution, such as the power to mint coins, regulate the value of foreign coins, and fix the standard of weights and measures (all dealing with outside money), while not unimportant, were neither controversial nor far reaching in their affect on the monetary structure of the economy and so will not be discussed.

In the U.S. Constitution the founding fathers decided by an explicit vote not to include the power to emit bills of credit, and (debatably) not to include the power to charter banks, among the powers to be granted to the Federal Government [Article 1, Section 8]. They also decided to prohibit individual States absolutely from emitting bills of credit and from having power to determine what could be legal tender, i.e. Article 1, Section 10 of the U.S. Constitution states, “No State shall…coin Money; emit Bills of Credit;
make any Thing but gold and silver Coin a Tender in Payment of Debts…” These decisions embedded in simple Constitutional clauses and Convention votes radically transformed the nation’s monetary structure.

The primary purpose of the analysis that follows is to trace and deconstruct the “what” and “how” of this dramatic constitutionally-manufactured transformation of governmental monetary powers as they evolved during the Constitutional Convention. These powers were not a reason why the Convention was called. They were not an issue at the 1785 Mount Vernon Conference or at the 1786 Annapolis Convention, precursors to the 1787 Constitutional Convention. Nor were they an issue in the numerous amendments to the Articles of Confederation from 1781 through 1786 (Grubb 2003, 1789; Jensen I, 140-229; Rutland II, 814-822). The primary reasons given for calling the Convention were to solve trade and navigation disputes between the States and to secure an independent and direct source of tax revenue for the National Government. By giving the National Government an independent power directly to raise tax revenue and regulate trade between the States, the structural allocation of power among the States within the National Government became a paramount concern and occupied most of the Convention’s time. The issue of governmental monetary powers, however, became one of the sub-texts at the Convention, similar to how the issues of slavery and restraining the “excesses” of democracy became sub-texts at the Convention.

In the process of deconstructing the evolution at the Convention of these constitutionally-specified monetary powers, several themes will emerge. The most prominent will be the systematic and perhaps deliberate conflation of legal tender (exchange rate) issues with the emission of paper money per se. The problems caused by the former being used by Convention delegates, perhaps deliberately, to erroneously tar the latter. Another prominent theme will be why monetary powers should be codified as absolute constitutional proscriptions as opposed to being left for democratic legislative debate, enactment, and modification to circumstance. How did the founding fathers during the Convention make the leap from angst over specific legislative policies regarding paper money and legal tender to making supreme law restricting the paper money powers of government? In the quarter century before the Revolution, colonial America had experience reasonably stable fiat paper money regimes. Why didn’t the founding fathers simply replicate that system? Why did they instead opt for something radically different? In other words, how did they get from a quarter century experience of reasonably stable paper money regimes in colonial America before the Revolution to a total Constitutional ban on paper money at all levels of government
after the Revolution? Was it via reasoning, ignorance, or crafty slight-of-hand? A brief history of American monetary regimes leading into the Constitutional Convention will be given first.

I. The American Monetary Regime Leading into the Constitutional Convention, 1750-1787

A. Legislature-issued Tax-backed Fiat Paper Money Regimes and Their Regulatory Constraints

The British North American colonies were the first modern western economies to experiment with large-scale government issuances of fiat paper money. Colonial legislatures directly issued bills of credit to pay for their government’s expenses and as mortgage loans to subjects who pledged their lands as collateral. These bills were not government bonds. Typically, they earned no interest, came in small denominations, circulated at market-determined rates of exchange to specie (gold and silver coins) and the paper monies of other colonies, and were accepted by the issuing government in payment of that government’s fees and taxes. Colonial governments never redeemed on demand their paper money for specie nor entered the market at their discretion to buy and sell their paper money for specie to defend a fixed exchange rate. These bills circulated inside, but seldom outside, the colony of issue as cash alongside specie monies, which only entered and exited the colony through merchant foreign trade and government transfers. Payments to parties outside the colony were typically in specie units. By the middle of the 18th century, these bills comprised a substantial portion of the money supply within their respective colonies. Colonial legislatures backed their paper money by linking it not to specie but to future taxes and mortgage payments designed to withdraw it from circulation in a timely fashion. Upon redemption, it was burned. Each colony maintained the market value of its paper money through its timely injection and then redemption, thereby controlling the quantity of paper money in circulation. The presence of competitive currency substitutes (specie) constrained colonies to follow a stable path with regard to the relative value of their inside paper monies. (Brock; Grubb 2003, 2004b; Perkins; Priest; Smith 1985; Wicker).

The British government extended the Bubble Act to the colonies in 1741 that effectively eliminated banks and imposed regulation on the emission of paper money with the Currency Acts of 1751 and 1764. These two Currency Acts allowed the colonies to emit paper money as long as it met two requirements, namely 1) that it not be made a legal tender and 2) that ample taxes be put in place to redeem each issue in a reasonable time. Some colonies had instituted such policies on their own accord long before these regulations were passed. After 1748, only Massachusetts (and some other New England colonies)
renounced paper money and returned to a specie standard for the rest of the colonial period. While paper money could not be made a legal tender for all debts, it was always accepted in payment for the issuing government’s taxes and so it became a de facto legal tender for public debts in the issuing government’s jurisdiction. This in turn provided the anchor that allowed the bills to circulate as cash within that colony, i.e. circulate as inside money in each issuing colony, respectively. By 1750 colonial legislatures had learned, for the most part, how to handle their tax-backed paper money regimes. This colonial monetary system produced remarkable long-run stability in terms of low inflation rates and stationarity in prices, exchange rates, and purchasing power parity. (Behrens; Bordo and Marcotte; Brock; Grubb 2003, 2004b, 2004c; Perkins; Pickering XX, 306-309; Priest; Smith 1985; Wicker).

The two regulatory pillars that made this colonial monetary system work were 1) that paper money could not be made a legal tender (other than for paying taxes levied by the issuing government), and 2) that the issuing government credibly commit, by enacting taxing policies concurrent with issuing said paper money, to redeeming its paper money in a timely fashion. The founder fathers must have been keenly aware of this. They had had decades of experiencing the difference between legal tender restrictions and the functioning of paper money per se. Certainly they knew that a non-legal tender paper money could be successfully created and sustained, and that such could work well in terms of financing government while maintaining low inflation rates and stability of nominal values.

This system continued through the Revolution. The Articles of Confederation allowed both individual States and the Continental Congress to issue their own tax-backed paper money. Beginning in 1775 the Continental Congress issued bills of credit—Continental Dollars—that depreciated to near zero and ceased to circulate after April 1781 (Bezanson 1951; Calomiris; Rockoff 14-42). Without the power to levy its own taxes, Congress under the Articles of Confederation could not credibly commit to redeeming its bills of credit. This structural flaw, along with the exigencies of wartime finance (short-term emergency spending exceeding near term tax-accessible resources) and doubts about the legitimacy of the Revolutionary government, would have been clearly apparent to the founding fathers as the source of the monetary troubles behind the Continental Dollar rather than just the emission of paper money per se. The Treaty of Paris resolved the issue of legitimacy. And one of the primary goals of the 1787 Constitutional Convention was to correct the structural flaw by giving the National Government an independent source of
revenue by granting it the direct power of taxation. This in turn would let Congress credibly commit to redeeming its bills of credit—potentially solving the National Government’s paper money problems.

Each of the 13 Colony/States also issued their own paper money during the Revolution that, while depreciating, held their value to a greater extent than did the Continental Dollar. Within three years of signing the Treaty of Paris, 7 of the 13 States—Pennsylvania, North Carolina, and South Carolina in 1785; Rhode Island, New York, New Jersey, and Georgia in 1786—returned to issuing their own paper money usable, as during the colonial period, to pay taxes levied and land mortgages held by the issuing State. In addition, State legislatures in Virginia, Maryland, and Massachusetts were debating whether or not to issue new bills of credit (Grubb 2003). The key difference between the colonial system and this latter State system, with the exceptions of Pennsylvania and South Carolina, was the extensive use of binding legal tender laws. In part this was caused by the exigencies of wartime finance and its immediate aftermath, namely wartime inflationary pressures caused by excessive emission of paper money relative to the taxing base and immediate post-war pressures to quickly service this war debt (Holton). Binding legal tender provisions were a kind of wartime (and its immediate aftermath) price-control device used to stem these pressures. War and its immediate aftermath were likely to cause some type of price-control exercise (Rockoff). The founder fathers would have been aware of this. They had for decades experienced the difference between the effects of binding legal tender restrictions and that of paper money emissions \textit{per se}. Once war and its immediate aftermath were over, a well-functioning non-legal tender paper money similar to the colonial monetary system surely could be successfully reinstated and sustained.

\textit{B. The Problem of Binding Legal Tender Laws versus Paper Money Emissions per se}

Legal tender provisions as discussed here are more than just the legal requirement that said monies be accepted for payment of all debts. If that were all there was to it then, for the most part, it would not cause serious problems as the monies would be priced in the market to account for the expected changes in their value. The legal-profession’s definition of “legal tender”—that a person can be compelled via legal sanctions to accept particular monies in payment of debt—is largely irrelevant in terms of economic impact as long as the said monies are competitively priced in the marketplace. Under such conditions the receiver is indifferent between accepting said money and any other market equivalent value (sans the minor issue of
transacting costs). The receiver would just proceed to the market and exchange his legal tender money for what was contracted for or really desired in the initial exchange with little loss of value.

Legal tender provisions have economic impact when the said tender is not competitively priced in the marketplace, typically due to government imposed price or exchange rate controls that artificially peg the value of the tender above its market value, i.e. a “binding legal tender.” Under such conditions a person legally compelled to receive the tender in payment of a debt receives less than its market equivalent in other goods or monies. As such, this person is no longer indifferent between receiving the tender and receiving payment in an alternative form or in what was initially contracted as payment—preferring the alternative to the legal tender. It is this binding legal tender problem that the founding fathers faced and understood as the “legal tender” issue. As such, throughout this paper, the term “legal tender” should be understood as referring exclusively to the condition of “binding legal tender.”

In the colonial and early Republican periods, legal tender provisions implied binding legal tender. Most Colony/State bills of credit had a par relationship to specie—either to Spanish dollars or pounds sterling, e.g. 1.33 Maryland pounds being par to 1 pound sterling (McCusker; Smith 1985). The par rate was the rate at which the issuing government typically committed to receiving its paper money in payment of its taxes. Without a legal tender provision, the rate of exchange in the marketplace could vary from the par rate, and thus little damage to contracting would occur in that real transaction values would be equivalently priced across different monies. If, however, the issuing government declared its paper money to be a legal tender for all debts, then the legal pressure was to accept it at its par rating to its specie counterpart. Because this legal expedient was typically used during wartime emergencies or inflationary periods, it meant being legally forced to accept paper money at considerably more than its market-determined value. In effect, this was a form of price or exchange rate control, and would typically drive foreign exchange (specie) out of circulation and stop long-term contracting in specie. That the Revolution could have been successfully fought and financed without some product price, currency price, and/or exchange rate control is unclear (Rockoff). Such controls could only function well in the short-run as stop-gap measures. They could not be successful in the long-run. The founding fathers likely knew this. Legal tender was understood as a separate issue from paper money emissions *per se* (Philoeunomos; Randolph).
The financial pressures in the immediate aftermath of the Revolution led several States to declare their new paper money to be a legal tender, i.e. enforcing an exchange rate price control, with Rhode Island being the most notorious (Bishop; Holton). Rhode Island will be used to illustrate important features of the post-Revolution finance problem. Like many States, Rhode Island had issued both paper money and debt (bonds) during the Revolution, well beyond the State’s near-term tax revenue capacity. The result was depreciation of both instruments. The risk of State-default on its bonds and the immediate post-war depression allowed some wealthy merchants to buy up these bonds at a price far below their face value, such as at 8 to 1. After having bought up these bonds at huge discounts, these same people in their position as, or influence over, State legislators were suspected of being the force behind getting the State to substantially raise taxes in specie so that the State could pay off the bonds at face value in specie. The proposed increase in specie taxes, in a depressed economy with little specie inflow due to trade disruptions, threatened to bankrupt many Rhode Island citizens and force them to sell off their property at fire-sale prices, thus further enriching those with resources and credit to buy.

Rhode Island voters stopped this “insider-trading” speculative scheme through defeating those involved at the polls. This was an example of the “excess” of democracy that some Federalists carped about. The new legislators ended the potential for any such future scheme through a new paper money emission in 1786. This emission was made a legal tender specifically for the purpose of forcing holders of Rhode Island war bonds to exchange them at face value for this new paper money (rather than allowing them to wait for a potential payoff in specie). As such, Rhode Island had honored its war bonds (though not in specie). Given that the fiscal capacity of the State government had not yet recovered, the taxing provisions in place were not sufficient to support this new paper money and so it also depreciated, though not necessary below the market price of the war bonds. Merchant-speculators in war bonds who were seeking a payoff in specie from the State so they could cover payments outside the State were suddenly forced to take the State’s inside paper money at par. In the marketplace they could not convert this paper money into specie at the same war bond face value, thus their ability to cover their outside money transactions were threatened.

Much of the rhetoric at the time of the Convention (and even to this day) that singled out Rhode Island as being the poster-child for irresponsible State management of paper money was written by the side
that had its insider-trading get-rich speculation scheme dashed by the “excess” of democracy in Rhode Island. Something similar to this scheme was likely tried in Massachusetts with Shay’s Rebellion being its major outcome. Certainly, setting the rhetoric aside, the founding fathers, at least some of them, knew and understood these problems. For example, at the Convention this knowledge is betrayed in a speech by Gouverneur Morris, Convention delegate from Pennsylvania, and very shortly after the Convention in a speech by Luther Martin, delegate from Maryland. They must have known that this was a short-term war finance problem and a legal tender issue, and not a problem of paper money *per se*. (Bishop; Farrand II, 307, III, 214-215; Grubb 2003, 1789-1790; Holton; Jensen III, 301-302; Perkins).

