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# The Gold Clause Decisions

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## *The Gold Clause Decisions*

It is a conservative estimate that existing contracts call for payment in seventy-five billions of gold dollars of a weight forty per cent greater than

<sup>30</sup> *People v. Hotz* (1927), 327 Ill. 433, 158 N. E. 743; *Gibson v. Commonwealth* (1925), 209 Ky. 101, 272 S. W. 43; *Lawton v. Steele* (1890), 119 N. Y. 226, 23 N. E. 878 (Aff. 152 U. S. 133); *Lawton Spinning Co. v. Commonwealth* (1919), 232 Mass. 28, 121 N. E. 518; *Caldwell v. State* (1918), 187 Ind. 617, 119 N. E. 999; *State v. Barrett* (1909), 172 Ind. 169, 87 N. E. 7; *Henderson v. State* (1894), 137 Ind. 552, 36 N. E. 257; *State v. Indiana & Ohio Gas & Mining Co.* (1889), 120 Ind. 575, 22 N. E. 778.

<sup>31</sup> *Davis v. Wallace* (1922), 257 U. S. 478; *Pollock v. Farmers' L. & T. Co.* (1895), 158 U. S. 601; *Foster v. College Park* (1923), 155 Ga. 174, 117 S. E. 84; *In re Gates* (1926), 243 N. Y. 193, 153 N. E. 45.

<sup>32</sup> *United States v. Missouri Pac. Ry.* (1914), 213 Fed. 169; *State v. Ruesswig* (1910), 110 Minn. 473, 126 N. W. 279; *Ex parte Alpine* (1928), 203 Cal. 731, 265 Pac. 947; *Commonwealth v. Florence* (1921), 192 Ky. 236, 232 S. W. 369; *Jones v. Lawson* (1920), 143 Ark. 83, 220 S. W. 311; *Board of Education v. Morgan* (1925), 316 Ill. 143, 147 N. E. 34; *Drake v. Drake* (1833), 15 N. C. 91; *Hallman v. Coker* (1921), 147 Ark. 226, 226 S. W. 1054.

<sup>33</sup> *Commonwealth v. Philadelphia Rapid Transit Co.* (1926), 287 Pa. 70, 134 Atl. 452; *State v. Humble Pipe Line Co.* (1923), 112 Tex. 375, 247 S. W. 1082.

that which the dollar contains today. Three to four billions of dollars in gold have been demanded annually as interest upon this principal indebtedness. Small wonder, then, that critics from the press, from the academy of economics, and from the bar have pronounced the decision of the United States Supreme Court upholding the constitutionality of a Congressional enactment abrogating gold clauses in private contracts as the most important decision of a half century. The decision of *Norman v. Baltimore & O. R. Co.*,<sup>1</sup> sustaining abrogation of a gold clause in a private contract, proceeds upon an entirely different rationalization than the holding of the Court in the cases of a gold certificate<sup>2</sup> and of a government bond<sup>3</sup> calling for payment in gold. The cases will be considered separately.

An understanding of the import of these decisions necessarily demands a knowledge of the legislation from which these conflicts arose and the social and economic turmoil which inspired that legislation. The United States was burdened with an indebtedness of two hundred and fifty billions of dollars.<sup>4</sup> That indebtedness represents a credit structure founded upon an expectation of earning power impossible of realization. Partial collapse was imminent. Forced repudiation, bankruptcy, and all the ills of economic chaos threatened this nation. It was imperative that social control be introduced through Congressional legislation designed to reduce this indebtedness to a point commensurate with the earning power of our people. With cognizance of these facts, Congress enacted the Agricultural Adjustment Act of 1933<sup>5</sup> authorizing the President to revise the weight of the gold dollar downward to fifty per cent of its then existing weight of twenty-five and eight-tenths grains. The social interests which Congress purported to protect by this measure were set forth as the stabilization of domestic prices and, further, to protect the foreign commerce from the adverse effects of depreciated foreign currency. On June 5, 1933, by Joint Resolution of Congress,<sup>6</sup> gold clauses in private and public contracts were said to be contrary to public policy whether heretofore or hereafter incorporated in contracts. In an effort to assure uniform values to the coins and currency of the United States, this act provided that payment of all contracts calling for amortization in gold should be dollar for dollar in present legal tender currency. Pursuant to the Gold Reserve Act of 1934,<sup>7</sup> the President set the gold content of the dollar at fifteen and five-twenty-firsts grains. Additional measures required that all

