

The Defects of the Articles of Confederation, Part 10

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Synopsis: This is the tenth in a series on the difficulties encountered under the Articles of Confederation. In this edition, the general problem of coinage and currency is considered.

In order to fully appreciate the situation regarding coinage and debt under the Articles of Confederation, and how it was addressed by the Constitution, it is necessary to review some basic facts. First, Congress became the symbol of the Revolution as the only institution recognized by all the states. Secondly, it came into being under emergency circumstances in order to coordinate the war effort. Recognizing a need for a formal arrangement governing relations among the states, the men of Congress first proposed the Articles of Confederation shortly after the Declaration of Independence, but they were not established in final form until November of 1778, when they were submitted to the state legislatures for consideration. They did not go into effect until all thirteen states had sanctioned them which occurred in March of 1781. The provisions concerning money and credit are as follows:

[Paragraph 4 of Article IX] The United States, in Congress assembled, shall also have the sole and exclusive right and power of regulating the alloy and value of coin struck by their own authority, or by that of the respective States; fixing the standard of weights and measures throughout the United States; regulating the trade and managing all affairs with the Indians not members of any of the States; provided that the legislative right of State, within its own limits, be not infringed or violated; establishing and regulating post-offices from one State to another throughout all the United States, and exacting such postage on the papers passing through the same as may be requisite to defray the expenses of the said office; appointing all officers of the land forces in the service of the United States, excepting regimental officers; appointing all the officers of the naval forces, and commissioning all officers whatever in the service of the United States; making rules for the government and regulation of said land and naval forces, and directing their operations.

[Paragraph 7 of Article IX] The United States, in Congress assembled, shall never engage in war, nor grant letters of marque and reprisal in time of peace, nor enter into any treaties or alliances, nor coin money, nor regulate the value thereof, nor ascertain the sums and expenses necessary for the defense and welfare of the United States, or any of them, nor emit bills, nor borrow money on the credit of the United States, nor appropriate money nor agree upon the number of vessels of war to be built or purchased, or the number of land or sea forces to be raised, nor appoint a commander-in-chief of the army or navy, unless nine States assent to the same, nor shall a question on any other point, except for adjourning from day to day, be determined, unless by the votes of a majority of the United States, in Congress assembled.

Article XII. All bills of credit emitted, moneys borrowed, and debts contracted by or under the authority of Congress, before the assembling of the United States, in pursuance of the present Confederation, shall be deemed and considered as a charge against the United States, for payment and satisfaction whereof the said United States and the public faith are hereby solemnly pledged.

Under Art. IX, paragraph 4, Congress had the power to regulate the nature of coin, but the states were allowed to coin their own money under that regulation. The states also had the power (already existing) to issue their own paper currency. Under paragraph 7 of Art. IX, Congress had the power to issue "bills of credit", which are notes issued on the credit of the United States; they functioned in the same manner as

a paper currency. Last, Article XII states that Congress shall be liable for full payment of all debts and bills of credit issued before the Articles are ratified. That means we must first review the progression of the "Continental money", which was mostly issued as bills of credit, but occasionally as paper currency. These were issued directly by Congress as shown in Figure 1, denominated in dollars, ostensibly to be regarded at the same value as the Spanish milled dollar (SM\$) then in common use (reckoned as 386.7 grains of silver). The reckoned value of the Continental bills of credit and currency depreciated rapidly, and those estimates compared to the Spanish dollar are given in the Comment column.

