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Introduction

Chief Justice John Marshall presided over the U.S. Supreme Court from 1801 to 1835. Most famously, his opinions made the Supreme Court a co-equal branch of government along with the executive and legislative branches, and solidified the principle of judicial review where the Court could declare an act of Congress or the President unconstitutional.

Less famously—students don't learn this in high school—three decisions by the Marshall Court had a profound role in defining the character of the U.S. economy. They were:

- **Fletcher v. Peck (1810),** which focused on the Constitution's contract clause
- **McCulloch v. Maryland (1819)**, which interpreted the necessary-and-proper clause
- **Gibbons v. Ogden (1824)**, the first Supreme Court decision to address the commerce clause

All three opinions were written by Marshall in a period of "aggressive nationalism" (in the words of history professor Richard E. Ellis) on the Court. These decisions served to enshrine free enterprise, protect the sanctity of contracts and private transactions, allow a central bank to promote economic development, prevent states from granting monopolies, and establish the federal government's supremacy in regulating interstate commerce—resulting in the growth of the U.S. economy into the world's largest and most influential.

While these decisions had a salutary effect on the economy, they also affected the course of American federalism.

John Marshall (1755-1835)

Part 1: *Fletcher* and the Yazoo Contract

In 1795 the Georgia legislature sold 35 million acres of land in the state's western territory, then known as Yazoo (now Mississippi and Alabama), to a group of four private land companies. The sale price was a colossal bargain: less than 2 cents an acre.

The land companies in turn divided up the tracts into parcels and sold them off to second-tier investors, including smaller land companies and individuals in several states. A number of northern speculators banded together as the New England Mississippi Land Company and bought some of the parcels from the original land companies.

There was one problem. Most of the Georgia legislators who voted for the 1795 land-sale legislation had been bribed by the first-tier investors to sell the land at a preposterously low price. When Georgia voters learned of the massive Yazoo scandal, they responded by replacing many of the corrupt legislators in the 1796 election, and the new Georgia legislature promptly rescinded the 1795 act, annulling the land sale. Title to the Yazoo lands was restored to the state. Seven years later Georgia ceded Yazoo Territory to the national government. This did not bother the first-tier land companies much, because they had already made huge profits selling parcels to second-tier investors. The second- and third-tier investors who now held annulled titles to Yazoo land were the real victims of the scandal.

John Peck, a Boston speculator, was one of the third-tier investors who bought some Yazoo land from the New England Mississippi Land Company in 1800. In 1803 he sold 13,000 acres of his holdings to New Hampshire investor Robert Fletcher for $3,000. In the sale contract, Peck explicitly stated that his title to the land was sound. Almost immediately Fletcher sued Peck for breach of contract, claiming Peck's title to the land had been worthless due to the 1796 act rescinding the original sale of Yazoo land, and demanding his money back. In Peck's defense of the lawsuit, he asserted *first* that Georgia's 1795 sale was a binding contract between the state and the land companies, the underlying fraud notwithstanding; and *second* that the 1796 rescinding act was unconstitutional because it "impaired the obligations" of the 1795 contract, in the violation of Article 1, Section 10 of the Constitution, known as the contract clause. The contract clause states:

> No state shall…pass any Bill of Attainder, ex post facto Law, or Law impairing the Obligation of Contracts, or grant any Title of Nobility.

If the 1796 rescinding act was unconstitutional, then the titles that both Fletcher and Peck held should still be sound and, therefore, valuable.

Fletcher's lawsuit failed at the federal circuit court in Boston. That is, the court agreed with Peck's argument that the 1796 rescinding act impaired a contract, and was therefore unconstitutional. The reasoning behind the court's decision was this: The Georgia legislature had entered into an enforceable contract with the land companies in 1795, which created binding obligations on both sides. Relying on the enforceability of that contract, many other parties—second-tier land companies, investors, and purchasers in the lawful pursuit of profit and economic advantage—entered into a series of transactions that resulted in the orderly distribution

of wealth and assets across the marketplace, facilitating the flow of commerce throughout the economy; the state of Georgia, thereafter and forever, should have been prohibited by the Constitution's contract clause from impairing, or rescinding, the obligations of that contract which had set those market forces in motion; no government had the authority under the Constitution to unravel the multitude of orderly transactions, distributions, and commercial activities that had transpired in reliance on the original contract of 1795.

Peck's title to the Yazoo land was therefore sound when he purchased it in 1800 and when he sold part of it to Fletcher in 1803, and the defendant Peck had therefore not breached his agreement with the plaintiff Fletcher.