<sup>1</sup> *Norman v. Baltimore & O. R. Co.*, *United States v. Bankers' Trust Co.* (1935), 55 S. Ct. 407. On Writ of Certiorari to the Supreme Court of the State of New York and to the United States Circuit Court of Appeals for the Eighth Circuit.

*Norman*, plaintiff, brought this suit upon a coupon of a bond executed by the *Baltimore & O. R. Co.*, demanding the equivalent of gold coins containing 25.8 grains, nine-tenths fine. The New York Court of Appeals gave judgment for plaintiff in an amount less than demanded.

In *United States v. Bankers' Trust Co.*, the *Trust Co.* intervened as trustees under a mortgage securing bonds issued by the assignor of the petitioner in bankruptcy. The trustees asked that the income from the property be applied to amortize the mortgage debt which was payable under the contract in gold coins containing 25.8 grains. The *United States*, a creditor of the debtor, intervened with a denial of the legality of the gold clause contained in the bonds.

<sup>2</sup> *Nortz v. United States* (1935), 55 S. Ct. 428.

<sup>3</sup> *Perry v. United States* (1935), 55 S. Ct. 432.

<sup>4</sup> *Eddie*, Principles and Problems of Economics, ch. 25; Fairchild, Furnis and Buck, Elementary Economics, Vol. 2, ch. 38; Gemmill, Contemporary Economics, Ch. 31; Taussig, Principles of Economics, Vol. 2, Ch. 35; Report of a Commission on Industrial Relations for 1915.

<sup>5</sup> 48 Stat. 51.

<sup>6</sup> 48 Stat. 112.

<sup>7</sup> 48 Stat. 337.

gold bullion, coins, and gold certificates be delivered into the Treasury.<sup>8</sup> All traffic in gold was thereby prohibited.

In *Norman v. Baltimore & O. R. Co.*<sup>9</sup> the Supreme Court accurately interpreted the contract as an obligation for the payment of money rather than a commodity contract to be performed by the delivery of gold bullion or gold coins. Gold clauses have no other purpose than the protection of the obligee in the event of currency depreciation. Although the case of *Bronson v. Rodes*<sup>10</sup> interpreted a gold clause as a commodity contract, a later decision in *Treblicock v. Wilson*<sup>11</sup> recognized that this clause was descriptive of a type of money. Under either construction of the contract the Joint Resolution was a taking of property without due process of law unless Congress acted within the ambit of its delegated powers.

That Congress may emit bills of credit making them legal tender for the payment of debts was decided in the *Legal Tender Cases*<sup>12</sup> and in *Julliard v. Greenman*.<sup>13</sup> These decisions overruled the case of *Hepburn v. Griswold*.<sup>14</sup> As a proper and appropriate incident to the express powers of Congress to regulate the currency and to borrow money on the credit of the United States, the issue of fiat money was declared constitutional. The Court refused to extend the character of legal tender to these notes when the contract stipulated for payment in gold.<sup>15</sup> It is to be noticed, however, that both gold and fiat currency were circulating media having legal tender quality at that time. Consequently, it was not illegal for parties to stipulate for payment in gold and those contracts were enforced without hesitation. For this reason those decisions are not precedents for the validity of gold clauses when they have been pronounced illegal.

