[SUBCOMMITTEE PRINT]

A PRIMER ON MONEY

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Who issues currency?

In the United States only the Federal Government may print currency. Specifically, the Federal Reserve banks issue Federal Reserve notes. As the table indicates, about 94 percent of all currency in circulation consists of Federal Reserve notes. However, the U.S. Treasury itself did issue some silver certificates and U.S. notes. The Treasury only recently ceased issuing silver certificates. For all practical purposes, only the Federal Reserve now issues paper money.

What backs the Treasury currency?

The Treasury currency in circulation today is largely silver certificates. By law, the Government requires the Treasury to keep on deposit a certain amount of silver to 'back" silver certificates. The Treasury must do the same for the Treasury notes of 1890. This means that anyone holding silver certificates can obtain silver for them on demand. The Treasury's legal reserve of silver amounts to about two-thirds the value of the silver certificates in circulation.

What backs the Federal Reserve notes?

Behind the Federal Reserve notes is the credit of the U.S. Government. If you happen to have a $5, $10 or $20 Federal Reserve note, you will notice across the top of the bill a printed statement of the fact that the U.S. Government promises to pay, not that the Federal Reserve promises to pay. Nevertheless, most Americans don't realize what the Government promises to pay: American citizens holding these notes cannot demand anything for them except *(a)* that they be exchanged for other Federal Reserve notes, or *(b)* that they be accepted in payment for taxes, and all debts, public and private. Certain official or semiofficial foreign banks may exchange any "dollar credits" they may hold—that is, deposits with the commercial banks—for an equal amount of the Treasury's gold. Americans themselves may not exchange them for gold. But because, in commerce with foreign nations, Americans may pay in gold, gold actually "backs[5]" American dollars.

Who *issues ^checkbook* money?

The private commercial banks issue "checkbook **money."** The next chapter will show the mechanics of how they do it, and how the Federal Reserve controls the amount of "checkbook money" **they** may create. Right now, it is just necessary to see what is meant **by** saying that the commercial banks create demand deposits, which may be exchanged for currency or coin anytime the depositor wishes.

Imagine there is only one bank in the country and that it has two private depositors, each with $50 in his **checking** account. Total bank demand deposits would then be $100. Suppose John Jones asked for a $50 loan from the bank, and the bank approved the loan. The bank would then lend the money to Mr. Jones by simply opening a **checking** account for him and depositing $5.0 in it. This is what ordinarily happens when anyone—business or private individual—borrows from a bank. The bank deposits the amount of the loan in the relevant checking account.

In making the loan to Mr. Jones, the bank did not reduce anyone's previous bank balance. It simply credited the Jones account with $50. The total amount held in bank demand deposits now becomes **$150.** The bank has, therefore, issued $50 in "checkbook money."

The natural question to ask is, Where does the bank get the additional $50 to issue and lend to Mr. Jones? The answer, as will become clear in the next chapter, is that the bank did not "get" the money at all. *Money has been created.* Of course, the bank's power to create money is limited. And a later chapter will show that the Federal Reserve sets the limits of this power to create money.

Did the State 'banks stop creating their own money after the Federal Government passed the National Bank Act ?

Although the State banks ceased issuing bank notes, they continued to create money, in the form of bank deposits, just as they do today. In fact, as "checkbook money[95] has become increasingly popular, State banks have continued to create money in this form. They now create more of this kind of money than before the Government passed the National Bank Act. This act merely stopped the State banks from printing and issuing *currency.*

Who should have the power to create money?

The power to create money is an inherent power of Government. **As** President Lincoln said:

> The privilege of creating and issuing money is not only the supreme prerogative of the Government, it is the Government's greatest opportunity.

During the past several centuries, various governments in the Western World have, at various times, delegated the money-creating power to private groups or had this power taken from them by default. In these situations, control of the Nation^ affairs has been not so much in the hands of the official head of state, but in the hands of the private groups controlling the money system. A famous British banker once summed up the matter this way:

> They who control the credit of the nation direct the policy of governments, and hold in their hands the destiny of the people. (Reginald McKenna, Chancellor of the Exchequer in Britain during the World War I period.)

As we look over human history, we find that the tribal chief, the king, the pharaoh, or the emperor has usually had direct or indirect control of the society's money. In the modern, constitutional governments, one or another branch of the government is given responsibility for establishing and managing the money system. *In* the United States, the Constitution gives these powers to the Congress.

Does the Constitution^ which mention's only the power to "coin" " "money " give Congress sole power over all money?

Yes. Article 1, section 8, paragraph 5, of the Constitution provides that "the Congress shall have power to coin money, regulate the value thereof, and of foreign coin.[55] It is generally agreed that only the word "coin" was used because there were no banks of issue in the country at the time the Constitution was written, and the Founding Fathers assumed that coins would always meet the needs for lawful money.

Over the past century and a half, many questions about Congress powers over the Nation's^ money system have arisen, and the Supreme Court has upheld the proposition that "whatever power there is over the currency is vested in the Congress."