Fletcher appealed to the U.S. Supreme Court. Fletcher's lawyer, Luther Martin, was one of the framers of the Constitution. Peck's legal team included future President John Quincy Adams and future Supreme Court Justice Joseph Story. The high court ruled in 1810, in the landmark case *Fletcher v. Peck*, that Georgia's rescinding act did violate the Constitution's contact clause, as Peck had asserted in his defense, by "impairing the obligations of" the Yazoo contract. So although Fletcher lost the case, the titles to Yazoo land that he and Peck held, even though the Yazoo land was now national property, should, as a matter of justice, still be valuable. The U.S. legislature eventually approved a payment to all title-holding victims of the Yazoo scandal.

It is almost certain that Fletcher and Peck both knew about Georgia's 1796 rescinding act when they made their deal in 1803, and they colluded to bring the lawsuit to court in the interest of all New England Mississippi Land Company investors. It is likely that Chief Justice John Marshall was aware that the lawsuit was collusive when he wrote the Court's opinion in 1810 in *Fletcher v. Peck*. Nevertheless, *Fletcher* was the first in a series of contract clause decisions in the high court that elevated business transactions and vested property rights to a sanctified status and protected them from arbitrary actions of state legislatures. Such protection gave entrepreneurs and investors reasonable assurance that once they risked their capital on a venture, their chances for a return would not be thwarted by corrupt or even well-meaning politicians. If the obligations of contract could be impaired by the legislatures, "all titles would be insecure, and the intercourse between man and man would be very seriously obstructed," Marshall wrote.

Free Enterprise

Free enterprise was already baked into the American economy in the early 1700s. Free-market capitalism was essentially imported from Britain and evolved in a loosely regulated confederation of colonies and then states after the War of Independence. But not one of the founding documents—the Declaration of Independence, the Articles of Confederation, the Constitution, and the Federalist Papers included—mention free enterprise or free markets. The *Fletcher* decision is the closest thing we have to official establishment of free enterprise. It was followed in 1819 by the Marshall Court's derivative decision in *Dartmouth College v. Woodward*, which extended the protection of contracts to the protection of corporate charters from state interference.

Federalism

The Marshall Court's decision in *Fletcher v. Peck*, though a boon to private enterprise, represented a threat to Jeffersonian states' rights advocates. By asserting jurisdiction over

Georgia's affairs and striking down a state law for the first time (the Court had struck down a federal law for the first time seven years earlier in *Marbury v. Madison*), the Marshall Court was perceived by Jeffersonians as consolidating power in the national government at the expense of state sovereignty. The Constitution, after all, had created a federal structure where sovereignty was divided between the national government and state governments, so that no unit of government would accumulate so much power that it could become tyrannical.

The fear that the national government was exercising too much power had been aroused immediately after the new government was launched, when Treasury Secretary Alexander Hamilton created the nation's financial system in 1791. Hamilton's plan involved national assumption of state debts, funding the national debt, and establishing a central bank. He believed that a federally chartered bank, like the great European central banks, was essential for unifying and stimulating the nation's sagging economy and establishing international credit.

Part 2: *McCulloch* and the Second Bank of the United States

Not long after George Washington's inauguration and the passage of the Bill of Rights, Hamilton persuaded Congress to establish the First Bank of the United States. Secretary of State Thomas Jefferson, later the third president, argued that the Constitution did not give the U.S. Congress the power to incorporate a bank, and thus only the states could grant corporate charters to banks. Article I, Section 8 enumerated 17 specific powers of the legislative branch (including the power to lay and collect taxes, borrow money, regulate interstate commerce, raise and support armies, declare and conduct war, etc.), and chartering a bank was not among them. Hamilton persuaded Washington and Congress, though, that the necessary-and-proper clause of Article I, Section 8, which immediately follows the list of enumerated powers, did give the national Congress such a power. That clause states:

> The Congress shall have Power…To make all Laws which shall be necessary and proper for carrying into Execution the foregoing Powers, and all other Powers vested by this Constitution in the Government of the United States, or in any Department or Officer thereof.

Congress agreed that the central bank was necessary, not a mere convenience, for the execution of its powers, especially fiscal and monetary ones.

When the First Bank's charter came up for renewal in 1811, Congress under the fourth president, James Madison (who as a Congressman in 1791 had been a leading opponent of the First Bank), allowed it to expire. The ensuing inflationary policies of the state banks, especially during the War of 1812, convinced Congress to re-charter the central bank to unify monetary policy and restore monetary restraint. In 1816, at the end of Madison's second term, Congress established the Second Bank of the United States (known among historians as 2BUS) with a 20-year charter.

