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Davis Andrew McFarland
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An Historical Study of Law's System

BY

ANDREW McFARLAND DAVIS

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AN HISTORICAL STUDY OF LAW'S SYSTEM.

I.

At the death of Louis XIV., France was practically bankrupt. It is true, the floating debt and the capital represented by the rentes amounted to only about 3,000,000,000 livres; but, for the statesmen and financiers of that day, the resources of the kingdom were inadequate to meet the interest charges of this debt and at the same time pay the ordinary expenses of the government. The protracted wars during the reign of the late king had exhausted the vitality of the kingdom. Commerce was prostrate, manufactures were stagnant, agriculture had almost been abandoned. To escape service in the army or starvation at home, many laborers had fled to Italy. Deserted farms were frequently to be met with, and there were vast stretches of uncultivated land where the traveller encountered neither peasants nor domestic animals.

The credit of the monarchy was almost entirely gone. In pursuance of a custom of many years' standing, the collection of a large part of the taxes had been farmed out for terms of years to individuals and to companies. To meet current expenses, the government had been obliged to negotiate with these farmers of the revenue for advances upon the taxes which they had the legal right to collect; and thus many of the important sources of revenue had been anticipated for several years.

Various forms of government notes and obligations were in circulation. Some of these had been issued in a regular manner, and some were practically certificates of indebtedness issued from the bankrupt offices of different branches of the revenue service. Double-entry book-keeping had not as yet been introduced by the government,
and no person knew the full extent of the government debt or the form in which it stood. Such patent opportunities for cheating had not been neglected; and the misery of the situation was aggravated by a large proportion of fraudulent paper, which circulated in the market among the various evidences of government indebtedness, and thus increased the government discredit. Notes issued by royal authority, which it was ordained by the Council of State should pass current between individuals, were, by the same authority, declared not to be available for payment of dues to the government. Little more confidence could be placed in the coin of the realm. The theory prevailed that the effigy of the reigning monarch and the denomination stamped upon the piece of metal which circulated as coin were what gave it value. The number of livres in the marc of gold or silver could be increased or diminished at the will of the ruling monarch. Theoretically, it was possible to call in all the coin of the State, and to reissue the same pieces of metal at a higher rate, the State thus receiving the benefit of the nominal increase in value.* No measure which their ingenuity could devise had been left untried by the financiers of Louis XIV. to raise money out of the people of France. As a result there had been established an ingenious system of direct taxes, which reached the most obscure branches of industry and trade, which hindered pros-

*These increases of denominational value were termed "augmentations"; the reverse processes were known as "diminutions." The manner in which they operated can be no better disclosed than by setting before the reader the argument used by the Parliament, in a remonstrance made to the regent, against a recoing with augmentation. In this case, the citizen who brought coin to the mint was permitted to add to his coin, for exchange into the new coinage, billets d'état to the extent of two-fifths of the amount of the coin. The result of this proceeding was stated to be substantially as follows: An individual carries to the mint 125 marcs of silver, which, at the rate of 40 livres to the marc, make 5,000 livres. He also brings 2,000 livres in billets d'état. He receives in new coin 7,000 livres, which, at the rate of 60 livres to the marc, weigh only 116 2-3 marcs. He loses 8 1-3 marcs on the 125 marcs which he brought, and all his notes.
perity, which even drove the laboring people over the border.