C. What the Founding Fathers Knew

The founding fathers knew the difference and made the distinction between binding legal tender laws and the emission of paper money *per se*. Most had lived and commercially prospered before the Revolution under colonial paper money regimes, and they would have been keenly aware of British regulation of said regimes regarding the distinction between legal tender laws and paper emissions *per se*. This distinction can also be readily seen in many of their statements. For example, William Paterson, Convention delegate from New Jersey, wrote in 1786, “An increase of paper money *if it be a tender*, will destroy what little credit is left…” Likewise, in a letter to George Mason, Convention delegate from Virginia, dated 15 May 1787, Richard Henry Lee wrote, “Knaves assure, and fools believe, that calling paper ‘money’ and making it a tender is the way to be rich and happy: thus the national mind is kept in continual disturbance by the intrigues of wicked men for fraudulent purposes, for speculative designs.” (Warren 551-552 [italics added]). In addition, Roger Sherman, Convention delegate from Connecticut, writing as far back as 1752, and Peyton Randolph, uncle and role model to Edmund Randolph, Convention delegate from Virginia, writing as far back as 1759, recognized the difference between binding legal tender laws and the emissions of paper money *per se* (Bradford 22, 166; Philoecunomos; Randolph).

Similarly, in a letter written 15 April 1787, just a month prior to the Constitutional Convention, Benjamin Franklin, Convention delegate from Pennsylvania, commented on Pennsylvania State paper money, “What you mention of our paper money, if you mean that of this State, Pennsylvania, is not well understood. It was made before my arrival [1785], and *not being a legal tender can do no injustice* to anybody nor does anyone here complain of it, though many are justly averse to an increase of the quantity
at this time,...” (Smyth IX, 561 [italics added]). Likewise, James Wilson, Convention delegate from Pennsylvania, in the ratification debates in Pennsylvania shortly after the Convention remarked, “It is true we have no tender law in Pennsylvania; but the moment you are conveyed across the Delaware [into New Jersey] you find it haunts your journey and follows close upon your heels. The paper [in New Jersey] passes commonly at twenty-five or thirty percent discount. How insecure is property!” (Jensen II, 500). The debate in the New Jersey Gazette on 30 January 1786 focused on the difference between a non-legal-tender and a binding-legal-tender paper money, the latter being bad. New Jersey nevertheless made its 1786 emission of paper money a legal tender. Finally, many of the anti-paper-money statements made by the Federalists before, during, and after the Convention focused not on inflation (the over-issue of paper money per se) but on the “fraud” and “injustice” caused when a paper money was made a binding legal tender (e.g. Farrand III, 350; Jensen III, 141, 402). In conclusion, the distinction between paper money emissions per se and making it a legal tender was clearly made and understood by the people of the time. It was when paper money was made a legal tender that serious problems arose, and not generally from the emission of paper money per se.

It is true that many of the founding fathers, both pro- and anti-federalists, had made anti-paper money statements or had anti-paper money sympathies both prior to and after the Convention, e.g. James Madison, George Mason, Robert Morris, Alexander Hamilton, etc. (Grubb 2003, 1781). This is not surprising given the debacle of the paper Continental Dollar issued by the National Congress during the Revolution and the continuing post-war efforts by the separate States to refinance their wartime debts and stem the post-war depression by reissuing paper money with the frequent use of legal tender provisions. But it is one thing to be against a current monetary policy, suffer angst over particular choices made by democratic legislatures and engage in debate over what the best current legislative policy should be, and quite another thing to make the leap to enshrining absolute monetary restrictions into the supreme law of a constitution. How did the founding fathers during the Convention make that leap from angst over specific legislative acts to making supreme law restricting the paper-money powers of government? Answering that question will be the task that occupies the bulk of what follows. The other important question—Why did they do it?—is more difficult to answer and a short analysis will be offered at the end.

II. The Beginnings—May 29 to July 26: The Virginia Plan, its Modifications, and Rivals
A. The Randolph Opening

The Convention began in earnest on May 29th with an address by Edmund Randolph of Virginia. Speaking for the Virginia delegation he presented, in order, the following: 1) the characteristics that a proper government ought to have, 2) the defects of the Articles of Confederation, 3) the present dangers being faced, and 4) a remedy in the form of a new plan of government embodied in 15 resolutions—traditionally known as the Virginia Plan (Farrand I, 15-28; III, 593-594). In assessing the defects of the confederation (item 2), Randolph praised its authors but noted that when they were crafting the Articles of Confederation [1776] certain problems had not been foreseen, one of these being that the “…the havoc of paper money had not been foreseen…”

Randolph’s choice of words is very telling in that it implies that the pervasive issuances of fiat paper money by colonial governments in the decades prior to the Revolution had not been problematic, at least not in the memory or experience of the Conventioneers. In other words, fiat paper money per se was not the problem. The difference between the pre-Revolutionary world of unproblematic paper money and the post-Independence havoc of paper money was obvious to most everyone. After 1775 with independence from British oversight and with the exigencies of financing the war and its immediate aftermath, each State issued more paper money than it could redeem in a timely fashion through taxes and (as a result) resorted to legal tender laws to support its value. The National Government had no direct power to tax and so had no credible way to commit to redeeming the paper money it issued. Thus, if legal-tender restrictions on paper money were re-imposed and the National Government given an independent source of taxation, then the havoc of paper money would be stopped. Randolph’s choice of words here implies that this understanding about what made paper money problematic may well have been common knowledge among the delegates.

When Randolph turned to his remedy, the Virginia Plan of government (item 4), he presented no specific resolution or words touching on paper money. However, Resolution 6 of the plan proposed to give the National Government new general powers that could potentially be applied to monetary issues. The Resolution stated, “…the National Legislature ought to be impowered…to legislate in all cases to which the separate States are incompetent, or in which the harmony of the United States may be interrupted by the exercise of individual Legislation; to negative all laws passed by the several States, contravening in the opinion of the National Legislature the articles of Union…” Deciding what monies could and could not be
used as a legal tender in exchange across States and with the National Government would appear to fall well within this new power to be given the National Legislature. However, as long as a State issuing paper money did not make it a legal tender for anything other than the payment of that State’s taxes, i.e. made it strictly an inside paper money within the issuing government’s jurisdiction, then such paper money emissions would appear to be untouchable by National Legislation. Such an inside paper money would not “contravene…the articles of Union” nor would the “harmony of the United States…be interrupted by this exercise of individual [State] Legislation…” In essence, this can be interpreted as potentially restoring one pillar of British monetary oversight of the colonies, namely that individual States (colonies) are allowed to issue their own individual paper monies as long as it is not made a legal tender. That Resolution 6 of the Virginia Plan could have been interpreted as a potential outright or even conditional ban on State paper money emissions per se is doubtful.5

Finally, Resolution 6 would also appear to give the National Legislature the power to issue its own national paper currency. Given that one of the new powers to be given the National Legislature was the ability to directly tax and collect revenue independent of the States (perhaps the single most important new power sought), the problem of the inability of the National Government to redeem its paper money issuances in a timely fashion through national taxation was removed. In other words, the key structural problem that led to the Continental Dollar fiasco during the Revolution would be solved. In essence, the new powers embodied in the Virginia Plan can be interpreted as potentially restoring part of another pillar of British monetary oversight of the colonies, namely that fiat paper money (on the national level) should be adequately backed by future taxes.

B. In the Shadows—The Pinckney Plan

At the end of the same day that Randolph presented the Virginia Plan, Charles Pinckney of South Carolina read his plan for a new national government to the Convention. The speech Pinckney made and the plan of government he laid before the Convention that day were not recorded by anyone, though James Madison of Virginia wrote that along with the Virginia Plan, Pinckney’s Plan was “referred to the Committee of the whole [the entire Convention]…” And Robert Yates of New York wrote that Pinckney “…confessed that it [his plan] was grounded on the same principle as of the above resolutions [the Virginia Plan].” (Farrand I, 16, 23, 24). Over the next two months the Convention debated the details of the
Virginia Plan, using it as the edifice for constructing a new plan of government. The Pinckney Plan disappeared into the shadows. As a distinct plan, it was never directly debated by the Convention. However, given that the Pinckney Plan appears to re-emerge after July 26th in the Committee of Detail (see below) and have an impact on that Committee’s reshaping of the amended Virginia Plan on monetary issues, it is important to reconstruct Pinckney’s May 29th speech and Plan with regard to monetary powers.

Shortly after the Convention concluded on September 17th Pinckney published a pamphlet purporting to be the speech he delivered or intended to deliver at the opening of the Convention. How much of this material comprises additions and deletions after the fact of his address on May 29th is hard to say (Farrand III, 106-123, 595-609). With that caveat in mind, Pinckney argued that the National Congress should have the power both to revise and negate any State laws that appear to the National Congress as improper. Pinckney wrote, “The proceedings of the States which merely respect their local concerns, will always be passed [by the national congress] as matters of form, and objections only arise where they shall endeavor to contravene the Federal Authority.” (Farrand III, 112-115). While this statement gives broader power over State laws than does the Virginia Plan, with regard to monetary issues it would appear to lead to the same outcome as the Virginia Plan. The National Government could not stop States from issuing a non-legal-tender inside paper money because that would be a purely local concern, but the National Government could stop States from making their paper money legal tender particularly with regard to it being used in outside-money transactions (payments across-States and to the National Treasury).

Pinckney continued on to write that the National Government should have, “The exclusive right of…determining in what species of money the common Treasury shall be supplied… If you allow the States to…emit Bills of Credit, they will force you to take them in payment for Federal Taxes and Duties,…and though, Congress may determine, that nothing but Specie shall be received in payment of Federal Taxes or Duties, yet, while the States retain the rights they at present possess, they will always have it in their power, if not totally to defeat, yet very much to retard and confuse the collection of Federal Revenues. … There can be no other mode of ascertaining this, than to give to the United States the exclusive right of coining, and determining in what manner the Federal Taxes shall be paid.” (Farrand III, 117-118). This statement again argues that the National Government should have power over legal tender
issues, namely to prevent States from making their paper money a legal tender regarding payments to the National Government.

In the second sentence quoted above Pinckney would appear also to be arguing that there ought to be an absolute ban, or that the National Government ought to have the power to ban, State emissions of paper money *per se*. However, a closer reading of the key elements of the passage suggests that that is not the case, namely “If you allow the States to…emit Bills of Credit, they will force you to take them…[as long as] the States retain the rights they at present possess…” The only relevant other “right” Pinckney could be referring to at the end of this passage (he explicitly mentions emitting bills of credit at the outset of the passage) is a State’s right to declare its paper money a legal tender. It is the State’s legal tender power that is the source of mischief not the emission of paper money *per se*. This interpretation is also consistent with why Pinckney ends his argument by proposing that the National Government be given only the power to determine in what money “Federal Taxes” should be paid and makes no proposal to ban State emission of paper money. This is also the interpretation used in the accepted reconstruction of Pinckney’s Plan of government submitted on May 29th as derived from this speech/pamphlet (Farrand III, 604-607).

However, in the Pinckney Plan that was among the papers of the Committee of Detail (July 26-Aug 6) there is no mention of any National Government power to determine “in what manner Federal Taxes shall be paid” or anything related explicitly to paper money or legal tender laws. Only the following related clause appears: “Each State retains its Rights not expressly delegated—But no Bill of the Legislature of any State shall become a law till it shall have been laid before S. &. H. D. in C. [Senate and House of Delegates in Congress] assembled and received their Approbation.” (Farrand II, 134-137). And a clause similar to this in the Virginia Plan was voted removed by the Convention prior to turning their deliberations over to the Committee of Detail (see below).

**C. Debating and Amending the Virginia Plan—May 30th through July 26th**

From May 30th through July 26th the Committee of the Whole (the entire Convention) debated and amended the Virginia Plan, including considering or hearing rival plans such as the New Jersey Plan and the Hamilton Plan. Monetary powers, while not directly addressed, remained one of the sub-texts of the debate and seemingly played some part in defining the path leading toward a total constitutional ban on government-issued paper money.
On May 31st Resolution 6 of the Virginia Plan was debated. Regarding the clause “the National Legislature ought to be impowered…to legislate in all cases to which the separate States are incompetent…” Pinckney and John Rutledge of South Carolina “objected to the vagueness of the term incompetent, and …[wanted to] see an exact enumeration of the powers comprehended by this definition.” Randolph “disclaimed any intention to give indefinite powers to the national Legislature, declaring that he was entirely opposed to such an inroad on State jurisdictions…” James Wilson of Pennsylvania “observed that it would be impossible to enumerate the powers which the federal Legislature ought to have.” Finally, Madison “said that he had brought with him into the Convention a strong bias in favor of an enumeration and definition of powers necessary to be exercised by the national Legislature; but had also brought doubts concerning its practicability.” 6 This phrase was then passed unaltered 10 to 1 (votes being recorded by State and not by individual delegate). The next two phrases of Resolution 6 (that the National Legislature should have the power to legislate where the harmony of the U.S. may be interrupted by the exercise of individual State legislation and to negate all laws by the States contravening the articles of Union) were agreed to without debate or dissent (Farrand I, 53-54, 60-61). As argued above, while not explicitly mentioned at the Convention, these powers could be construed to give the National Government power over defining what could and could not be declared a legal tender, but it probably did not give the National Government power to ban State emissions of non-legal tender paper money.

What is interesting about this debate is that while no list of enumerated powers were offered or debated by the Convention before the Convention’s deliberations were handed on July 26th to the Committee of Detail to hammer out a draft constitution, and while the Convention did not charge the Committee with enumerating any powers, the draft constitution produced by this Committee nevertheless contained a list of specific enumerated powers including monetary powers. Interestingly, the three Committee members most responsible for writing out these enumerated powers, including the monetary powers, were Rutledge, Wilson, and Randolph.

State paper money is first explicitly mentioned in the Convention on June 6th by George Mason of Virginia in the debate over whether the National Legislature should be elected by the people or by the State legislatures with Mason being strongly in favor of election by the people. 7 Mason argued that “…there was a better chance for proper elections by the people,…than by the State Legislatures. Paper money had been
issued by the latter when the former were against it. Was it to be supposed that the State Legislatures then
would not send to the National legislature patrons of such projects if the choice depended on them.”
(Farrand I, 134). By contrast, Pinckney favored election by the State Legislatures rather than by the people.
Pinckney “differed from gentlemen who thought that a choice by the people would be a better guard against
bad measures, than by the Legislatures. A majority of the people in S. Carolina were notoriously for paper
money as a legal tender; the Legislature had refused to make it a legal tender. The reason was that the latter
had some sense of character…” (Farrand I, 137). Finally, in the continuation of this debate the next day
Elbridge Gerry of Massachusetts, who also favored election by the State legislatures, insisted “that the
commercial & monied interests would be more secure in the hands of the State Legislatures, than of the
people at large. The former have more sense of character, and will be restrained by that from injustice. The
people are for paper money when the Legislatures are against it. In Massachusetts the County Conventions
had declared a wish for a depreciating paper that would sink itself.” (Farrand I, 154-155).

