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## **Gold and Freedom, Part 2**

**by Jacob G. Hornberger**

The Framers had experienced the ravages of paper money during the Revolutionary War and under the Articles of Confederation, and they were fully aware of how governments had plundered and looted their own citizenry with inflation throughout history. Therefore, the Framers used the Constitution to ensure that neither the states nor the federal government could ever do that to the American people.

The result was that from the founding of the nation and for more than a century, the money that the American people used was coins consisting of gold, silver, nickel, and copper. People became accustomed to transacting business with such coins. It was that type of monetary system — one in which people used coins made of precious and non-precious metals — that became known as “the gold standard.”

It wasn't a purely free-market standard. The U.S. government was in charge of minting America's coins and, therefore, of defining the weight and fineness of the coins. Moreover, the government established a policy of defining the exchange ratio between gold and silver, a price control that would inevitably be out of sync with changing market conditions and that often led people to hoard one metal or the other.

What was important, however, was that the monetary standard for the United States was a metallic one, not one based on paper money. It's important to conceptualize what the “gold standard” meant. It did not mean some exchange ratio between paper money and gold. Instead, the “gold standard” meant that gold coins, silver coins, nickel coins, and copper coins were the money that the American people had chosen to use in their society.

### **Liberty, power, and the Constitution**

Let's examine how the Framers used the Constitution to establish a government of limited powers and then examine how it protected Americans from the ravages of inflation with the establishment of a gold standard.

First of all, keep in mind the overall political philosophy that was guiding the Framers and the Americans during the founding of the nation. While Americans believed that a federal government was necessary, they also believed that it would nonetheless constitute the greatest threat to their freedom and well-being. Unlike so many Americans today, who view the federal government as their provider and caretaker, our American ancestors looked upon the federal government as a very dangerous entity, one that needed to be watched very carefully.

One can see this mindset most clearly in the Bill of Rights, which actually should have been called the Bill of Prohibitions. Behind every one of the prohibitions and guarantees in those Amendments was the conviction held by the people that in the absence of such express prohibitions and guarantees, the federal government would engage in the conduct that was prohibited or proscribed.

The reason that the First Amendment prohibited Congress from enacting any law abridging freedom of speech and freedom of the press, for example, was that in the absence of such an amendment, Congress would enact laws that would infringe such freedoms.

The reason the Second Amendment guarantees the right to keep and bear arms was that in the absence of such an express guarantee, federal officials would confiscate weapons from the citizenry in order to maintain order, stability, and obedience.

The same goes for criminal cases in which the government seeks to incarcerate and punish people. Express guarantees prohibiting unreasonable searches and seizures and cruel and unusual punishments, and relating to due process of law, right to counsel, and right to bail were included because our ancestors knew that federal officials would ignore the people's rights and liberties in the absence of express restrictions.

The cornerstone of American society was private property, whose protection was guaranteed in the original Constitution as well as in the Due Process Clause and the Just Compensation Clause in the Bill of Rights. Realizing that the institution of private property was a necessary prerequisite for a free society, the Constitution and the Bill of Rights prohibited federal officials from arbitrarily confiscating people's money, land, and other property. There was also an express restriction prohibiting the states from impairing private contracts.

All those enumerated powers and express prohibitions and guarantees reflected the mindset of the Framers. Since they viewed the federal government as the greatest danger to the freedom and well-being of the American people, they decided to use the Constitution not only to call the federal government into existence but also, at the same time, to limit its powers to those that were expressly enumerated.

In other words, one option would have been to delegate to the federal government general, unlimited powers to take whatever actions federal officials deemed to be in the best interests of the American people. That's not the option the Framers chose, because they knew that such a government would inevitably oppress the citizenry.

What they did instead was to make it clear that the government the Constitution was calling into existence would be one with very few, limited powers. The federal government's powers would be limited to those expressly enumerated in the Constitution. If a power wasn't enumerated, the federal government couldn't exercise it, even if federal officials deemed it to be in the best interests of the citizens.

### **The Constitution and gold**

How did the Framers protect the American people from the ravages of inflation, which had beset people for centuries?

First, the Constitution granted the federal government the power to coin money and to regulate its value in accordance with a fixed standard of weights and measures.

Second, it did not grant the federal government the power to issue paper money or the power to debase the currency.

Third, while the Framers did grant the federal government the power to borrow, they refused to grant the power to make bills and notes legal tender. In other words, the government lacked the power to force people to accept its bills and notes in ordinary transactions or in payment of debts.

Fourth, the Framers expressly prohibited the states from issuing paper money, or what was commonly called "bills of credit."

Fifth, the Framers expressly prohibited the states from making anything but gold and silver coins legal tender.

Thus, it was clear that the Framers intended the United States to operate on a precious-metals standard, one in which gold coins, silver coins, and copper coins were the money in society.

In fulfillment of that intention, Congress enacted the Coinage Act of 1792, which established the U.S. Mint and provided for the minting of coins that would be based on a dollar unit of value. For example, there were silver dollars and silver half-dollars and \$10 gold Eagles and \$5 Half-Eagles.

### **A heritage of economic liberty**

While statisticians love to regale us with stories of how horrible the Industrial Revolution was, the truth is that compared with what had gone on before, the Industrial Revolution was providing people with the means to escape death by starvation. Before long and as wealth began being accumulated, people were not only surviving, they were actually prospering.