With headquarters in Philadelphia, the 2BUS opened branch offices in several other U.S. cities in 1817, including Baltimore. Maryland's legislature considered the 2BUS branch a competitor of its state banks, and it levied a $15,000 per year tax on all banks operating within the state but not chartered by the state. The cashier of the Baltimore branch of 2BUS, James McCulloch, defied the state law and refused to pay the tax, claiming the state had no power to tax an institution of the national government. The state sued the bank to try to collect the tax, and after the county court and the Maryland Court of Appeals upheld judgments against McCulloch, the bank appealed to the U.S. Supreme Court. At the high court, McCulloch was represented by Daniel Webster, the most prominent constitutional lawyer of his generation (he argued 223 cases before the Supreme Court and won about half of them), and later a U.S. senator and secretary of state under President Harrison.

In its 1819 decision in *McCulloch v. Maryland*. the Supreme Court resolved two issues. First it upheld the power of Congress to incorporate the 2BUS, based on a broad construction of the necessary-and-proper clause. This decision reaffirmed the "implied power" (as opposed to an enumerated one) of the national government to create institutions that would operate within state

boundaries, for the benefit of a unified national economy. Second, the *McCulloch* decision prohibited the states from taxing and thereby impeding the operation of such institutions, even when they arguably competed with the state's economic interests. John Marshall famously stated, in his opinion, "The power to tax is also the power to destroy."

Both *Fletcher* and *McCulloch* dealt with the limits of state legislative power, but *McCulloch* also broadened the scope and extent of the national government's power. Marshall's opinion in *McCulloch* again provoked condemnation among states-rights advocates, especially in Virginia and Georgia; and outright hostility in Ohio, where the governor sent agents to forcibly collect the taxes it had enacted upon two 2BUS branches in that state.

Part 3: *Gibbons* and the Steamboat Monopoly

The authority of the U.S. Congress to regulate interstate commerce is the third of those 17 enumerated powers in Article 1, Section 8. A broad interpretation of the commerce clause has been the constitutional basis for civil rights legislation, environmental and worker protection laws, financial regulation, and President Obama's health care reform. It continues to generate controversy regarding the extent of the national government's reach into the commercial (and other) affairs of the nation.

The commerce clause gives Congress the authority to "regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes."

A mere 16 words, the commerce clause deserves an exalted place in Constitutional history. The need for more centralized regulation of interstate commerce was the primary impetus for convoking the constitutional convention of 1787 in Philadelphia. Hamilton, Madison, and 10 other national leaders had met in Annapolis the year before to try to resolve the young republic's fiscal crisis, and they decided that the Articles of Confederation needed to be revised, if not replaced. In the word of author Richard Beeman, the Articles "lacked any provision permitting the American government to impose uniform commercial regulations among the states. As a consequence, the individual American states frequently fell into destructive competition with one another." (Beeman is author of *Plain, Honest Men: The Making of the American Constitution*, Random House, NY, 2009.)

The 12 Annapolis delegates in 1786 produced a resolution, which Hamilton presented to the Continental Congress, seeking authority to call a convention "to meet at Philadelphia on the second Monday in May next…to devise such further provisions as should appear…necessary to render the constitution of the Federal Government adequate to the exigencies of the union." Congress approved the resolution by a margin of a single vote. Said constitutional law professor Dan T. Coenen in his 2004 book on the commerce clause:

> The Philadelphia [c]onvention of 1787 was called to address one overarching problem—the shared sense that the federal government was too weak [under the Articles of Confederation] and the states were too strong, with respect to the power to regulate interstate and foreign commerce.

The result of the Philadelphia meeting in 1787 was the creation of an entirely new form of republican government, based on the most durable written constitution in history.

The New York Steamboat Monopoly

Despite the importance of the commerce clause in constitution history, it took 36 years from ratification in 1788 to bring a case based on it to the U.S. Supreme Court. *Gibbons v. Ogden*, popularly known then as the steamboat case, arose from a clash between a federal statute governing navigation on all American coastal and inland waters and a New York law that restricted steam navigation on that state's rivers.

In 1807, the New York legislature granted a 20-year monopoly for commercial steam navigation on the state's waters to Robert Fulton, the most prominent of the developers of steam-powered watercraft, and his partner Robert R. Livingston, formerly the highest-ranking judge in New York (he administered the oath of office to George Washington in 1789, and in 1803 negotiated the Louisiana Purchase as U.S. minister to France). The Fulton-Livingston syndicate also received a similar monopoly from Louisiana for navigation on the lower Mississippi River in 1811. The partners established a steamboat ferry service on the Hudson River between New York City and Albany, and they issued an exclusive license to Aaron Ogden for the purpose of ferrying passengers between Manhattan and Elizabeth, New Jersey.

Rival steamboat lines mounted legal challenges to the Fulton-Livingston monopoly, but the New York courts repeatedly upheld their exclusive license granted by the state legislature. Connecticut and New Jersey passed retaliatory legislation forbidding steamboats licensed by the New York monopoly to navigate their waters, and others began to grant their own steamboat monopoly rights.