This initial explicit introduction of State paper money into the Convention debates illustrates two
argument-transformation themes in the rhetoric used at the Convention that will continue and escalate in
intensity over the remainder of the Convention. The first argument-transformation theme is the
equivocation or conflation of paper money emissions per se with legal tender powers. While Pinckney
makes a clear distinction between State paper money as a legal tender and State paper money per se
(suggesting that its is the former and not the latter that is bad), his statement will be (sans one other) the last
time this distinction will be made at the Convention. Instead, as illustrated by Mason’s and Gerry’s
comments, the subsequent comments on State monetary powers will undergo definition creep whereby
emitting paper money and making paper money a legal tender will become synonymous. The rhetoric will
then slide into just referencing the emission of paper money per se, rather than its legal tender designation,
forcing it to take on the entire mantel of what is evil about State monetary powers. The second argument
transformation theme is that in all subsequent comments on paper money, also illustrated here by Mason’s
and Gerry’s comments, there is a presumption usually without any explanation that paper money per se is
bad, rather than just the distinct power of making it a legal tender. The power to emit paper money slides
into becoming a rhetorical code phrase for evil.
On June 8th Pinckney and Madison proposed strengthening Resolution 6 of the Virginia Plan so that the National Legislature would have the power to negate any state law the National Legislature thought was improper rather than just those contravening the articles of union. Though not directly mentioned, this change would clearly give the National Legislature the power to stop State emissions of paper money if it so wanted. In the ensuing debate, Gerry argued that he “could not see the extent of such a power, and was against every power that was not necessary. … [But] He had no objection to authorize a negative to paper money and similar measures.” Roger Sherman of Connecticut wanted the cases enumerated where a negative could be applied. However, Wilson again stated, “A definition of the cases in which the Negative should be exercised, is impracticable.” John Dickenson of Delaware reiterated Wilson’s point. Others thought it would become a tool whereby the large States would tyrannize the small States. The Convention voted the change down 7 to 3. (Farrand I, 162-168).

Gerry’s comment in the above debate is the only time at the Convention prior to submitting the Convention’s deliberations to the Committee of Detail (July 26th) that anyone suggested a specific narrowly enumerated power that the National Government should possess, namely the power to stop State emissions of paper money. Gerry’s suggestion was also not taken up, commented on, or further debated before July 26th. His comment also illustrates the ease with which the definitional slide was made at the Convention from legal tender laws being the problem to branding all State paper money as the problem.

On June 15th William Paterson of New Jersey presented what is typically referred to as the New Jersey Plan to the Convention. Largely designed as a “small” State alternative to the “large” States’ views on representation in the National Government, it contained nothing specifically or indirectly that would bear on monetary powers, certainly nothing beyond that in the Virginia Plan. Hamilton’s Plan also contained nothing specifically or indirectly that would be a problem on monetary powers, certainly nothing beyond that in the Virginia Plan. Hamilton did take the opportunity in his speech to join the chorus of rhetoricians using the emission of paper money per se as an illustration of an evil that had to be stopped. In lauding the British Constitution over the proposed method of electing a U.S. Senate, Hamilton said, “Their house of Lords is a most noble institution. … They form a permanent barrier against every pernicious innovation,…
No temporary Senate will have firmness enough to answer the purpose. The Senate of Maryland which seems to be so much appealed to, has not yet been sufficiently tried. Had the people been unanimous & eager, in the late appeal to them on the subject of a paper emission they would have yielded to the torrent.” (Farrand I, 282-311, III, 617-630).

In a long speech on June 19th Madison argued against the New Jersey Plan claiming that the Plan would not “...prevent trespasses of the States on each other...[that] He considered the emissions of paper money as also aggressions. The States relatively to one another being each of them either Debtor or Creditor; the Creditor States must suffer unjustly from every emission by the debtor States. We have seen retaliating acts on this subject which threatened danger not to the harmony only, but the tranquility of the Union.” (Farrand I, 317-318). Again the two argument-transformation themes appear in Madison’s speech, namely, the problem created by legal tender laws is redefined as being created by the emission of paper money \textit{per se} and that this in and of itself is evil.

On July 16th the Convention revisited the clause of Resolution 6 of the amended Virginia Plan giving the National Legislature the power “…to legislate in all cases to which the separate States are incompetent; or in which the harmony of the U.S. may be interrupted by the exercise of individual legislation…” The Convention again considered the vagueness of this power and whether it should be explicitly enumerated. Pierce Butler of South Carolina called for “…some explanation of the extent of this power; particularly of the word \textit{incompetent}. The vagueness of the term rendered it impossible for any precise judgment to be formed.” Nathaniel Gorham of Massachusetts argued, “We are now establishing general principles, to be extended hereafter into details which will be precise & explicit.” Rutledge “…moved that the clause should be committed...[so] a specification of the powers comprised in the general term, might be reported.” The vote failed, 5 in favor versus 5 against. While the Convention appeared to vote against enumerating these powers, the Committee of Detail (July 26-August 6), on which Rutledge participated, took it upon itself to so enumerate them. (Farrand II, 17).

On July 17th the Convention again took up this clause in Resolution 6. This time it was Sherman who “observed that it would be difficult to draw the line between the powers of the General Legislatures, and those to be left to the States...” He proposed that the clause be amended to rule out national legislation that would “…interfere with the Government of the individual States in any matters of internal police
which respect the Government of such States only, and wherein the General welfare of the United States is not concerned.” Sherman also offered an enumeration of the powers to be given the National Legislature. Gouverneur Morris of Pennsylvania opposed this wording. He argued that “The internal police, as it would be called & understood by the States ought to be infringed in many cases, as in the case of paper money & other tricks by which Citizens of other States may be affected.” (Farrand II, 25-26). Notice here that Morris’ rhetoric has again completely muddled the lines between State paper money emissions per se and the power to declare them a legal tender, making the emission of paper money per se bear the entire burden of the problems cause by legal tender laws.

Sherman’s proposal was voted down, 8 to 2, and the original clause of Resolution 6, with some slight rewording, was passed as is (without any enumeration of powers), 6 to 4. (Farrand II, 25-26). The debate over this clause is interesting for monetary powers. The strict construction of the clause would appear to give the National Legislature no power to stop State emissions of paper money per se, but would appear only to give the National Legislature the power to stop States from declaring said money a legal tender in trans-State or national transactions. However, Morris’ statement—“The internal police…[of] the States ought to be infringed in many cases, as in the case of paper money & other tricks by which Citizens of other States may be affected” (Farrand II, 25-26)—would appear to construe the clause more broadly, namely to include national prohibition of even a purely inside State paper money. Basically Morris’ statement seems to be claiming that anything whatsoever that will possibly affect a citizen of another State falls under the power of national prohibition.

Yet, later that same day (July 17th), Morris strongly opposed giving the National Legislature the power to veto the “…laws passed by the several States…” (Farrand II, 27-28). This action contradicts the seemingly broad-power interpretation of his prior statement which he used when rejecting Sherman’s motion. Considering all of Morris’ statements together would appear to yield one consistent and narrow concern, namely getting the power to prevent State emission of paper money per se. In a letter to Timothy Pickering, 22 December 1814, Morris more-or-less admitted to such, saying that he had “little recollection” of the details of the Convention, but that “Propositions to countenance the issue of paper money, and the consequent violation of contracts, must have met with all the opposition I could make.” (Farrand III, 419-420). Even years after the Convention, Morris continues to muddle the lines between paper money per se
and legal tender laws. The “consequent violation of contract” would only occur if paper money was made a legal tender—again illustrating the slide of logic and definition creep intended to make the emission of paper money \textit{per se} bear the entire burden of the problems cause by legal tender laws.

On July 17th the Convention also revisited the clause of Resolution 6 of the amended Virginia Plan giving the National Legislature the power “To negative all laws passed by the several States contravening in the opinion of the National Legislature the articles of Union, or any treaties subsisting under the authority of ye Union.” This clause, agreed to on May 31st without debate or dissent, now excited significant opposition. It was deleted by a vote of 7 to 3. (Farrand II, 27-28). Removal of this power would make it more difficult for the National Government using the power in the prior clause in Resolution 6 (considered immediately above) to directly stop a State from issuing a legal tender paper money.

On July 21st while debating whether the National Judiciary along with the executive should have the power to revise or veto laws passed by the National Legislature, Morris continued the drumbeat of the evils of legislative emissions of paper money \textit{per se}. He said, “Emissions of paper money, largesses to the people—a remission of debts and similar measures, will at sometimes be popular, and will be pushed for that reason… The press is indeed a great means of diminishing the evil, yet it is found to be unable to prevent it altogether.” (Farrand II, 76). Morris’ rhetoric here erroneously identifies paper money emissions \textit{per se} with “largesses to the public” and “a remission of debts.” But this would only typically be the case for paper money under a legal tender law and not for paper money \textit{per se} (Holton). And so again the two argument-transformation themes appears, namely, the problem created by legal tender laws is redefined as being created by the emission of paper money \textit{per se} and that this in and of itself is evil.

On July 26th the Convention’s deliberations were submitted to a Committee of Detail to craft a draft constitution. Up to this point no explicit or direct proposals regarding monetary powers had been made. At best, what remained of Resolution 6 of the Virginia Plan potentially gave the National Government the power to determine what monies could be legal tender for cross-State trade and in transactions with the National Government, but as strictly constructed it probably could not be construed as giving the National Government power to prohibit State paper money emissions \textit{per se}, i.e. emissions that were not a legal lender. However, the Convention rhetoric on paper money, such as that used by Mason, Madison, Hamilton, and Morris had continuously conflated paper money with legal tender laws thus
forcing the emission of paper money *per se* to bear the entire burden of the problems caused by legal tender laws. This rhetoric set the stage for the Committee of Detail to leap for the first time at the Convention to incorporating explicit clauses into the Constitution dealing with paper money emission *per se*, as opposed to clauses dealing only with legal tender laws. Convention rhetoric, however, may not have been enough to achieve this leap. Whether by conspiratorial craft or lucky accident, a timely demonstration of the “evils” of State paper money was displayed in mid-July in Philadelphia for the delegates to witness.

### III. Paper-Money-Riot Interlude?

A riot over Pennsylvania State paper money broke out in Philadelphia in mid-July. The *Pennsylvania Herald and General Advertiser* described two incidents—the first on July 14th:

A correspondent observes that the speculations of a few artful people have been frequently found extremely detrimental to the public; and no class is too low; that it cannot by a bold combination, accomplish its object. The hucksters lately came to a resolution not to receive the copper-currency at less than 24 pieces for a shilling; but this depreciation was not publicly divulged till they had passed all their stock of half-pence at the former value. There are others who derive a livelihood from the exchange between the current mediums, that without any regard to the relative value, keep it in constant fluctuation, and, from day to day, pronounce upon the rate at which paper-money shall be taken for specie. The first instance is a reproach to the policy and morals of the state, for government should never leave it in the power of one part of the citizens to take advantage of the innocent ignorance of another; and the second instance is a reproach to the folly and weakness of those people, who will passively adopt the suggestions of interested men, instead of exercising their own judgment to show, that the security of the paper money is of an improving rather than a decaying nature.

And the second on July 21st:

A correspondent remarks that the panic which prevailed on Saturday last [July 14th], respecting the paper-money of this state has not been more distressing to the poor, than astonishing to the intelligent part of the community. Many causes have been assigned for the sudden event, some grounded on mercantile negotiations, that never existed, and others drawn from mistaken or perverted interpretation of an expression which lately dropt from an eminent law character—but not one can stand a rational investigation.

Convention delegates were certainly aware of the goings on and they took away a darker view of the event than that painted in the newspaper. For example, Madison related the events to Thomas Jefferson, who was in Paris, in a letter dated 18 July 1787 (Smith 1995, I, 484):

The paper money here ceased to circulate very suddenly a few days ago. … The entire stagnation is said to have proceeded from a combination of a few people with whom the Country people deal on market days against receiving it. The consequence was that it was refused in the market, and great distress brought on the poorer Citizens. Some of the latter began in turn to form combinations of a more serious nature in order to take revenge on the supposed authors of the stagnation. The timely interposition of some influential characters prevented a riot, and prevailed on the persons who were opposed to the paper, to publish their willingness to receive it. This has stifled the popular rage, and got the paper into circulation again. … Nothing but evil springs from
this imaginary money whenever it is tried, and yet the appetite for it, when it has not been tried, continues to be felt.

An interesting question ripe for further research is whether this paper-money riot was in some way engineered by Morris’ “monied interest” and/or the Bank of North America in an effort to help pave the way for an outright constitutional ban on paper money emissions. In assessing the paper-money riot, Allan Nevins (522) concluded that the bank was involved, “In July of 1787, by concerted action, the banks and markets of Philadelphia ceased to accept them [Pennsylvania State paper money].” The timing of the stoppage by itself is suspicious. The paper-money riot took place shortly after Morris, a chief operating advisor of the Bank of North America, returned to the Convention after a lengthy absence. He had been away in New York from the end of May through June, returning to the Convention in Philadelphia on July 2nd. The paper-money riot occurred right before the Convention decided to revisit Resolution 6 of the Virginia Plan on the extensiveness of national powers over State laws, and right before Morris began his drumbeat on the evils of paper money in his speeches from July 17th through July 21st. And it occurred a little over a week before the Convention’s deliberations were turned over to the Committee of Detail on which Wilson, a member of the board of the Bank of North America, would be a key member. Otherwise, Pennsylvania State paper money had remained relatively stable over the long-run as measured by its relatively constant (stationary with no trend) exchange rate to pounds sterling from 1784 through 1790 (Bezanson 1936, 346; Grubb 2003, 1786; Grubb 2004a). Finally, it would probably be difficult to find a short-run combination of speculators in Philadelphia with a tight enough control over specie and money exchange to accomplish such a concerted stoppage of paper-money exchange that didn’t somehow involve the Bank of North America. In any event, whether by conspiratorial craft or lucky accident, this heretofore overlooked episode may have been an important contributor to the radical transformation in constitutional monetary powers about to be undertaken at the Convention.