In *Norman v. Baltimore & O. R. Co.*<sup>16</sup> the Court reasoned that the Congressional power to regulate the currency permitted a government monopoly of gold and the establishment of a managed currency. The syllogistic deduction from this major premise gives Congress power to preclude private individuals from frustrating that policy through gold clauses. A state cannot usurp that which a sovereign people have delegated to the federal government.<sup>17</sup> Why, then, should private persons be permitted to alienate the power of Congress to regulate the value of the currency?

Under a symposium of express powers, including the power to regulate and establish the monetary structure, Congress constitutionally taxed currency issued by state banks into oblivion. The social interest was a unification of the currency under single parentage. Despite the fact that this program invalidated existing contracts, the Court held, in *Veazie Bank v. Feno*,<sup>18</sup> that Congress, as an incident to its express powers, could frustrate contracts which interfere with or are in derogation of these express powers.

Abundant analogies were produced by the majority opinion as instances of the power of Congress to invalidate the provisions of then existing con-

<sup>8</sup> 48 Stat. 1.

<sup>9</sup> (1935), 55 S. Ct. 407.

<sup>10</sup> (1868), 74 U. S. 229; *Butler v. Horwitz* (1868), 74 U. S. 258; *Dewing v. Sears*, (1870), 11 Wall. 379.

<sup>11</sup> (1871), 12 Wall. 687; *Gregory v. Morris* (1877), 96 U. S. 619.

<sup>12</sup> (1870), 12 Wall. 457.

<sup>13</sup> (1884), 110 U. S. 421.

<sup>14</sup> (1869), 8 Wall. 603.

<sup>15</sup> *Treblicock v. Wilson* (1884), 110 U. S. 421; *Gregory v. Morris* (1877), 96 U. S. 619; *Dewing v. Sears* (1870), 11 Wall. 379; *Butler v. Horwitz* (1868), 74 U. S. 258; *Bronson v. Rodes* (1868), 74 U. S. 229.

<sup>16</sup> (1935), 55 S. Ct. 407.

<sup>17</sup> *McCullough v. Maryland* (1819), 4 Wheat. 316.

<sup>18</sup> (1869), 8 Wall. 533; *Ling Su Fan v. United States* (1910), 218 U. S. 302.

tracts which infringed upon the constitutional power to regulate interstate commerce.<sup>19</sup> Private property was thereby annihilated. In each instance, the Court determined whether the contract in question interfered with the exercise of the power of the federal government to regulate commerce.

With the exception of the concurring opinion of Justice Stone, to which later reference will be made, the Court failed to announce that Congress was legislating within the domain of the police power. In deference to clarity of analysis, this implication should have been asserted positively. The police power of Congress can be exercised only in favor of those special matters within the embrace of the powers delegated to Congress and then only in support of a recognized social interest. What were the social interests in favor of which this body of legislation was enacted?

First, a uniform, managed currency was thought to be necessary to raise the domestic price level. Second, an indebtedness which overpowered the earning power of our people demanded reduction in the interest of preserving the economic and social life of a great debtor class. Third, it is possible that Congress conceived of a long range scheme of planned economic progress in which these measures formed an integral part. And, fourth, it is not without reason to believe that contracts were impaired, paradoxically enough, only to save them from total destruction by forces beyond the physical power of government to control.

If this be a correct analysis of the major social interests involved, it became the duty of the Court to first determine whether these declared interests might be protected through the powers delegated to the federal domain; and, if so, to ascertain whether these interests overbalance the social value in security of property and contract (if, indeed, the Congressional measure was in conflict with security of property and contract). An affirmative answer would require a further judgment to decide whether the legislation in controversy sustained these social interests.