Date of Issue	Amount (\$)	Form	Comment
29 Nov 1775	3,000,000	bills of credit	
1 Mar 1776	4,000,000	bills of credit	
9 May 1776	5,000,000	bills of credit	
28 Dec 1776	5,000,000	bills of credit	
26 Feb 1777	5,000,000	bills of credit	Continental commonly valued at SM\$ 0.80
20 May 1777	5,000,000	bills of credit	
1 Aug 1777	1,000,000	bills of credit	Continental commonly valued at SM\$ 0.40
15 Aug 1777	1,000,000	bills of credit	
7 Nov 1777	1,000,000	bills of credit	
3 Dec 1777	1,000,000	bills of credit	
8 Jan 1778	1,000,000	bills of credit	Continental commonly valued at SM\$ 0.25
22 Jan 1778	2,000,000	bills of credit	
16 Feb 1778	2,000,000	bills of credit	
4 Apr 1778	1,000,000	paper currency	
11 Apr 1778	5,000,000	bills of credit	
18 Apr 1778	500,000	paper currency	
22 May 1778	5,000,000	paper currency	
20 Jun 1778	5,000,000	paper currency	Continental commonly valued at SM\$ 0.25
30 Jul 1778	5,000,000	paper currency	
5 Sep 1778	5,000,000	paper currency	
26 Sep 1778	10,000,000	bills of credit	
4 Nov 1778	10,000,000	bills of credit	
14 Dec 1778	10,000,000	bills of credit	Continental commonly valued at SM\$ 0.14
14 Jan 1779	50,000,400	bills of credit	
3 Feb 1779	5,000,160	bills of credit	
19 Feb 1779	5,000,160	bills of credit	
1 Apr 1779	5,000,160	bills of credit	Continental commonly valued at SM\$ 0.05
5 May 1779	10,000,100	bills of credit	
4 Jun 1779	10,000,100	bills of credit	
17 Jul 1779	10,000,100	bills of credit	
17 Jul 1779	5,000,180	paper currency	
17 Sep 1779	10,000,100	bills of credit	
17 Sep 1779	5,000,180	paper currency	
14 Oct 1779	5,000,180	paper currency	
17 Nov 1779	5,000,040	bills of credit	
17 Nov 1779	5,050,500	paper currency	
29 Nov 1779	10,000,140	bills of credit	Continental commonly valued at SM\$ 0.025

Figure 1: Issues of "Continental" Bills of Credit and Paper Currency by Congress 1775 - 1779

By the end of 1779, the "Continental" was worth about 2 cents in hard money; by Jun 1780, it was valued at about one cent. It then became the object of ridicule and simply went out of circulation. Finally, on 11 Jul 1780, Congress published a redemption schedule for all the Continental bills and currency: they would be redeemed at 40 to 1 (SM\$ 0.025), although their reckoned value by that time was about 65 to 1 (i.e., worth about SM\$ 0.015). Thus the \$232,000,000 or so Continentals that had been issued ultimately was reduced to SM\$ 5,800,000 in actual redemption value. Because Congress could not raise any revenue on its own, as mentioned in Part 9 of this series, this was simply added to the national debt. Keep in mind that all this occurred prior to the formal operation of the Articles of Confederation (2 Mar 1781). What happened to all the people that accepted the Continental at face value? They were robbed.

Why did the Continental depreciate so quickly? For the same two reasons any fiat currency depreciates: a) in the short run, the issuer knows it has no value that he is responsible for, so he issues as much as he can without startling the public or the business community; and b) in the long run, the public loses confidence in it once they realize it has no true value. These explain why every fiat currency requires a "legal tender" law in order to force the public and the business community to pretend that it actually does have value. That continues until the issuer decides to get out of the business (having made his money on interest payments) and simply abolishes the fiat currency, thus robbing those who accepted it. Going back to the case of the Continental, Congress issued it under emergency conditions, that is, to fight the war against Britain. Perhaps it was necessary and justifiable to do so, given the enormous benefits to be derived from independence; but it corrupted the economy.

The states had also issued a great deal of paper money during the war, and their currency had also depreciated somewhat. Although the Articles permitted Congress to issue bills of credit, it no longer did so, having learned its lesson from the history of the Continental currency. But the evil of paper money was not solved thereby, since some of the states continued to issue paper money after the war, which also depreciated. Georgia redeemed its paper money at 1,000 to 1 in Feb 1785; Delaware redeemed its paper in the same month at 75 to 1. Pennsylvania issued paper money in May 1785; by Aug 1786, it had already depreciated 12%. South Carolina issue paper currency in Oct 1785; followed by North Carolina in Nov 1785, New York in Mar 1786; New Jersey and Rhode Island in May 1786; and Georgia in Aug 1786. By Aug 1786, New Jersey's currency had become worthless, and Rhode Island's paper had depreciated to 4:1. The other paper issued by the states suffered similar fates, especially in North and South Carolina. It was the debate over paper currency that started Shays' rebellion in Massachusetts (a case where the people wanted it).

Simply issuing paper at the state level was not the only problem; it was coupled with constant alterations in its official value, which affected contracts between parties in different states. Certainly there is no incentive to extend credit if the currency can be manipulated, or as in South Carolina and Virginia, terms of contracts were altered to allow payments in land or tobacco, or as again in South Carolina, contracts were altered to require different payment schedules.