IV. The Committee of Detail—July 27 to August 6: The Initial Restructuring of Monetary Powers

On July 26th the Convention referred the Virginia Plan as amended by the Convention to that point, as well as the non-debated Pinckney Plan that was submitted on May 29th and the New Jersey Plan offered on June 15th, to a Committee of Detail to craft a draft constitution. This Committee consisted of Oliver Ellsworth of Connecticut, Gorham, Randolph, Rutledge, and Wilson. (Farrand II, 85, 97-98, 128-137). Five working drafts attributed to the Committee have survived—four written by Wilson, with the last
containing emendations by Rutledge, and one written by Randolph with emendations by Rutledge.

Working backwards from the final product reported by the Committee to the Convention on August 6th, Wilson’s last working draft (with emendations by Rutledge) appears to be the principle penultimate draft of the Committee (Farrand II, 163-175, 177-189; Meigs 316-324).

Where Randolph’s draft fits within the first three Wilson drafts is hard to say, they overlap in some ways but not in others (Farrand II, 137-163; Meigs 316-324). Randolph’s draft is more an extensive yet sketchy outline than an articulated draft. While the Convention had seemingly voted against an enumeration of National Government powers (see above), the Committee took it upon itself to incorporate extensive lists of specific enumerated powers, including monetary powers in their drafts. Randolph’s draft, unaltered by Rutledge, and the first two Wilson drafts, however, say nothing prescriptive or proscriptive about the power to emit paper money or about determining what monies may be made a legal tender either by the National Government or by the State Governments.

Wilson’s third draft includes for the first time in the constitution-creation process an explicit clause enumerating a monetary power, namely a limited power to restrict legal tender—“The Legislature of U.S. shall have the exclusive Power…of determining in what Specie of Money the public Treasury shall be supplied.” (Farrand II, 158-159). Nothing else, however, is said prescriptive or proscriptive in this draft about the power to emit paper money or about determining what monies may be a legal tender within State jurisdictions. This power as explicitly enumerated here by Wilson was not mentioned in the records of the Convention. But as argued above, it clearly seems to be one of the powers within the scope of the amended Resolution 6 of the Virginia Plan granting the National Legislature the power to legislate “…in all Cases for the general Interests of the Union, and also in those Cases to which the States are separately incompetent, or in which the Harmony of the United States may be interrupted by the Exercise of individual Legislation.” While not appearing in the Pinckney Plan that was given to the Committee of Detail, the wording of Wilson’s legal tender clause closely follows the wording in Pinckney’s speech to the Convention on May 29th—as published after the Convention (Farrand III, 118).

At this juncture of the Committee’s efforts, the structure of the constitutional monetary powers being crafted were the closest to replicating the colonial monetary system as they ever would be. Under the Currency Acts of 1751 and 1764, the British Crown had allowed the colonies to emit paper money as long
as they taxed sufficiently to redeem said money in a timely fashion and as long as they did not make said money a legal tender. In Wilson’s third draft constitution in the Committee of Detail both the National Government and the States Governments still retained the right, as under the *Articles of Confederation*, to emit paper money. The National Government had been given an independent power to directly tax, thus allowing it to credibly commit to redeeming its’ paper money, a power which it had not had under the *Articles of Confederation*, thus solving the key structural problem underlying the collapse of the Continental Dollar. And Wilson gave the National Government the power to determine what could be legal tender for National Government transactions which almost replicated the effective application of the British Crown’s legal tender restrictions on the colonies. This power, in effect, used the market for exchanging money in trans-State or National transactions to discipline State Government paper money emissions.

From this point, the Convention embarked on a path leading to a radical departure from the colonial system. In Wilson’s last (fourth) working draft, he dropped the legal tender restriction clause from his third draft, namely dropped the phrase “The Legislature of U.S. shall have the exclusive Power...of determining in what Specie of Money the public Treasury shall be supplied,” and substituted in its place the clause, with Rutledge reordering the sequence of words slightly, “No State shall...without the Consent of the Legislature of the United States emit Bills of Credit.” In addition, the National Legislature’s implied power to emit bills of credit in the third draft (which had been included as part of the powers carried over from the *Articles of Confederation*) is now, in Wilson’s fourth draft, made one of the separate explicit enumerated powers given to the National Legislature (Farrand II, 168-169). No statement about legal tender powers at any level of government, however, was included in this last draft. Perhaps Wilson reasoned that if Congress had the power to ban States from emitting paper money that this resolved the problem of determining what monies could be a legal tender for National Government transactions—the former power encompassing the latter power. But this change was also a radical step in that it gave Congress, for the first time, the power to ban States from issuing even a non-legal-tender inside paper money. This change would appear to be a clear step beyond the principles laid out so far by the Convention regarding national powers not being allowed to interfere in matters purely internal to a State.

Besides emendating Wilson’s last working draft, Rutledge also added comments to Randolph’s draft. In a margin note to Randolph’s enumerated powers given to the National Government “To regulate
coining” Rutledge wrote “no State to be perd. in future to emit Paper Bills of Credit witht. The App: of the Natl. Legisle nor to make any Thing but Specie a Tender in paymt of debts” (Farrand II, 144). Given that the second half of this clause does not appear in Wilson’s last working draft which Rutledge had also emendated but does appear in the Committee’s final draft submitted to the Convention on August 6th, it seems likely that Rutledge added this note to Randolph’s draft near the very end of the Committee’s deliberations. As argued above, the true monetary problem was the legal tender issue. Perhaps Rutledge reasoned that if Congress only had Wilson’s power to ban State paper money that that would not necessarily solve the legal tender problem. States might declare something else to be a legal tender, such as bonds, tobacco contracts, or land deeds. If outside money was always to be specie, then States had to be prevented from making “any Thing” but specie a legal tender.

The final draft constitution submitted by the Committee to the Convention on August 6th gave the National Legislature the explicit enumerated power to “…emit bills on credit…”, and an explicit enumerated power over State paper money and legal tender laws, i.e. stating that “No State, without the consent of the Legislature of the United States, shall emit bills of credit, or make any thing but specie a tender in payment of debts…” (Farrand III, 182, 187; Meigs 134-135, 180-182, 311). By explicitly enumerating individual monetary powers, the Committee was forcing the Convention to deal up or down with just these separate powers, as opposed to dealing with monetary powers that were incorporated with other powers under a broad principle as the Convention had done up to this point. While the Convention may have been reluctant to give the National Government power over matters purely internal to the States, they might be willing to grant such a power narrowly over State paper money, even when said paper money was not made a legal tender. What is interesting is that it will be Wilson himself, along with his Bank of North America protégé Morris, who will lead the attack on these narrowly enumerated monetary clauses, the clauses that Wilson was the first to draft out, in order to narrow their scope even further.

V. The End Game—August 6 to 28: The Absolute Constitutional Proscription of Monetary Powers

A. The Abolition Prohibition on Paper Money Issued by the National Government

From the initial Virginia Plan presented at the beginning of the Convention through all the Convention’s deliberations given to the Committee of Detail, the National Legislature was designed to have all the rights and powers it possessed under the Articles of Confederation plus some new and enlarged
powers. The Committee of Detail drafted a list of these new and enlarged powers. In Wilson’s last draft, but not before, this list included the power to “emit bills on the credit of the United States.” (Farrand I, 21; II, 131, 142-144, 158-159, 167-169, 181-183). Under the *Articles of Confederation*, Congress had exercised the power to emit bills of credit. Why the Committee of Detail took it upon itself in its last draft, and for the first time in the constitution-revision process, to put this one already existing “old” power on the list of specifically enumerated “new and enlarged” powers of the Federal Government is unclear. One outcome of doing this became clear within a few days. By isolating this one “old” power from the other exiting “old” powers, it became easier to attack, modify, and expunge.

With Congress being granted the new power to directly tax, the problem under the *Articles of Confederation* of the Federal Government not being able to credibly redeem its paper money with future taxes, the key structural problem that distinguished the well-working colonial monetary system from the Continental Dollar disaster, had been removed. Under the draft of the new constitution offered by the Committee of Detail, paper money issued by the Federal Government, if not made a legal tender, should have worked as well as it had in the late colonial period. However, within ten days of receiving this draft constitution, the Convention decided that under absolutely no circumstances should the Federal Government have the power to issue paper money.

The attack on this power was led by Gouverneur Morris. The first two attacks were indirect, with the first presented on August 15th during the debate over how easily an executive veto of Congressional legislation could be overridden. Morris argued that Congress should not have an ability to override an executive veto and, if that was not agreeable, requiring a 3/4 vote rather than the proposed 2/3 vote of Congress to override an executive veto would be preferable. Madison recorded Morris as having dwelt on the importance of public Credit, and the difficulty of supporting it without some strong barrier against the instability of legislative Assemblies. … The legislature will contrive to soften down the President. He recited the history of paper emissions, and the perseverance of the legislative assemblies in repeating them, with all the distressing effects of such measures before their eyes. Were the National legislature formed, and a war was now to break out, this ruinous expedient would be again resorted to, if not guarded against. (Farrand II, 299).

The Convention voted for a 3/4 rule over the initially proposed 2/3 rule. (Farrand II, 301).

What is interesting about Morris’ argument here is that he explicitly links the ruinous problems of paper money to “war.” Was he admitting that paper money issued by the Federal Government under the new constitution would not be a problem during peacetime? Having given the Federal Government the new
power to directly tax, and so the power to credibly commit to redeeming through taxation the paper money it issued, a Federally-issued inside paper money should have worked as well as the inside paper money issued by separate colonies during the late colonial period. Morris would have known and understood this idea and he would have known that the other Convention delegates would have known and understood this as well. But Morris also knew that the Convention delegates were well aware of the “ruinous” effects of Congress’ wartime issue of the paper Continental Dollar. The exigencies of war would typically require issuing more bills of credit to pay than what could be credibly redeemed in the near future through taxation. Wartime inflation and price controls would be the likely result (Rockoff). Whether wartime inflation could have been avoided, regardless of the monetary powers of the Federal Government, was not considered. However, given that the debate was not about distinguishing between wartime versus peacetime powers, it would appear that Morris was really trying to link the disastrous wartime inflation of the Continental Dollar already well planted in the minds of every delegate with the “evils” of paper money per se, thereby chipping away at any notion that paper money might be managed well by Congress in the future even given the new constitutional powers to tax.

The second indirect attack came early on August 16th when the Convention took up debating whether the Federal Government should have the power to tax all trade, both exports and imports, as opposed to just the power to tax imports. Among his arguments in favor of taxing exports, Morris asserted that “Taxes on exports are a necessary source of revenue. For a long time the people of America will not have money to pay direct taxes. Seize and sell their effects and you push them into Revolts—.” The Convention, however, for other political reasons voted eventually not to allow the Federal Government to tax exports. (Farrand II, 307, 374, 657).

While not directly addressing governmental monetary powers, Morris’ comments here say a lot about what he anticipated those powers to be and what the monetary course of events would be under those powers. Why would the “people of America…not have money to pay direct taxes” to the Federal Government? If the Federal Government issued an inside paper money, it would have to accept that paper money in payment of its taxes. Having issued said inside money the people of America would have little problem getting said money to pay Federal taxes because unlike outside money (specie), it would seldom exit the country. If, however, the Federal Government did not issue or was prohibited from issuing an
inside paper money, then taxes would have to be paid in outside money, namely specie. For the most part, specie flowed into the economy from the trade surpluses with the Caribbean and flowed out through the trade deficits with Europe. Given the exigencies of trade, short-run imbalances always occurred. While periods of specie surplus would not create a problem for paying Federal taxes, periods of specie scarcity under a system where the Federal government did not or could not issue an inside paper money must be what Morris was referring to when he talked about people not having “money to pay direct taxes.” Morris also seemed to be expecting that periodic specie scarcity would be a prevalent condition in the near future (Holton). Because exports are typically paid for with specie, taxing exports would give the Federal Government direct access to specie as tax payments, whereas society at large might not have specie. Why Morris was assuming here that the Federal Government would need a lot of specie and so needed a direct source of specie tax revenue (as opposed to exchanging its inside paper money in the marketplace for specie when it needed to spend an outside money) will be addressed later.

Another interesting aspect of Morris’ comment here is that it comes close to confessing what the true underlying problem was regarding the late 1786 and early 1787 rebellion in Massachusetts, called Shay’s Rebellion, that so affected the delegates at the Convention—the most likely reference to “Revolts” in the above quote. If you suddenly eliminate or fail to issue an inside paper money and then require the public to pay taxes in specie, as Massachusetts did shortly after the Revolution, and if short-run shifts in external trade cause a period of specie scarcity, then some people will be tax delinquents and forced into bankruptcy. Government will have to confiscate and sell the tax delinquents’ property at auction to collect the tax arrears and pay off other creditors. Such distressed property auctions when specie is scarce leads to substantially lower than average prices for the tax delinquents’ property. Those with wealth scoop up this property as fire-sale bargains. Given that those who got the fire-sale bargains may have also been or were suspected of being involved in engineering the passage of such money-tax policies in the first place, a sense of injustice and hence revolt was the outcome—largely taking the form of trying to stop court actions against debtors. This was the essence of Shay’s Rebellion, as well as the Whiskey Rebellion in western Pennsylvania in 1796. And stopping something like this was what lay behind the Rhode Island emission of paper money in 1786 (Bishop; Bouton; Grubb 2003, 1789-1790; Holton). Federalist rhetoric, uncritically used to write most histories of this period, successfully (though erroneously) painted these episodes as
examples of the excess of democracy where maddening outbreaks of populous rage for an inflationary paper money occurred in order that the many (poor debtors) could cheat the few (wealthy creditors). Whereas in almost all these episodes it may well have been a few wealthy creditors who were out to use their power in the government to alter the rules and so confiscate more wealth from the poor. Luther Martin, a delegate to the Convention from Maryland, made similar observations (Farrand III, 214-215).

Having set the stage and gauged the opinions of Convention delegates, late on August 16th Morris made his move to absolutely ban Federally-issued paper money—moving to strike out the words “and emit bills on the credit of the United States” from the enumerated powers granted the National Legislature. He reasoned that “If the United States had credit such bills would be unnecessary: If they had not unjust & useless.” The debate that followed is worth quoting at length:

Mr. Madison, will it not be sufficient to prohibit the making them a tender? This will remove the temptation to emit them with unjust views. And promissory notes in that shape may in some emergencies be best.

Mr. Gouverneur Morris. Striking out the words will leave room still for notes of a responsible minister which will do all the good without the mischief. The Monied interest will oppose the plan of Government, if paper emissions be not prohibited.

Mr. Gorham was for striking out, without inserting any prohibition. If the words stand they may suggest and lead to the measure.