Before investigating whether this body of legislation subserved these social values, a review of the reasoning of the Court in *Perry v. United States*<sup>20</sup> and in *Nortz v. United States*<sup>21</sup> will determine if the first social interest has been realized. Both cases involved government contracts calling for payment in gold dollars containing twenty-five and eight-tenths grains. A majority of the Court declared that the federal government could not employ its power to regulate the currency in a manner that would frustrate the credit of the United States which had been pledged pursuant to the express power of Congress to borrow money. Therefore, this legislation, in so far as it attempted to abrogate governmental contracts, was unconstitutional. Having set forth this legal and moral obligation of the government in robust terms, the Court astutely withdrew all manner of legal remedy. Upon the theory that a change in the weight of the gold dollar does not constitute a loss to the plaintiff per se, the Court purported to measure the plain-

<sup>19</sup> *New York v. United States* (1922), 257 U. S. 591; *Employer's Liability Cases* (1912), 223 U. S. 1; *Addyson Pipe & Steel Co. v. United States* (1899), 175 U. S. 211.

<sup>20</sup> (1935), S. Ct. 432. On certificate from the Court of Claims. Plaintiff brought suit as owner of an obligation of the United States for \$10,000 executed by authority of an Act of 1917. The Bond provided for amortization in gold coin of the then "present standard of value." Plaintiff declares the Joint Resolution amounts to a taking of property without due process of law and is therefore unconstitutional.

<sup>21</sup> (1935), 55 S. Ct. 428. On certificate from the Court of Claims. Plaintiff brought suit as owner of gold certificates of the Treasury of the United States. These certificates certified that each dollar thereof was supported by a gold dollar deposited in the United States Treasury. Plaintiff demands an ounce of gold for every \$20.67 of gold certificates tendered. The declaration avers that an ounce of gold bullion is worth \$33.42 in the market. The resulting loss amounts to a deprivation of property without due process of law under plaintiff's contention.

tiff's damages for breach of contract by the value of the deprived gold at the nearest available market for all legal and available uses. Of course, the market for gold has been abolished by Congressional action, and as a consequence, damages could not be measured. Should specific performance be given, all that plaintiff could do with his gold coins would be to return them to the Treasury in return dollar for dollar in currency. The Court of Claims in which the United States may be sued cannot entertain an action for nominal damages.<sup>22</sup> Furthermore, under the doctrine of *Lynch v. United States*,<sup>23</sup> Congress cannot barter away the immunity of the people of the United States to suit, that capacity being an attribute of sovereignty.

In the concurring opinion of Justice Stone, before referred to, he expresses the opinion that Congress may denounce the contracts of the United States through its police power in the regulation of the currency. This reasoning, although not accepted in so far as the gold clauses are concerned by the majority opinion of Chief Justice Hughes, must have been accepted by the majority of the Court in sustaining legislation which gave the federal government a gold monopoly. The very fact that Congress withdrew the gold in which government contracts were payable manifests an exercise of the police power of Congress. Although contracts are adversely affected, the government does not have to pay for injury caused in the exercise of the police power.<sup>24</sup> The economic reason for this position is that embarrassment would be spared should the United States return to a gold bullion standard making gold and obligations payable in gold legal; but, at the same time, stabilizing the dollar on a gold content basis lower than twenty-five and eight-tenths grains.

The majority opinion in the Perry case intimated that had plaintiff shown a loss in purchasing power, he might have obtained substantial damages. The United States Bureau of Labor Statistics report for May, 1934, shows that the price level in terms of legal tender dollars is only slightly more than seventy per cent of the price level of 1926 expressed in gold dollars. Therefore, the creditor is receiving more in purchasing power than he advanced upon his loan. This datum reveals that the social interest in raising prices has not been accomplished by this body of legislation. The legislation proceeded upon the quantity theory of money which ignores the all important element of the velocity of money and credit.<sup>25</sup> A fear of continued economic distress has impaired the velocity of credit as witnessed by the liquid condition of banks. The failure of prices to rise substantially has, of course, limited the earning power of our people. The machinery for drastic inflation is present, nevertheless. Should it be operated intensively, the momentum of inflation would remove the regulation of currency from social control for all practical purposes. Managed currency would be a misnomer. Although price regulation attempted through a controlled currency is constitutional by reason of their inseparable identity, the first social interest has not reached fruition.