Part of the reason for this remarkable outburst in economic prosperity was the fact that our Americans ancestors had rejected income taxation. Thus, through most of the 19th century,

Americans could keep everything they earned and there was nothing the federal government could do about it.

It was also a society in which there was a lack of economic regulation on the part of the government. That's what "free enterprise" meant — economic activity that was free of government control.

There was no socialism — no Social Security, Medicare, Medicaid, public schooling, education grants, foreign aid, or welfare.

There was no large standing army, no foreign aid, no foreign wars, no entangling alliances, and no overseas empire.

There were no controls on immigration, except for a cursory health inspection at Ellis Island.

All those factors contributed to the unbelievable rise in the standard of living of the American people. People were going from rags to riches in one, two, or three generations. They included the thousands of penniless immigrants who were fleeing the lands of taxation, regulation, socialism, conscription, militarism, and empire to come to the land of self-reliance, independence, voluntary charity, and limited government.

### **Savings, capital, and gold**

Another critically important factor in the economic prosperity, however, was the gold standard. For the first time in history, people felt safe from the threat that had besieged people throughout history — the threat that government officials would take away their wealth by debasing their currency.

Equally important was the positive effect that the gold standard had on capital markets. Companies were issuing bonds with a 100-year maturity date, with the proviso that the loan had to be paid back in a specified amount of gold or the same unit of value as when the bond was issued. In other words, no repayment in debased, inflated paper currency. Thus, people were willing to buy such long-term bonds because they didn't fear being paid back in depreciated currency. The massive accumulation of capital, brought about by the absence of an income tax, the propensity of people to save, and the existence of sound money, was among the critical factors that brought about an enormous increase in real wages in the 19th century.

Since America's money consisted of gold coins, silver coins, and copper coins, people knew that the federal government couldn't easily inflate the currency. After all, it's much more difficult to arbitrarily increase the supply of gold, silver, and copper than it is to increase the supply of paper money. Mining for precious metals can be expensive, while simply printing money off a printing press is much less onerous.

Of course, the federal government could have "clipped the coins," as regimes of old had done, leaving the coins with less gold and accumulating the shavings for government use. But the

federal government didn't do that. While there were sometimes controversial adjustments in the weight or fineness of U.S. coins as well as in the exchange ratio between the coins, by and large U.S. coins were renowned for their quality and trustworthiness.

That's not to say that there weren't periodic increases in the supply of money, but at least they were localized or brought about by unusual market conditions rather than by government policy. A new gold discovery in California, for example, would increase the supply of gold overnight, causing prices of everything to go up in relationship to gold. It was the gold and silver coins that were the money, not the federal government's dollar bills.

By and large, the American people had confidence in the ability of their coins to hold their value. The consequence was that people were saving vast amounts of money, oftentimes passing it from one generation to the next. Thus, not only could people leave their children large sums of money that had been accumulated from the fact that there was no income tax, but they knew that federal officials lacked the power to ravage those savings with inflation.

### **Borrowing and gold**

What about the federal government's power to borrow, which was among the enumerated powers granted in the Constitution? In principle, the power entailed nothing different from ordinary citizens' borrowing money. For example, people would lend gold coins to the government.

To evidence the debt, the government would issue a promissory note, which promised to repay the lender the gold that was being borrowed. Everyone understood that it was the gold and silver coins that were the money, not the government's notes. The notes were promises to pay money, not money itself.

Of course, there was nothing to prevent the federal government from simply printing an excess number of notes and using them to pay for goods and services in the marketplace, except that by doing so, it would run the risk that everyone would show up at the government's gold window and demand to have the promissory notes redeemed in gold coin. Thus, an excess issue of notes would, at some point, result in the bankruptcy of the government. That possibility operated as a very real constraint on excessive government spending.

All this is like ancient history to today's Americans. They've heard of the "gold standard" but it's a vague concept in their minds. They might be somewhat aware that gold coins, silver coins, and copper coins once circulated in American society, but most of them have no idea of the integral part the gold standard played in the lives of our American ancestors.

Most Americans today have no idea why a gold standard was important to our ancestors. The notion that a gold standard was established to protect them from the federal government is an alien notion to most people.

To most people today, the gold standard was a system in which the federal government's paper bills and notes were the real money, which was "linked" to some fixed amount of gold.

When people pull out a Federal Reserve Note from their billfolds or wallets, it never occurs to them to ask why it's called a "note," given that it's not promising to pay anything. They have no idea that the "note" is a cruel reminder of a bygone era in which the American people once had a monetary system based on sound money rather than on irredeemable notes issued by the Federal Reserve.

What happened to the gold standard on which the United States was founded? What happened to all those gold and silver coins that Americans used to use in their day-to-day transactions? Why do people use irredeemable paper money today instead of coins made of precious metals? What happened to bring about such a monumental, even revolutionary, change in America's monetary system? Why do so few Americans know what happened and why it happened?

The answers to those questions require an examination into the economic policies of two presidents: Abraham Lincoln and Franklin D. Roosevelt.

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**This article was originally published in the May 2009 edition of *Freedom Daily*.**