Col. Mason had doubts on the subject. Congress he thought would not have the power unless it were expressed. Though he had a mortal hatred to paper money, yet as he could not foresee all emergencies, he was unwilling to tie the hands of the Legislature. He observed that the late war could not have been carried on, had such a prohibition existed.

M. Gorham—The power as far as it will be necessary or safe, is involved in that of borrowing.

Mr. Mercer was a friend to paper money, though in the present state & temper of America, he should neither propose nor approve of such a measure. He was consequently opposed to a prohibition of it altogether. It will stamp suspicion on the Government to deny it a discretion on this point. It was impolitic also to excite the opposition of all those who were friends to paper money. The people of property would be sure to be on the side of the plan, and it was impolitic to purchase their further attachment with the loss of the opposite class of Citizens

Mr. Ellsworth thought this a favorable moment to shut and bar the door against paper money. The mischiefs of the various experiments which had been made, were now fresh in the public mind and had excited the disgust of all the respectable part of America. By withholding the power from the new Government more friends of influence would be gained to it than by almost any thing else—Paper money can in no case be necessary—Give the Government credit, and other resources will offer—The power may do harm, never good.

Mr. Randolph, notwithstanding his antipathy to paper money, could not agree to strike out the words, as he could not foresee all the occasions that might arise.

Mr. Wilson. It will have a most salutary influence on the credit of the United States to remove the possibility of paper. This expedient can never succeed whilst its mischiefs are remembered. And as long as it can be resorted to, it will be a bar to other resources.

Mr. Butler. remarked that paper was a legal tender in no Country in Europe. He was urgent for disarming the Government of such a power.

Mr. Mason was still averse to tying the hands of the Legislature altogether. If there was no example in Europe as just remarked it might be observed on the other side, that there was none in which the Government was restrained on this head.
Mr. Read, thought the words, if not struck out, would be as alarming as the mark of the Beast in Revelations.

Mr. Langdon had rather reject the whole plan than retain the three words “and emit bills.” [The motion to striking out “and emit bills” was passed 9 to 2]12 (Farrand II, 308-310).

There are several very important and telling aspects to this debate. First, for only the second (and last) time at the Convention the distinction was raised between legal tender issues and the emission of paper money per se. The two structural pillars that were connected with the successful performance of paper money in colonial America were the restrictions on its legal tender status and the enactment of taxes designed to redeem said money. The new power to directly tax was to be given to the Federal Government, thus resolving the prior absence of one of the pillars. That just left enacting a legal tender restriction in order to come close to replicating the colonial monetary structure. When Madison raised this issue—making the distinction between the legal tender restrictions and banning paper money emission per se and indicated that it was the legal tender issue that was causing all the problems—Morris’ response was blunt and absolute, “The Monied interest will oppose the plan of Government, if paper emission be not prohibited.” This absolute prohibition with no qualifying considerations, and the (rather grandstanding) willingness of Morris and his “monied interest” to risk losing the whole Constitution if an absolute prohibition was not agreed to, was also echoed by several other delegates, e.g. see the quotes of Mercer, Read, and Langdon above.13 In addition, as if in answer to Madison, the game of erroneously conflating legal tender issues with the emission of paper money per se was reasserted by Butler when he “remarked that paper was a legal tender in no Country in Europe. [And] He was urgent for disarming the Government of such a power.” This absolute, risk all (losing the entire constitution), no-compromising position taken by the “monied interest” on absolutely banning Federally-issued paper money, must have also implied the same position with regard to State-issued paper money, which will be seen to be the case below. These delegates were not stupid or inexperienced people. They knew the difference between legal tender restrictions and the emission of paper money per se. Some other purpose must have been afoot to cause them to take such a strong uncompromising risk-all position on the necessity of an absolute ban on government-issued paper money.

Second, this debate reveals that the delegates knew that the recent problems with paper money were not due to paper money per se, but due largely to the problems of wartime finance and its aftermath.
For example, Mercer refers to the “present state & temper of America” regarding paper money, Wilson refers to the memory of paper money’s mischiefs, and Ellsworth refers to this time being “a favorable moment to shut and bar the door against paper money. The mischiefs of the various experiments which had been made, were fresh in the public mind…” In other words, they knew that during peacetime, under colonial-type restrictions, paper money had worked well. Even if paper money was the best way of financing war, its performance would be worse than during peacetime. They were willing to try the ignorance of the public and muddle the distinction between peacetime and wartime financial performance in order to justify an absolute ban on paper money emissions. If the public only remembered that the Continental Dollar hyper-inflated, and did not delve into the underlying causes of it, then they might easily blame it on the emission of paper money per se. The delegates knew that during war such a paper money expedient could be the best choice from among the set of necessary financing evils. Madison’s reference to some “emergencies” and Randolph’s to not being able to “foresee all occasions,” when paper money might be useful, would seem to refer to wartime financing, and Mason explicitly says that “the late war could not have been carried on” without paper money. This knowledge, however, was to be suppressed by the majority of the delegates in the drive to absolutely ban government-issued paper money.

Third, Morris says something very cryptic and telling about what alternatives might be available. In response to Madison’s legal tender question, Morris initially says “striking out the words leave room still for notes of a responsible minister which will do all the good without the mischief.” Who did Morris mean by “responsible minister”? If it cannot be an official arm of the National Government, who else is left? There is perhaps only one candidate, Morris’ Bank of North America. Since 1782 this bank had been trying to operate as the National Government’s bank by attempting to get its banknotes to circulate as a national paper currency and making loans to the National Government (Grubb 2003, 2004a; Lewis; Wilson). As such, Morris clearly is not against all paper money, only against tax-backed government-issued paper money. Bank-issued paper money that was fractionally specie-backed was acceptable. In other words, Morris wanted governments at all levels to surrender paper money issuing power to banks, with the only quasi-national bank at the time being his Bank of North America. Why did Morris use the cryptic phrase “responsible minister” and not just come right out and say “Bank of North America”? It is likely, as
will be shown below, that Morris did not say “bank” because the mere mention of the word, even among
the Convention delegates, was so controversial that it was likely to kill the new Constitution.¹⁵

B. The Absolution Prohibition on Paper Money Issued by State Governments

Having secured an absolute ban on Federally-issued paper money, the move to absolutely prohibit
State-issued paper money was probably a foregone conclusion. It only waited for the Convention to get to
that part of the draft constitution.¹⁶ On August 28th the Convention got there. Wilson and Sherman moved
to cut the phrase “without the consent of the Legislature of the United States” from the clause “No State,
without the consent of the Legislature of the United States, shall emit bills of credit, or make any thing but
specie a tender in payment of debts…” thus “making these prohibitions absolute…” Note that it is Wilson
who is moving to change (make more radical) the very clause that he first added to the draft constitution
while on the Committee of Detail. Having already achieved an absolute prohibition on National
Government bills of credit on August 16th with the forceful argument that “The Monied interest will
oppose the plan of Government, if paper emissions be not prohibited” the ensuing debate was short:

Mr. Gorham thought the purpose would be as well secured by the provision…which
makes the consent of the General Legislature necessary, and that in that mode, no opposition
would be excited; whereas an absolute prohibition of paper money would rouse the most desperate
opposition from its partisans—

Mr. Sherman thought this a favorable crisis for crushing paper money. If the consent of
the 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.

The question was divided into whether to have an absolute prohibition on States emitting bills of credit,
which passed 8 to 2, and whether to make the legal tender clause an absolute prohibition, which passed 11
to 0. (Farrand II, 435, 439). The separate votes on the two clauses indicate that they could have potentially
decided just to absolutely ban legal tender provisions but not to absolutely ban State paper money
emissions per se. Again the tandem linking of these two issues appears to illustrate the erroneous conflation
by the delegates of the problems caused by legal tender laws with that of paper money emission per se.

As in the debate over an absolute ban on Federally-issued paper money, Sherman’s statement
about it being a “favorable crisis” for crushing paper money indicates that the delegates knew that paper
money per se was not the problem, but that they could muddle the debate and play on the public’s
confusion of wartime with peacetime monetary problems to win an absolute paper money ban. And again,
their rhetoric indicates that some other reasons were afoot for banning paper money per se than that
expressed by the delegates or commonly given in the ratification debates and historical accounts. Finally, Gorham’s statement, along with that of John Francis Mercer’s statement in the prior quote, suggests that the anti-paper money faction at the Convention was willing to risk alienating a considerable part of the public, and perhaps jeopardize ratification of the Constitution, in order to have their way and get an absolute ban on paper money at all levels of government.17

VI. National Banking as a Substitute Monetary Power?—August 16 to September 14

The British extended the Bubble Act to the colonies in 1741. This Act did not allow corporations to form that had over six partner/investors, which in turn effectively stopped commercial banks from developing in the colonies (Perkins 41; Priest). With independence, Colony/States were free to incorporate banks, which they began to do in 1781 when Pennsylvania chartered the Bank of North America, and in 1784 when New York and Massachusetts chartered the Bank of New York and the Bank of Massachusetts, respectively. Efforts to charter banks were underway in other States between 1784 and 1787, such as in Maryland where a bank charter bill passed by that State’s Senate was being blocked by that State’s House of Delegates. These banks took in deposits in specie and issued banknotes as claims against said deposits and as loans. Depositors could also issue checks as claims on their specie deposits. These banks were basically engaged in modern, though unregulated, fractional-reserve practices with specie serving as reserves. They issued more banknotes, loans, and claims on their specie deposits than they had specie on reserve. While not a legal tender, these banknotes circulated to some extent as a geographically localized currency because they could be redeemed in specie at the issuing bank at face value, except during liquidity crises, but typically at variable market-determined discounts off the face value farther away from the issuing bank. As such, these banknotes competed for usage as an inside paper money with the notes issued by other banks chartered in the same “geographic reputation” region and with the bills of credit issued by their respective States when said States issued such. Banks and bank charters were a contentious and controversial issue in many State legislatures. (Behrens 79-87; Bryan 17-19; Freeman 575-612; Gras; Grubb 2003, 2004a; Lewis; Webster; Wilson).

At the Convention, the delegates did not discuss nor ever address the States’ power of incorporation, either in general or with specific reference to banking. Apparently such State powers were acceptable to the founding fathers and they were to be left in tact by the new Constitution. Several
delegates were closely involved with State chartered banks in their respective states, either as stockholders, board members, directors, legal advisors, or sponsors of banking bills, including Alexander Hamilton of New York, Elbridge Gerry of Massachusetts, John Langdon of New Hampshire, Abraham Baldwin of Georgia, Rufus King of Massachusetts, John McHenry of Maryland, and the entire Pennsylvania delegation of Thomas Mifflin, Robert Morris, George Clymer, Jared Ingersoll, Thomas Fitzsimons, James Wilson, Gouverneur Morris, and Benjamin Franklin (Grubb 2003, 2004a; McDonald 89). Perhaps then it is not surprising that the State power to charter banks was left untouched by the Convention.

On the national level, under the *Articles of Confederation* it was unclear whether Congress had the power to charter a national bank. In the 1785-1787 controversy in the Pennsylvania State legislature over the Pennsylvania State charter of the *Bank of North America*, which Congress had also chartered and intended to be its national bank, the actions of both the pro- and anti-bank parties indicated that both sides had little faith in the validity and efficacy of a charter from Congress and that both sides thought a State charter was necessary (Lewis; Rappaport; Webster; Wilson). If a national bank chartered by the Federal Government was to be allowed, it would have to be one of the new and enlarged powers specifically enumerated in the new Constitution. On August 16th, in the debate to eliminate the Federal Government’s power to emit paper money, Gouverneur Morris hinted at some national paper money substitute when he suggested that the notes of some “responsible minister” might take the place of a National Government paper currency (Farrand II, 309). There seems little doubt that Gouverneur Morris probably meant the *Bank of North America*, acting as the Government’s national bank, by the term “responsible minister.”

By August 28th, the Convention had absolutely banned both State and Federal Government paper money emissions. The question as to whether the National Government could charter a national bank that could serve a national-paper-currency function was taken up in a round-about way on September 14th when the Convention addressed the general versus specific powers of incorporation to be granted to the National Government. With regards to the power of incorporation, the draft constitution up to that point gave the National Government only the specific enumerated power to establish post offices and post roads. Franklin moved that the National Government also have the power to cut canals. From there the debate expanded and the exchange between the delegates is worth quoting at length (from Madison’s notes):

> Mr. Madison suggested an enlargement of the motion into a power “to grant charters of incorporation where the interest of the U.S. might require & the legislative provisions of
individual States may be incompetent.” His primary object was however to secure an easy communication between States which the free intercourse now to be opened, seemed to call for—The political obstacles being removed, a removal of the natural ones as far as possible ought to follow. Mr. Randolph 2ded. the proposition.

Mr King thought the power unnecessary.

Mr Wilson. It is necessary to prevent a State from obstructing the general welfare.

Mr King—The States will be prejudiced and divided into parties by it—In Philadelphia & New York, It will be referred to the establishment of a Bank, which has been a subject of contention in those Cities. In other places it will be referred to mercantile monopolies.

Mr. Wilson mentioned the importance of facilitating by canals, the communication with the Western Settlements—As to Banks he did not think with Mr. King that the power in that point of view would excite the prejudices & parties apprehended. As to mercantile monopolies they are already included in the power to regulate trade.

Col: Mason was for limiting the power to the single case of Canals. He was afraid of monopolies of every sort, which he did not think were by any means already implied by the Constitution as supposed by Mr. Wilson.

The motion being so modified as to admit a distinct question specifying & limited to the case of canals. [The motion failed 8 to 3.]

The other part fell of course, as including the power rejected. (Farrand II, 615-616).

McHenry also made brief notes for this day that, in general, support Madison’s notes on this issue. He wrote, “Moved by Dr. Franklin seconded by Mr. Willson, to empower Congress to open and establish canals. This being objected to—moved by Virginia To empower Congress to grant charters of incorporation in cases where the U.S. may require them and where the objects of them cannot be obtained by a State. Negatived.” (Farrand II, 620).