When this legislation automatically reduced the indebtedness of the country forty per cent, it was to be hoped that outstanding obligations might eventually be leveled to meet the earning power of the people. This action,

<sup>22</sup> *Grant v. United States* (1868), 7 Wall. 331; *Marion & Rye V. R. Co. v. United States* (1926), 270 U. S. 280.

<sup>23</sup> (1934), 292 U. S. 571.

<sup>24</sup> When, through a proper exercise of the police power, the performance of a contract has been rendered impossible because of illegality, the obligor is excused from performance. The intervening illegality constitutes a casual condition subsequent. It is to be noticed in these cases that the contracts are executory on one side only. *Storke, Monetary Legislation and the Gold Clause* (1934), 6 *Rocky Mountain L. R.* 237.

<sup>25</sup> *Kilborne, Principles of Money and Banking* (1932, 3rd ed.), chapters 4, 5, 9.

has undoubtedly brought some relief to the debtor class, but, as has been shown, earning power has failed to rise correspondingly. Should debtors be forced to pay in the equivalent of old gold dollars from an income based upon the new devalued currency, their condition would be rendered insufferable.<sup>26</sup> Congress, having the power to devalue the currency, possessed the ancillary power to enact measures which alone would permit the first named power to be exercised effectively.

A planned economic progress incorporating a species of the commodity dollar may be identified with these measures.<sup>27</sup> The interdependence of the supply and demand for commodities with the supply and demand for money in fixing the price level requires a social control of commodities as well as of the medium of exchange. This legislation was not sufficiently inclusive to be fairly said to be more than a pretense at the beginning of a controlled economy.

It is believed that this legislation impaired contracts only that they might ultimately be performed in part, at least. The Court necessarily determined in favor of the less vicious of alternative evils. The huge indebtedness of this country is the result of unregulated private credit expansion. That indebtedness, incapable of amortization, faltered between an imminent danger of repudiation or a partial reduction under legal sanction. The Court accepted the more equitable distribution of loss. A representative illustration will reveal the compulsion of this argument. Ostensibly, the privilege of the railroads to pay the interest and principal on their bonds in debased currency is to injure creditors, the more important being insurance companies. In turn, the small policy holder would be injured. Yet, if the railroads were thrown into forced liquidation, it is probable that insurance companies could not have absorbed the loss, and, in consequence thereof, the small creditors of the country would have sustained disaster. We are of the belief that should insurance companies fail, the economic structure would be paralyzed. In short, the intangible property interests of these United States would be annihilated should the vicious circle of forced liquidation be permitted to pursue its course without interference.

That property of individuals was destroyed is beyond denial. To contend that it was taken only as an incident of the monetary policy is a contradiction of the avowed social interest motivating this legislation. From the opinion of the four dissenting Justices comes a pronouncement that the monetary power was the servant of Congress in the destruction of property and the Fifth Amendment. The salvation of private property was probably the major objective of both factions of the Court. Under the majority view private property is sacrificed to save the institution of private property. In view of this curious fact it is suggested that these decisions demonstrate the undervision and the inadequacy of the pure, analytical logic which has become an onerous precedent in legal thinking upon constitutional problems.

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<sup>26</sup> It has been suggested that creditors incorporate a provision in contracts which will assure a parity of purchasing power between the amount of money loaned and the amount to be repaid. In lieu of gold clauses the commodity index would be employed. Based upon the truthful premise that the real value of money is in purchasing power, the index would provide a just and accurate standard. Nebolsine, *The Gold Clause in Private Contracts* (1933), 42 *Yale L. J.* 1051.

<sup>27</sup> Kilborne, *Principles of Money and Banking* (1932 3rd ed.), ch. 11; Fairchild and Compton, *Economic Problems* (1930 re. ed.), p. 253 ff.