Such was the situation at the Constitutional Convention in 1787. Providing Congress a power to borrow money and establish coinage was agreed to easily. Likewise, the states were prohibited from coining money or issuing bills of credit; furthermore, only gold and silver could be made legal tender in the states. The corrective provisions in the U. S. Constitution read:

[Article I, Section 8] The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defence and general Welfare of the United States; but all Duties, Imposts and Excises shall be uniform throughout the United States;
To borrow money on the credit of the United States;

[Article I, Section 10] No State shall enter into any Treaty, Alliance, or Confederation; grant Letters of Marque and Reprisal; coin Money; emit Bills of Credit; make any Thing but gold and silver Coin a Tender in Payment of Debts; pass any Bill of Attainder, ex post facto Law, or Law impairing the Obligation of Contracts, or grant any Title of Nobility.

It is of great interest while on this subject to examine the debate in the Constitutional Convention about whether the federal government shall have a power to emit bills of credit. A draft had been presented on 6 Aug 1787, containing a provision [Art. VII, Section 1] stating "The legislature of the United States shall have the power ... to borrow money, and emit bills, on the credit of the United States." This clause was debated on 16 Aug 1787, as follows [1]:

Mr. Gouverneur Morris moved to strike out "and emit bills on the credit of the United States." If the United States had credit, such bills would be unnecessary; if they had not, unjust and useless.

Mr. Butler seconds the motion.

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 moneyed 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.

Mr. 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.

Mr. 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 and temper of America, he should neither propose or 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 mischief's 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 anything else. 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 money. This expedient can never succeed whilst its mischief's 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 Revelation.

Mr. Langdon had rather reject the whole plan, than retain the three words, "and emit bills."

On the motion for striking out, --

New Hampshire, Massachusetts, Connecticut, Pennsylvania, Delaware, Virginia, North Carolina, South Carolina, Georgia, aye, 9; New Jersey, Maryland, no, 2.

The clause for borrowing money was agreed to, *nem. con.*

Adjourned.

Elliot added a footnote regarding Virginia's positive vote to strike out "and emit bills." It reads:

"This vote in the affirmative by Virginia was occasioned by the acquiescence of Mr. Madison, who became satisfied that striking out the words would not disable the government from the use of public notes, as far as they could be safe and proper; and would only cut off the pretext for a paper currency, and particularly for making the bills a tender, either for public or private debts."

Madison defended this view more directly in the *Federalist Papers* #44:

The right of coining money, which is here taken from the States, was left in their hands by the Confederation, as a concurrent right with that of Congress, under an exception in favor of the exclusive right of Congress to regulate the alloy and value. In this instance, also, the new provision is an improvement on the old. Whilst the alloy and value depended on the general authority, a right of coinage in the particular States could have no other effect than to multiply expensive mints and diversify the forms and weights of the circulating pieces. The latter inconveniency defeats one purpose for which the power was originally submitted to the federal head; and as far as the former might prevent an inconvenient remittance of gold and silver to the central mint for recoinage, the end can be as well attained by local mints established under the general authority.

The extension of the prohibition to bills of credit must give pleasure to every citizen, in proportion to his love of justice and his knowledge of the true springs of public prosperity. The loss which America has sustained since the peace, from the pestilent effects of paper money on the necessary confidence between man and man, on the necessary confidence in the public councils, on the industry and morals of the people, and on the character of republican government, constitutes an enormous debt against the States chargeable with this unadvised measure, which must long remain unsatisfied; or rather an accumulation of guilt, which can be expiated no otherwise than by a voluntary sacrifice on the altar of justice, of the power which has been the instrument of it. In addition to these persuasive considerations, it may be observed, that the same reasons which show the necessity of denying to the States the power of regulating coin, prove with equal force that they ought not to be at liberty to substitute a paper medium in the place of coin. Had every State a right to regulate the value of its coin, there might be as many different currencies as States, and thus the intercourse among them would be impeded; retrospective alterations in its value might be made, and thus the citizens of other States be injured, and animosities be kindled among the States themselves. The subjects of foreign powers might suffer from the same cause, and hence the Union be discredited and embroiled

by the indiscretion of a single member. No one of these mischief's is less incident to a power in the States to emit paper money, than to coin gold or silver. The power to make any thing but gold and silver a tender in payment of debts, is withdrawn from the States, on the same principle with that of issuing a paper currency.

[1] Jonathan Elliot, *Debates on the Adoption of the Federal Constitution in the Convention Held at Philadelphia in 1787, With a Diary of the Debates of the Congress of the Confederation; As Reported by James Madison*, Philadelphia: J. B. Lippincott & Co., 1881, Vol. 5, pp. 434, 435