Both Madison’s and McHenry’s notes of the Convention for that day are corroborated by an incident recorded by Jefferson some years later. Jefferson, who was in Paris during the Convention, recorded in his personal notes that on 11 March 1798:

[Abraham] Baldwin [Convention delegate from Georgia] mentions at table the following fact. When the bank bill [First Bank of the U.S.] was under discussion in the House of Representatives [1791], Judge [James] Wilson came in, and was standing by Baldwin. Baldwin reminded him of the following fact passed in the grand [1787] convention. Among the enumerated powers given Congress, was one to erect corporations. It was, on debate, stuck out. Several particular powers were then proposed. Among others, Robert Morris proposed to give Congress a power to establish a national bank. Gouverneur Morris opposed it, observing that it was extremely doubtful whether the constitution they were framing could ever be passed at all by the people of America; that to give it its best chance, however, they should make it as palatable as possible, and put nothing into it not very essential, which might raise up enemies; that his colleague (Robert Morris) well knew that ‘a bank’ was, in their State (Pennsylvania) the very watch-word of party; that a bank had been the great bone of contention between the two parties of the State…that therefore, to insert this power, would instantly enlist against the whole instrument, the whole of the anti-banking party in Pennsylvania. Whereupon it was rejected, as was every other special power, except that of giving copyrights to authors, and patents to inventors; the general power of incorporating being whittled down to this shred. Wilson agreed to the fact. (Farrand III, 375-376).

It would appear that banks were as, or even more, controversial than paper money emissions, with the mere mention of banks, even by indirect implication, being so controversial that it threatened the likely
ratification of the Constitution. Perhaps this is why on August 16th Gouverneur Morris used the term “responsible minister” rather than “Bank of North America” when referring to a paper-money substitute to Federally-issued bills of credit (Farrand II, 309).

Given the above records, it would appear that the Convention intended not to give, and in a round-about way voted against giving, the Federal Government the general power of incorporation, including the particular power to incorporate a national bank. The only exception to this denial of power was that the Federal Government could establish post offices and post roads. In 1791, however, Congress voted to charter a national bank anyway, i.e. the First Bank of the U.S., which was to serve as the Federal Government’s bank. A sharp debate and on-going controversy over the constitutionality of this act, i.e. over the constitutionality of the First Bank of the U.S., ensued (Holdsworth 17-19). How was such a debate even possible given the above quoted records? The answer involves memory, record availability, plausible deniability, and perhaps a willingness to subvert the Constitution over this issue.

At the Convention, the Constitution’s construction was understood to be that any new and enlarged power that went beyond the Articles of Confederation that was not explicitly enumerated as granted to the Federal Government was denied to it. This construction explains the Constitution’s brevity. Except for erecting post offices and post roads, the power of incorporation in general including the power to charter a bank in particular was not one of the new enumerated powers to be given to the Federal Government. Thus by construction, Congress would appear not to have the power to charter a national bank. However, the powers explicitly voted by the Convention not to be included among these enumerated powers of the Federal Government, by construction, were not to be written into the Constitution. Again, this design kept the Constitution from becoming an overly long and unwieldy document.

This method of construction, however, opened an interpretive door that Hamilton and supporters of a national bank rushed through. When a new power was not explicitly enumerated, Congress might still possess that power if that power was implied by other powers that were explicitly enumerated in the Constitution. This doctrine of implied powers was first articulate by Hamilton over the issue of the constitutionality of the First Bank of the U.S. (Rutland XIII, 370-404; Syrett VIII, 62-134). It went on to become a famous, well-known, and well-studied doctrine of interpretation of constitutional law. The application of the implied-powers doctrine here, however, would all be for not if it was known or could be
shown that the Convention had intended or explicitly voted not to give the Federal Government the said power. Such an intent or explicit vote against including such a power among the enumerated powers would negate any implied-powers interpretation of said. Thus the bank supporters had to argue that no such debate, intent, or vote ever took place at the Convention that denied the Federal Government general powers of incorporation and the power to charter a bank in particular. Because no records of what transpired at the Convention were yet published in 1791, such an argument might work—and did.

The Convention had been closed to the public. The Convention’s official Journal, which was not made public until 1819, was deposited in President Washington’s keeping (Farrand I, xi-xxi; II, 648). As such, this Journal would have been available at least to President Washington, if not the administration in general, to consult regarding the above issue. The Journal, however, recorded almost nothing for that day (September 14th). With regards to the discussion quoted above, the Journal only recorded an 8 to 3 vote against “To grant letters of incorporation for Canals &ca” (Farrand II, 610-611). Madison’s notes were the most detailed of the Convention debates in general, as well as of the debate on the particular day in question (September 14th). They, however, were not public, and would not be published until 1840 (after Madison’s death). And McHenry’s notes, the only other notes taken for that day, would not be published until even later (Farrand I, xv-xxi).

In 1791, when Congress proposed the bill to charter the First Bank of the U.S., Madison argued that such a bill was unconstitutional “because he well recollected that a power to grant charters of incorporation had been proposed in the General Convention and rejected.” (Farrand III, 362). Being the person who proposed the power in question, Madison’s was likely to have been the most attentive of the Convention delegates regarding the ensuing discussion, and so have the clearest memory regarding the debate over said power. In addition, Madison had his very detailed notes to consult in order to reach this conclusion. Whether Madison let anyone else see his notes, however, is unclear. There is no indication by him or from anyone else that he did so.

Madison, however, was “regarded by his fellow delegates to the Convention as a semi-official reporter of their proceedings, for several of them took pains to see that he was supplied with copies of their speeches and motions.” (Farrand I, xvi). Given that the Journal failed to record most of the debates at the Convention, Convention delegates who did not remember the debates of a given day should have deferred
to Madison’s recollection as derived from his detailed semi-official notes. Some clearly did. For example, Edmund Randolph, Convention delegate from Virginia and Attorney-General in 1791 under President Washington, as well as Thomas Jefferson as Secretary of State, concurred with Madison’s memory and/or accepted the authority of his recollections as based on his detailed semi-official notes. As such, for Madison, Randolph, and Jefferson there wasn’t much to argue or debate. The Convention had voted not to give Congress that power, so the First Bank of the U.S. was unconstitutional, and they recommended that President Washington veto said bill as unconstitutional (Farrand III, 362-363; Rutland XIII, 370-404).

President Washington was at the Convention that day (September 14th). Either he knew from his own memory that Madison was right and he chose to ignore it, or he did not rightly remember that day’s debates. The latter very well could be likely. Washington never engaged in the debates at the Convention. As such, he may have paid little attention to particular debates and specific issues and so had no memory of the issue at hand. Washington did have possession of the Convention’s Journal, but this Journal recorded almost nothing on the topic at hand. But if he didn’t remember the debates of that day himself, why did he reject Madison’s recollections, or why did he not accept Madison’s opinion as definitive since it was based on Madison’s own semi-official detailed notes of the Convention? Washington had to have watched Madison take these notes every day. Perhaps Washington’s sympathies were strongly tied to his fellow officer, and some would say sycophant, Hamilton, and/or perhaps Washington had long been persuaded by Hamilton and Robert Morris (head of the Bank of North America and at whose house Washington often dined during the Convention) that a national bank was necessary (Huston; Warren). Perhaps Washington was looking for an interpretative opening regarding the constitutionality of the bill so as not to veto the bill.

With no official public record showing that the Convention explicitly voted to deny Congress the power of incorporation in general and the power to charter a bank in particular, the supporters of the bank could choose to ignore Madison’s statements based on his semi-official but unpublished notes. Instead, they could claim that no one at the Convention rightly remembered what happened and that no such debate or vote on said may have even taken place. With no published record, they could plausibly deny that such a power was explicitly denied Congress. As such, while not enumerated, such a power could nevertheless still be included as an implied power, even if their own memories told them otherwise. Indeed, Gerry, who favored a national bank, was present at the Convention on September 14th, but in February of 1791 he
disagreed with Madison’s recollection of that day. He said, in direct reference to Madison’s statement above on this issue, “…are we to depend on the memory of the gentleman [Madison] for a history of their debates…. This would be improper, because the memories of different gentlemen would probably vary,… with respect to those facts;… no motion was made in that Convention, and therefore none could be rejected for establishing a National Bank;…” (Farrand III, 362-363). This also indicates that it was unlikely that Madison showed his notes of the Convention to anybody else.

Hamilton made a similar statement later that month when he wrote a defense of the constitutionality of First Bank of the U.S. in order to give Washington a reason not to veto the bill,

Another argument…is, the rejection of a proposition by the Convention to empower Congress to make corporations, either generally, or for some special purpose.

What was the precise nature or extent of this proposition, or what the reasons for refusing it, is not ascertained by any authentic document, or even by accurate recollection. As far as any such document exists, it specifies only canals. … It must be confessed, however, that very different accounts are given the import of the proposition, and of the motives for rejecting it. Some affirm that it was confined to the opening of canals and obstructions in rivers; others, that it embraced banks; and others, that it extended to the power of incorporating generally. Some, again, allege that it was disagreed to because it was thought improper to vest in Congress a power of erecting corporations. Others, because it was thought unnecessary to specify the power, and inexpedient to furnish an additional topic of objection to the Constitution. In this state of the matter, no inference whatever can be drawn from it. (Farrand III, 363-364).

Hamilton makes two interesting references in his argument. First he referred to no “authentic document” supporting Madison’s interpretation and that the only “authentic document” that existed only refers to canals. It seems clear that Hamilton must be referring to, and had consulted, the Convention’s official Journal which at the time was in Washington’s keeping. As such, Hamilton considered none of the other notes from the Convention, such as Madison’s notes, as being an “authentic document.” Given that none of these other notes had yet been published or made available for others to consult, Hamilton could plausibly deny that he was making an inaccurate assessment.

Second, Hamilton asserted in reference to the debates at the Convention on September 14th that “…the precise nature or extent of this position…[can] not [be] ascertained…by accurate recollection.” Why did Hamilton not refer to his own recollection from that day? His statement here seems to suggest that he was not present for that day’s debates. Madison records Hamilton as speaking at the Convention on September 12th and then next on September 17th, but not between those days. His absence on September 14th would also be consistent with the fact that if he were there it seems likely that he would have spoken since national banks had long been an important issue of his (Freeman 1040; Syrett II, 400-418). If
Hamilton was there and remembered the debate as recorded by Madison, then he was willingly subverting the Constitution. If Hamilton either was there but did not remember the debate or was not in attendance that day, why did he reject Madison’s recollections, or why did he not accept Madison’s opinion as definitive since it was based on Madison’s own semi-official detailed notes of the Convention? Hamilton knew that Madison had taken copious and semi-official notes of the Convention. Hamilton had himself given Madison a copy of his own speech to the Convention so that Madison could accurately record it and include it in Madison’s notes (Farrand I, xvi, 282-293; III, 617-630). Washington’s and Hamilton’s unwillingness to defer to Madison’s semi-official note-based recollection suggests a knowing willingness on their part to subvert the Constitution over the bank issue.

In the end, Washington accepted Hamilton’s arguments and did not veto the bank bill (Holdsworth 19). The nation got a national bank with a national banknote currency that circulated along side the increasing plethora of State-chartered banks issuing their own banknotes. At this juncture, it could be plausibly argued that within two years of its adoption Washington, Hamilton, and the other First Bank of the U.S. supporters among the Convention delegates were willing over the bank issue to knowingly subvert the Constitution. And the circumstances of the notes and records of Convention deliberations and the extent to which these were not made available and not published gave them plausible deniability of having intentionally subverted the Constitution. Perhaps Madison could have stopped the First Bank of U.S. if he would have made his notes of the Convention publicly available. Why didn’t he? Perhaps his sense of honor or vow of secrecy trumped his desire to stop constitutionally questionable acts from being passed.

**VII. Why Did They Do It?**

The primary purpose so far has been to trace and deconstruct the “what” and “how” of the dramatic constitutionally-manufactured transformation of monetary powers brought about at the 1787 Constitutional Convention. Before the U.S. Constitution, inside paper money was issued directly by State and National legislatures. It was backed not by specie but by the future taxes of the issuing government thus making each paper currency inside to that jurisdiction, respectively. Under British regulation, it was also not a legal tender during the quarter century prior to the Revolution. After the U.S. Constitution, both State and National Legislatures were banned absolutely from issuing paper money. In its place, State and National Government-chartered, but privately run, banks rushed to fill the void. They issued paper money
that was backed fractionally by reserves in specie. While not a legal tender, banknotes functioned as an effective inside paper money—inside to the geographic reputation area of each bank. Thus, from potentially 13 different State and one National paper currencies, the U.S. after 1789 experienced an increasing plethora of different banknote paper currencies. Judging by the outcome, the intent of the founding fathers was not to create a single uniform national paper currency or prevent States and their banks from competing for seignorage with each other (Grubb 2003, 1782; Rolnick, Smith, and Weber).

Why the founding fathers at the Convention created the conditions for this radical monetary transformation by embedding it in the new Constitution is harder to know. A few (of the many) speculations as to why will be addressed here.

First, if the founding fathers are assumed not to be stupid, or ignorant, or inexperienced in monetary matters, if they are assumed not to be fooled by the difference between legal tender laws and paper money emission *per se*, and if they are assumed not to be fooled by the exigencies Revolution finance or to have confused war with peacetime monetary performance, then many of the simplistic explanations offered in the literature and by the delegates themselves in the ratification debates for why they did it are ruled out (Elliot 333-336; Grubb 2003, 1781-1782; Jensen II, 500). The pre-Revolution-system of paper money had worked well for a quarter century under the restriction of not making it a legal tender except for payment of the issuing government’s taxes. A pure non-legal tender fiat paper money emitted by legislatures that was backed by future taxes rather than specie was not inherently unstable or inflationary, especially during peacetime (Grubb 2003, 2004a, 2004b, 2004c; Smith 1985; Wicker). Wartime inflation under any monetary system would be expected, not just under the old pre-U.S. *Constitution* system (Rockoff). For example, inflation during the War of 1812 rivaled that during the Revolution (Bezanson 1936, 388-389; 1951). The founding fathers likely knew that the recent problems caused by paper money emissions were the result of war conditions and legal tender laws and not due to paper money *per se*. And most of the Federalist arguments for the Constitution’s absolute prohibition on paper money *per se* were in fact arguments against legal tender provisions and not against paper money *per se* (Elliot 333-336; Grubb 2003, 1781-1782; Jensen II, 500). So why did they seek an absolute ban on paper money *per se* rather than just a ban on legal tender laws?
Grubb (2003, 2004a) argued that it was the banking faction, e.g. Langdon, Baldwin, King, Hamilton, Gerry, McHenry, the entire Pennsylvania delegation, and maybe a few others, that wanted an absolute constitutional ban on the emission of paper money by both State and National Governments so as to constitutionally eliminate the competition with banknotes over what would become the dominant paper medium of exchange. Banknotes were having a hard time supplanting government-issued paper money as the paper medium of exchange. With government-issued paper money now constitutionally eliminated, the power and profitability of these publicly chartered by privately run banks, especially of the national banks, such as the Bank of North America and subsequently the First Bank of the U.S., and of the people who held stock in and directed said banks, were substantially increased. While consistent and plausible, and would explain why the founding fathers focused on paper money emission \textit{per se} at both the National and the State level, rather than just focusing narrowly on the problem of legal tender, it does not explain the concurrence of those founding fathers with no apparent banking connections with the monetary-power restrictions put in the Constitution at the Convention. Unless these other founding fathers were just duped or arm-twisted by the banking faction something more is needed.