In 1818 Thomas Gibbons, a former partner of Ogden, began running two steamboat ferries between Manhattan and Elizabeth, in defiance of Ogden's exclusive state license. One of Gibbons's vessels was piloted by a young Cornelius Vanderbilt. Gibbons was operating under a federal license based on the Coastal Licensing Act, passed by the U.S. Congress in 1793 (more than a decade before New York's steamboat monopoly legislation) to regulate the "coasting trade" on all American waters. Although enrollment was not mandatory, vessels that did obtain a license under the Coastal Licensing Act enjoyed certain privileges, including exemption from some port fees. Foreign vessels were not eligible to enroll.

Ogden went to the New York chancery court and got a restraining order against Gibbons's two vessels. Gibbons appealed to New York's highest court and then to the U.S. Supreme Court, claiming the federal coasting act superseded New York's monopoly grant, because the commerce clause gave Congress *exclusive* power in the regulation of interstate commerce. Ogden's lawyers argued at the high court that the states "ought to have fully *concurrent* power over commerce between the states."

The steamboat industry was to the economy of the first half of the 19th century what the automotive industry was to the first half of the 20th. Given the growth of steamboat navigation on many U.S. rivers, and its role in opening the west to trade and settlement, the decision in this case would affect economic expansion throughout the union—so *Gibbons v. Ogden* acquired national significance. From an economic point of view, the issue before the Supreme Court was "whether steamboat navigation…would continue to be controlled by state-oriented monopolies or be opened to free competition. More broadly, the case promised to clarify the federal government's role in establishing a unified economic policy," in the words of John Marshall biographer Charles F. Hobson.

The Supreme Court decision in 1824, following closely the arguments made by plaintiff's lawyer Daniel Webster, gave Gibbons the victory, dissolving the restraining order and nullifying the monopoly grant—not because it was unconstitutional but because it "collided" with a federal

law. John Marshall's opinion asserted the federal government's *supremacy*, rather than exclusivity, in regulating interstate commerce.

In contrast to the *Fletcher* and *McCulloch* decisions, reaction to the Court's decision in *Gibbons* was "overwhelmingly favorable." Throughout the country, especially in the press, Marshall's opinion was hailed as a breakthrough for free enterprise.

Gibbons "heralded the expansion of entrepreneurship and investment in technology characteristic of the next [nearly] two hundred years of American life," wrote law professor Herbert A. Johnson in his 2010 book about the *Gibbons* case.

Part 4: Federalism Endures

Taken together as a body of law, *Fletcher*, *McCulloch*, and *Gibbons* formed a legal foundation for the American economy, where vested property rights, contracts, and private transactions are honored and protected from government interference; where Congress has power to create institutions to stimulate the flow of capital investment and effectuate unified fiscal and monetary policy; where states may not inhibit the stream of commerce across borders within the union; and where competition is favored over monopolies.

The Marshall Court's decisions in *Fletcher*, *McCulloch*, and *Gibbons*, coming in the early years of the American republic, addressed the most important political issues of the time, issues that occupied the minds of politicians and voters, lawyers and courts, businesses, and citizens—including the struggle between Alexander Hamilton's vision of an American empire based on industrial, commercial, and military preeminence and Thomas Jefferson's agrarian vision of limited, decentralized government. The former depended on strengthening the unifying power of the national government in the early 1800s, while the latter aimed to preserve the sovereignty of the states and guard against tyranny that would presumably result from vesting too much power in a central authority.

Ellis pointed out in his 2007 book *Aggressive Nationalism* (Oxford University Press) that John Marshall's opinion about the necessary-and-proper clause in *McCulloch* was obiter dictum, comments that were irrelevant to the case because it was narrowly about whether the state could tax a federal bank, not whether the bank was constitutional. Marshall took it upon himself, perhaps improperly, to use this case to expand the scope of the necessary-and-proper clause.

James Madison, a principal framer of the Constitution and fourth President, although opposed to the central bank, believed that strengthening the power of the national government was essential to preserve liberty, especially with respect to minority and individual rights.

Such issues, which first took center stage in the nationwide debates over ratification of the Constitution in 1787 and 1788, still occupy minds today and, if the American republic is to endure, always will.

About the Author

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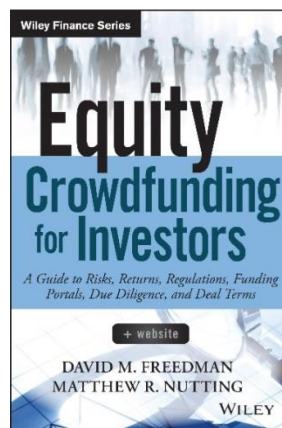

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