Perhaps the founding fathers thought that only banning paper money that was a legal tender, rather than banning all paper money, would not stop legal-tender issues of paper money. The only way to stop legal-tender issues of paper money was to stop the issuance of all instruments that could tempt legislatures into legal tender provisions. Certainly much of the Federalists rhetoric cited above conflates paper money emissions \textit{per se} with legal tender laws or considers the latter to be a consequence of the former. This would be the “big tent” theory of legal proscription, e.g. it is not enough to ban murder you must also ban all the instruments that might be used to murder. This explanation seems unlikely because for one the late colonial system had worked just fine with only a ban on legal tender paper money and not on all paper money. Second, they did not ban other instruments that States had in the past made a legal tender. Third, the founding fathers did not pursue this theory on other, arguably more important, legal proscriptions put in the Constitution. For example, one of the key reasons for holding the Convention was to regulate trade between the States. As such, the founding fathers sought to prohibit States from taxing imports from, and exports to, other States. However, contrary to the “big tent” theory of Constitutional prescript, they allowed States to tax said to support the execution of State-inspection laws (Farrand II, 605, 657), thus opening the
door for States to erect cost wedges between products traded intra- versus inter-State. Finally, under this theory the founding fathers should have also banned banknotes or at least banned their acceptance as a legal tender. However, they did not do so. And Hamilton, as Secretary of the Treasury, simply declared that the notes of many banks were specie and therefore acceptable as payments to the Federal Government (Syrett V, 394, 532-533; VI, 386-388; IX, 489).

After the Revolution, substantial legislative polarization and civil unrest in many States, e.g. in Massachusetts, Rhode Island, Pennsylvania, Maryland, and Virginia, had been linked by Federalist rhetoric to the popular rage for paper money (Farrand I, II; Grubb 2003, 1781; Holton). If a goal of the Constitution was to eliminate sources of polarizing civil and political disputes that evoked high passions and potential violence within the States then an absolute ban on State paper money rather than just restricting legal tender laws might make sense. However, if such was the case then why constitutionally ban Federally-issued paper money? In addition, under such a motivation, the Constitution should have also banned banks, or tried to replicate something like the British Bubble Act as applied to the colonies in 1741, because State banking laws were as much a source of political and civil commotion as were paper money emissions. A similar case could be made for constitutionally restricting the insider trading of government securities by those with access to government power and information over said instruments. No other controversial State legislative issue was singled out for constitutional proscription. Again, something else is needed.

A popular and much debated explanation for why the Convention banned paper money *per se*, has been that delegates held public securities and feared that they would not be redeemed at face value if governments could issue paper money (Beard 178-188; Holton; McDonald 89-110; McGuire 72-74). This idea is also consist with Gouverneur Morris’ argument (see above) about why the Federal Government should have the power to tax exports—namely that the Federal Government needed a direct access to tax revenue paid in specie. What scholars have missed in this debate, however, is that this issue is only about legal tender laws and not about paper money emissions *per se*. If the Convention had simply banned paper money from being made a legal tender, securities denominated in specie monetary units would be protected against being paid off in depreciated paper money. Governments issuing paper money would have to pay off their old specie denominated debts at the market-determined exchange rate of their paper money for
specie. No losses would be incurred by creditors. As such, efforts to link security holding by Convention delegates with votes at the Convention for banning paper money emissions may miss the mark.

The part of this public-securities argument that can be salvaged involves government securities denominated in that government’s paper money units. For such securities, governments could pay them off with newly issued paper money, even if that money was not a legal tender, because it was what was explicitly contracted. Security holders would receive the face value of the debt, though that value may have depreciated substantially from what it was at the time of contracting. This (unanticipated) inflation risk-cost, however, was what any security holders faced no matter what monetary unit they contracted in.

Market expectations governed price adjustments of said securities at the time of contracting. The gains or loss due to deflation or inflation of said currency would only be residual unanticipated luck. However, if governments were absolutely banned from issuing paper money then they would have to pay off their non-specie denominated securities in specie—the only money available. Because the courts would likely uphold contract “nominalism,” this created the potential for insider speculative gains by Convention delegates and their confidants (Holton; Priest). With the Convention deliberations kept secret, Convention delegates would have superior information (a lower-risk expectation) that soon governments would have to pay off their non-specie-denominated securities at par in specie. They would have had a head start on the market and could buy up government securities at their current discounted prices, knowing that the securities would appreciate in the near term. Such a motive would not show up as contemporaneous correlations between delegate security holding and Convention votes because the speculative scheme had not been executed yet. This explanation, however, has not been tested formally yet. Casual empiricism suggests that it is unlikely to have been a pervasive motivation.

Finally, a broader and more general (new) reason why they did it will be offered here. While not all Convention delegates were directly connected to the nascent banking movement or holders of large amounts of public securities, most were nevertheless connected in some way—as merchants, planters, or lawyers—with international trading and to the nation’s international trading community (Beard; Bradford; McDonald; McGuire 51-54). Access to outside money, namely specie, was critical to the functioning of this trade. In general, specie flowed in from the trade surpluses with the Caribbean and specie flowed out with the trade deficits with Europe. With trade having to balance in the long-run, specie would typically be
available and the presence of a non-legal-tender tax-backed inside paper money would not threaten access to specie. The paper money which merchants received from local citizens in payment for goods, if not used to pay taxes, could always be exchanged at the market-determined exchange rates for specie when needed to meet outside payments. However, the exigencies of trade and trade disruptions, and hence of specie flows, were not always balanced in the short-run. Sometimes more specie flowed in than out, and at other times trade disruptions reduced specie inflows relative to the contractual commitments for specie outflows leading to local specie scarcity. When more specie temporarily flowed in than out there was no merchant problem. However, when more specie temporarily flowed out than in, merchants became desperate to find specie so as not to default on their outside-money contract commitments.

This problem could be solved if the merchant community could secure a ‘reservoir’ of specie that could be tapped in times of short-run short-falls in specie inflows and then filled back up again in times of short-run excess specie inflows. In other words, create a sort of specie smoothing device. In essence this is one of the ideas behind the nascent merchant banks that were being developed at the time, i.e. a “bank” of specie. If all merchants dealing with international trade deposit their specie in said bank—pooling the specie of the merchant community, then temporary short-run excesses and short-falls in specie flows caused by the exigencies of trade would at least be smoothed across individuals within the community. However, this could not stop large macro-trade shock from causing specie short-falls and price depressions community wide, as what happened when the British closed much of their Caribbean trade to the Americans shortly after 1784 (Bezanson 1951; Holton; Rappaport).

The international-trading merchant community could secure a broader reservoir of specie in society at large from which they could draw in times of short-run short-falls in specie inflows if they could force the mass of citizens who were not directly engaged in international buying and selling to nevertheless hold and use specie as their primary medium of exchange. They could only achieve this if they eliminated all non-specie-backed inside paper money. This meant eliminating the tax-backed paper money issued both by the States and by the Federal Government. In other words, constitutionally making all money either outside money (specie) or backed by outside money (banknotes) that was convertible directly into specie on demand. This is what the founding fathers got constitutionally. So maybe it was their overriding intent.
This constitutionally-manufactured revolution in governmental monetary powers was not about securing general monetary stability, but about securing narrow special interests (Grubb 2003; 2004a; McGuire).

In the end, society at large paid for serving as this specie reservoir. Given the exigencies of trade, during period of short-run excess specie inflows, the public experienced credit expansion and suffered inflationary price rises and investment overextension. Then during periods of short-run short-falls in specie inflows (relative to outflows), the public experienced credit contraction, money scarcity, and arguably the more costly effects of bankruptcies, deflation, and investment retrenchment. Banks, functioning as a money multiplier in this process, may have structurally amplified this short-run or cyclical pain inflicted on the public for being the merchant community’s specie reservoir. An inside government-issued tax-back paper money not directly linked to specie would likely have dampened the effects of international trade-flow shocks on the public. Again, Luther Martin (and in an odd way Gouvernuer Morris) probably saw the issue correctly (Farrand II, 307; III, 214-215).

VIII. Epilogue

Today the U.S. has the same written Constitution in terms of monetary powers that the founding fathers created in 1787. And yet, we have a national paper money which is backed not by specie but only by Federal Government taxes, or the good faith and credit of the Federal Government—a Government that also has the power to institute price and exchange rate controls on said currency (Rockoff). This paper money is also a legal tender, with the legal tender clause “This note is legal tender for all debts, public and private” printed on each note. It is issued by the Federal Reserve Banking system that, while only a quasi-government agency in the strict legal sense, is about as close as you can get to a national banking system incorporated by the Federal Government. Unless we take the original intent of the founding fathers in their debates and votes at the 1787 Convention on monetary/banking powers to be a devious rouse, then it is hard not to conclude that we have strayed far away from what they tried to prohibit constitutionally.
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FOOTNOTES

1 From May 28th through September 17th the delegates meet every day except Sundays. There was a brief adjournment from July 27th through August 5th while the Committee of Detail crafted a draft constitution, on the 4th of July, and on September 11th while the Committee on Style polished the draft (Farrand I, II). Not all States or delegates attended continuously, see Farrand (III, 557-559, 586-590).

2 The “inside” versus “outside” money distinction is important. Outside money (specie) is that used to clear international (trans-government-jurisdictional) debts for both private and public trades. For a nation, such as the U.S. in 1787, that did not produce specie to have its money supply be only outside money meant that specie had to be imported to serve as the domestic money supply. This could only be done by exporting goods to import this money thus sacrificing the importation of other real goods. It also meant that the government had little direct influence over domestic monetary policy (other than regulatory powers over foreign trade), and that the economy was exposed to short-run swings in the availability of money (specie) caused by the exigencies of trade flows, wars, etc. These short-run swings could put severe pressure on domestic transactions, debt recovery, and tax revenues. The gain from using only outside money was that in the long-run international markets would equilibrate. Specie would flow from where it was plentiful to where it was scarce, leading to a common long-run stability in price trends internationally (Redish 713-714). Long-run domestic inflation would be constrained to be similar to long-run inflation in the outside money internationally. In addition, merchants would have a reservoir of specie in society to draw on to help smooth the short-run shocks to trade flows that they faced when doing international business. By contrast, when an inside money (not directly linked to specie) is used in place of outside money for purely domestic transactions, debt recovery, and tax payments it frees the outside money to buy imported real goods thus increasing social welfare (Pennsylvania Archives IV, 3284). It also increases the income (seignorage) of the government issuing the inside money—a non-inflationary substitute for direct tax revenue. The government would pay directly for goods with the initial issue of the inside money that would then circulate in society as currency, and/or loaning out said money at interest to its citizens. Issuing an inside money also gave the government a short-run monetary policy instrument to counter swings in economic activity caused by the exigencies of trade flows and other international disruptions to the outside money supply. The government could issue more inside money than it taxed out of circulation or vice versa.
to counterbalance short-run swings in the availability of outside money (Grubb 2003, 1780, 1792). Having an inside money also insulated purely domestic transactions, debt recovery, and tax payments from money scarcity caused by short-run specie outflows due to short-run imbalances in trade flows. In essence, the market exchange rate between the inside and outside money, and thus primarily the international merchant trading community as opposed to the whole society, would be forced to absorb the brunt of monetary shocks generated by the short-run imbalance in specie flows caused by the exigencies of trade, wars, etc. When only outside money is used these short-run shocks are borne by the entire society and sometimes disproportionately by purely domestic traders. The cost of using an inside money is the temptation to engage in (unanticipated) inflationary finance by over issuing the inside money thus inflating prices in the inside money faster than prices in the outside money and so (unexpectedly) driving the exchange rate between inside and outside money down. The typical causes (and why it is an easy temptation) are popular politics (promising more government services than the people are willing to pay for with taxes) and emergency expenditures such as during wars. The exchange rate between inside and outside money is the primary disciplining tool to restrain governments from excess inflationary finance. The binding legal tender issue (discussed later) becomes economically important when the government tries to escape this discipline by legally mandating the exchange rate between the inside and outside money to be different from what is determined by the market. For an up-to-date discussion for contemporary economies, see Feldstein (1-92).

3 I will rely primarily on Convention records and supporting documents as compiled in Farrand (I, II, III), and on his interpretation of those records and documents. The most detailed record of the debates at the Convention are the notes taken by James Madison. These “…have remained the standard authority for the proceedings of the Convention.” (Farrand I, xvi). As such, unless otherwise indicated, quotations of Convention debates are taken from Madison’s notes. At the Convention, votes on motions were recorded by State, not by individual delegate. As such, when votes are reported in the text, e.g. 8 to 3 against, they refer to the number of States on either side of the issue.

4 See the paper-money pamphlets written in 1752 by Roger Sherman, delegate to the 1787 Convention from Connecticut, and in 1759 by Peyton Randolph who was the uncle and role model to Edmund Randolph, delegate to the 1787 Convention from Virginia (Bradford 22, 166; Philoecunomos; Randolph).
On May 29th while taking notes on Randolph’s speech James McHenry of Maryland jotted down, “Congress ought to possess a power to prevent emissions of bills of credit.” (Farrand I, 26). Was McHenry quoting Randolph’s speech or was this phrase simply McHenry’s own sentiment expressed in his notes? The evidence strongly points against the former and in favor of the latter interpretation. First, this phrase, or anything like it, does not appear in the Convention’s Journal or in the notes taken by Madison, or by Robert Yates (New York), or by William Patterson (New Jersey) for that day. Second, the phrase in question, or anything like it, does not appear in Randolph’s own text of the speech. Randolph provided the written text of his speech to Madison who substituted it in place of his notes on the speech (appearing in Randolph’s handwriting in Madison’s notes of the Convention for that day). Third, the phrase in question was jotted down by McHenry in an odd location, namely in the section where Randolph was talking about blessings that the National Congress could bestow on the union if only it was given its own power of taxation (as opposed to appearing in the section which addressed the disharmony and conflict among the States). Thus, one possible interpretation of McHenry’s phrasing is that, given its own power to tax, Congress would not have to resort to emissions of paper money as it did during the Revolution. In other words, McHenry simply deduced that Congress ought to possess the power to tax which in turn would mean that they would possess the power to prevent themselves from engaging in emissions of bills of credit. Finally, McHenry’s notes for other days during the Convention frequently contain his own assessments and views in addition to recording some of the day’s discussions among the delegates. Thus, another likely interpretation would be that the phrase in question was simply McHenry’s own personal desires. McHenry had recently been the sponsor of a bill in the Maryland State Senate for establishing a bank. The Maryland House of Delegates had repeatedly blocked this banking bill. In its place the Maryland House of Delegates had passed a bill for a new emission of Maryland State paper money. In turn, the Maryland Senate had repeatedly blocked this paper money bill. McHenry may have seen a national congressional power to ban State paper money as the solution to this stalemate between the banking faction and the State paper-money faction that would allow his banking bill to succeed (the banking faction to win). See Bryan (17-19); Behrens (79-97); Grubb (2003, 1788-1789).
On June 2nd during the debate over how to elect the national executive Elbridge Gerry of Massachusetts also opined that “he thought the Community not yet ripe for stripping the States of their powers, even such as might not be requisite for local purposes.” (Farrand I, p. 80). However, shortly after Gerry will be the only delegate to mention an explicit enumerated monetary power that should be withheld from the States, and it wasn’t power over legal tender issues, but the power to emit paper money per se.

Randolph’s opening speech on May 29th only referred to the “havoc of paper money.” As such, it may have only been referring to the debacle of the National Government’s paper Continental Dollar.

Alexander Hamilton’s notes for June 6th also mention paper money. His notes, however, are a bit cryptic and lacking in context and reference, and so it is hard to interpret what to conclude from Hamilton’s written comments. He wrote, “Paper money is capable of giving a general impulse. It is easy to conceive a popular sentiment pervading the E states—.” (Farrand I, 146-147).

Among the papers of Roger Sherman of Connecticut is a document outlining proposals for a plan of government which includes the following: “That the legislature of the individual states ought not to possess a right to emit bills of credit for a currency, or to make any tender laws for the payment or discharge of debts or contracts, in any manner different from the agreement of the parties, unless for payment of the value of the thing contracted for, in current money, agreeable to the standard that shall be allowed by the legislature of the United States, or in any manner to obstruct or impede the recovery of debts, whereby the interests of foreigners, or the citizens of any other states, may be affected.” (Farrand III, 616). When this plan was written and to whom it was shown is difficult to determine. No specific reference to it appears in the Convention debates. Farrand (III, 615) suggests that it represented the ideas of the Connecticut delegation in forming the New Jersey Plan. However, nothing like the above passage appears in the New Jersey Plan, and it was not among the documents referred to the Committee on Detail on July 26th. The passage does have the hallmark of continuing the slide into conflating legal tender laws with the power to emit paper money per se, thus making these two distinct monetary powers the same evil to be stopped.

The reference here is to the paper money emitted by Rhode Island in 1786. A major complaint against this action by out-of-state creditors came when Rhode Island made this paper money a legal tender, because it meant that out-of-state creditors would have to accept Rhode Island paper money for payment of loans...
made within Rhode Island. The retaliation of which Madison speaks were laws passed by the Connecticut and Massachusetts legislatures that allowed their citizens, respectively, who owed debts to Rhode Island creditors to pay their debts in Rhode Island in Rhode Island paper money (Grubb 2003, 1782).

11 Hamilton made almost the same confession in 1790 as Secretary of the Treasury in his *Report on a National Bank* in reference to the peacetime stability of State-issued paper money. He said, “The emitting of paper money by the authority of Government is wisely prohibited to the individual States, by the National Constitution. … In times of tranquility, it [State-issued paper money] might have no ill consequences, it might even perhaps be managed in a way to be productive of good; but in great and trying emergencies, there is almost a moral certainty of it becoming mischievous.” (Freeman 591-592).

12 McHenry’s notes for this day corroborate the Convention’s decision to strike the words “and emit bills” from the powers granted to the Federal Government (Farrand II, 311). Shortly after the Convention, at the South Carolina ratification debate, Charles Pinckney, Convention delegate from South Carolina, when defending the Constitution’s ban on State-issued bills of credit, said, “Besides, if paper should become necessary, the general government still possess the power of emitting it, and Continental paper, well funded, must ever answer the purpose better than state paper.” (Elliot 335). While Pinckney did not speak on the day (August 16th) when the Convention voted to ban the National Government from emitting bills of credit, he did speak on August 15th and again on August 17th and is thought to have been present on August 16th. And South Carolina was recorded as voting for this ban on August 16th. (Farrand II, 298, 304-310, 314; III, 589-590). Whether Pinckney had just conveniently forgotten or was strategically lying is hard to say. But Pinckney’s claim here illustrates the key problem with the Constitution’s construction that would prove so controversial regarding a national bank (see the next section). By only enumerating the new powers given the National Government and not enumerating the powers the Convention explicitly voted not to give the National Government, coupled with keeping all the Convention’s deliberations and votes secret, individual Convention delegates could falsely assert, due either to mistaken memory or knowingly lying, that the National Government had certain powers even though said powers were not mentioned in the Constitution. Others would have no way of independently verifying said assertion. The fact that delegate memories of events could conflict gave plausible deniability to a delegate knowingly lying to the public.
Putting an absolute ban on government-issued paper money into the Constitution was considered a potentially high-risk, all-or-nothing, less-than-popular position. Those who most advocated it, such as Gouverneur Morris and James Wilson, while not directly connecting it with the issue of how to get the Constitution ratified, took a position on ratification seemingly consistent with this high risk strategy. For example, Wilson argued for approval of only 7 out of the 13 States for the new Constitution to be adopted and put into operation in place of the Articles of Confederation. Considering that 6 of the 13 States had so far won the political battle within their respective State against issuing paper money after the Revolution, and that Wilson, along with the rest of the Pennsylvania delegation and its connection with the Bank of North America, had recently gained control of Pennsylvania’s political process on the anti-paper money side, the number that Wilson advocated to achieve ratification is very telling (Farrand II, 468, 477, 562; Grubb 2003, 1790).

Gouverneur Morris could have also meant something like the personal notes issued by Robert Morris during the Revolution as Congress’ Superintendent of Finance. Given the close relationship between these notes and those soon issued by Robert Morris’ Bank of North America the distinction here is probably minor. (Perkins 115-116).

In a footnote to his notes on the Convention written sometime after the War of 1812 Madison explained Virginia’s affirmative vote for Gouverneur Morris’ motion despite the objections raised by the Virginia delegates Randolph, Mason, and himself, as “This vote in the affirmative by Virga. Was occasioned by the acquiescence of Mr. Madison who became satisfied that striking out the words would not disable the Govt from the use of public notes as far as they could be safe & proper; & would only cut off the pretext for a paper currency and particularly for making the bills a tender either for public or private debts.” (Farrand I, xv-xix; II, 310). This explanation may be just a hindsight effort by Madison to cover himself for the problems he and the National Government faced during his presidency in financing the War of 1812 given no constitutional power to emit bills of credit and given that the charter of the First Bank of the U.S. had lapsed in 1811 (Perkins 324-348).

On August 28th Pinckney moved again to add the power to the National Legislature to negate all State laws interfering with the harmony of the union. This power had already been defeated by the Convention
on July 17th and would not be adopted at this time either (Farrand II, 27-28, 382, 390-392). Because the
draft constitution submitted by the Committee of Detail already explicitly gave the National Legislature the
power to negate State emissions of paper money, giving the National Legislature a general negative over
State laws is not relevant to the issue of monetary powers here as it was before August 6th. But Pinckney’s
move here does indicate that the prior demand for a general negative over State laws was not just a
disguised demand for a negative over State monetary powers.

17 During the South Carolina’s ratification debate, Pinckney argued (Elliot 333-336), “This section
[Articles 1, Section 10 restricting State sovereignty] I consider to be the soul of the Constitution,… The
only parts of this section that are objected to are those which relate to the emission of paper money, and its
consequence, tender-laws, and the impairing the obligation of contract.” He then goes on for several pages
defending the Constitution’s absolute ban on State paper money. Clearly, Pinckney expected the strongest
opposition to ratifying the Constitution to come from this single clause. It should also be noted that
Pinckney, at several points in this speech, continued the strategy of conflating legal tender laws with the
emission of paper money per se, using the evils of the former erroneously to tar the latter. During the
ratification debates, Luther Martin, Convention delegate from Maryland, objected strenuously to the
absolute ban on paper money, claiming that it was the result of the Convention being “…smitten with the
paper money dread,…” Martin “considered that this State [Maryland], and some others, had formerly
received great benefit from paper emissions,…[that] such emissions might hereafter be equally
advantageous; and further, that it is impossible to foresee, that events may not take place, which shall
render paper money of absolute necessity…” (Farrand III, 214-215). Finally, Main (1961, pp. 268-79)
argued that a lot of Americans, maybe even a large majority, were on the side of paper money and unhappy
with the Constitution over absolutely banning its emission:

This thesis….stressed the correlation between Antifederalism and paper money… This
interpretation has much truth. … It is also true…that paper money was a factor in the [ratification]
contest. In Massachusetts, towns opposing paper were Federal by about four to one, while pro-
paper money towns were Antifederal by an even wider margin. [footnote 58: Pro-paper money
towns cast only 3 votes for and 22 votes against ratification; anti-paper money towns favored
ratification 29 to 7.] The hard (or less soft) money towns in New Hampshire were Federal; most of
the Antifederal strength in Connecticut was found in paper money districts; and the case of Rhode
Island is sufficiently familiar. … In Maryland and Virginia the paper money forces opposed
ratification. This was also the case in North Carolina, while in South Carolina, Antifederal
strength lay in the backcountry, which had favored inflation. … All the foregoing does not prove
an exact correlation… There are…exceptions… Leaving aside the fact that many Antifederalist, especially the leaders, specifically denounced state currency emissions, we have to consider the following exceptions: (1) in South Carolina, a large number of planters, most of whom became Federalist, supported paper emission; … (4) New Jersey endorsed both paper money and the Constitution; (5) in Pennsylvania, although it is probable that a majority of the people were Federal, a majority favored paper money… That paper money sentiment was in some degree a factor in the existence of Antifederalism is scarcely to be doubted—the Antifederalists drew more heavily by far than their opponents from the ranks of paper money advocates…

18 The following is Madison’s description of how he took notes at the Convention: “I chose a seat in front of the presiding member, with the other members, on my right and left hand. In this favorable position for hearing all that passed I noted in terms legible and in abbreviations and marks intelligible to myself what was read from the Chair or spoken by the members; and losing not a moment unnecessarily between the adjournment and reassembling of the Convention I was enabled to write out my daily notes during the session or within a few finishing days after it closed.” (Farrand I, xvi).

19 Because New York did not vote at the Convention after July 10th, Hamilton may not have paid close attention to specific debates even when he was in attendance. Robert Yates and John Lansing, the other delegates from New York, left the Convention after July 10th and did not return. (Farrand I, II, III).

20 Hamilton’s role here is difficult to fathom, in particular his silence during the Convention on the issue of banks, especially on the crucial day in question—September 14th. None of Hamilton’s recorded statements at the Convention, including his plan of government, mention banks or the power to charter a national bank (Farrand I, II, III). However, before the Convention, Hamilton had long advocated that the National Government be given the power to charter banks (Holdsworth 9-19). As early as 1780, in a letter to James Duane, his proposed “remedies” to the Articles of Confederation included that a national “Convention should assemble” and grant Congress the power of “establishing banks…” (Freedman 76-77). After the Convention as Secretary of the Treasury under the first Washington administration, Hamilton was the chief architect and proponent of Congress’ right to charter a national bank, i.e. the First Bank of the U.S. (Freeman 575-646). Reconciling Hamilton’s very active argumentation and pursuit of a national bank both before and after the Convention with his silence during the Convention on this issue is hard to do without regarding Hamilton as being strategically cunning and deceptive (Grubb 2003, 1791). Perhaps Hamilton considered banking to be too controversial, whose positive mention might excite too much opposition at the Convention, and/or kill the Constitution’s chances of ratification. Perhaps Hamilton
thought if he “played possum” he could get his way and have a national bank no matter what the Convention intended as long as the Convention did not absolutely ban national banking by written clause in the Constitution.

21 In a letter to James Madison, dated 20 June 1791, George Nicholas concluded, “The Bank &c. [First Bank of the U.S.] prove that paper barriers [the U.S. Constitution] are very weak; could it have been foreseen that no greater regard would have been paid them many federalists would have been the warmest opposers of the government.” (Rutland XIV, 33).

22 For example, as early as 1780 Hamilton, in a letter to James Duane, confided,

And why can we not have an American bank? Are our monied men less enlightened to their own interest or less enterprising in the pursuit? I believe the fault is in our government which does not exert itself to engage them in such a scheme. … The only certain manner to obtain a permanent paper credit is to engage the monied interest immediately in it by making them contribute the whole or part of the stock and giving them the whole or part of the profits. (Freeman 83-84).

23 For example, during the South Carolina ratification debates, Pinckney referred to “…the emission of paper money and its consequences, tender-laws, and the impairing the obligation of contracts.” (Elliot 334 [italics added]).

24 For example, Pinckney’s argument in his post-Convention speech for constitutionally banning paper money made during South Carolina’s ratification debates is consistent with this position (Elliot 334).

25 For an up-to-date discussion of these issues for contemporary economies, see Feldstein (1-92).

26 In the 19th century, the U.S. Supreme Court ruled that under the “Necessary and Proper” clause of the Constitution the Federal Government had the Constitutional power to emit bills of credit and to incorporate a national bank (Warren 696, 700-701). Article 1, Section 8 of the U.S. Constitution enumerates the new and enlarged powers of the National Government. It concludes with the following phrase: “To make all Laws which shall be necessary and proper for carrying into Execution the foregoing Powers…” That the Supreme Court found that this “Necessary and Proper” clause trumped powers explicitly voted not to be included in the list of “foregoing Powers” is difficult to comprehend, unless the Supreme Court engaged in definitional creep—turning the words “Necessary and Proper” into the words “Expedient and Desired.”