It is not to be wondered at that, with such a legacy of misery, the regent was forced to discuss the propriety of repudiating the State debts. This step, however, he declined to take openly, although many of the operations to which he actually resorted were of the same nature. The outstanding obligations of the government which were of the character of demand debts were called in. Some of them were cancelled. Others were arbitrarily reduced in amount. In place of the old evidences of debt, new notes called *billets d'état* for 250,000,000 livres, uniform in character and bearing four per cent. interest, were issued.* The process of inspection and cancellation was known as the "*Visa,*" and was carried on under the management of the Paris Brothers, who were afterwards prominent in their opposition to Law. All those who had dealt with the government or who were suspected of usury were compelled to disclose their affairs, and were subjected to arbitrary amercements of their property by the order of a "Chamber of Justice," composed of important government officials. Proceedings of this nature were not calculated to restore confidence on the part of capitalists. Yet the bare-faced corruption which had prevailed during the latter days of the preceding reign somewhat mollified popular judgment; and when the regent in various ways made feeble efforts to remove the trammels from trade, to encourage labor, to systematize taxation, and to relieve the State from the burden of payments largely absorbed in support of the privileged classes through pensions and offices, the fact that these steps were in the right direction was felt and appreciated.

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*There can be no doubt that the title "*billets d'état*" was first specifically applied to this issue of notes. Yet so competent an authority as the Baron de Nervo speaks of the government obligations called *billets d'état,* which were emitted under the preceding reign. *Les Finances Françaises sous l'Ancienne Monarchie,* par M. le Baron de Nervo, t. ii., p. 9.
While the authorities were thus groping in the dark, seeking for some ray of light which should reveal the pathway to prosperity, Law appeared upon the scene. He was born in Edinburgh, in 1671. His father was a goldsmith, which in those days meant that he was also a banker. While Law was still a mere boy, his father died, leaving his family in comfortable circumstances. Under the guidance of his mother, Law received an education suitable to his station in life and to the activity of an intellect which even in childhood gave signs of its capacity. Arrived at early manhood, he drifted to London, where he led a career of dissipation, which culminated in 1694 in a duel, in which he killed his opponent. He was thereafter tried for murder, convicted, and sentenced to death. Pending certain legal proceedings subsequent to the sentence, he escaped from prison, and fled to Amsterdam. While there, he is said to have devoted himself to a study of the Bank of Amsterdam, which was then at the height of its prosperity, and it is supposed that he learned the secrets of its mysterious management. In 1705, he submitted to the Scotch Parliament a plan for a land-bank. This scheme was published under the title “Money and Trade Considered.”

The land-bank did not meet with favor at the hands of the Scotch Parliament; and Law, shortly after submitting it, became a rover upon the continent of Europe. He is reported to have passed several years travelling from place to place, during which time he amassed a fortune by gambling and by fortunate speculations. His brain, meanwhile, was teeming with schemes of credit which should revolutionize trade and make the fortune of what-

*John Briscoe, in 1696, unfolded a scheme for a land-bank in a publication entitled A Discourse on the Late Fund of the Million Act, etc., together with Proposals for supplying their Majesties with Money, etc., by a National Land-bank. Law himself referred to a project submitted by “Doctor H. C.” (Hugh Chamberlayne). Other schemes of a similar nature, suggested by men of speculative temperaments, are referred to by students of the history of that time,
ever State should adopt them. These plans he freely discussed with men of power and position who would listen to him, thus establishing for himself a continental reputation as a financier who had new ideas concerning banks, and who was thoroughly competent to elucidate and defend them. While searching for some sovereign bold and needy enough to experiment with his theories, he proposed to Chamillart to establish a bank, and he forwarded to the Prince de Conti memorials, which, during the latter days of Louis XIV., were submitted to Desmarets.* The record of an attempt in another quarter is preserved through the epigrammatic answer attributed to Victor Amadeus of Savoy, who relieved himself from the perils of the experiment by saying, "I am not rich enough to ruin myself." It is probable that, when Law came to Paris and approached the regent with his schemes, he was known in every capital in Europe as a brilliant financier, whose reasoning it was difficult to refute, but whose plans differed so materially from those then in vogue that he had not been able to find any ruler willing to adopt them. His success at the gaming-table and his career of dissipation were no bar to his influence.

Law submitted to the regent several memorials and letters in which he discussed the relations of money and credit to trade. In these papers, he referred to many of the banks then in existence; but it is evident that the banks from which he deduced most of his theories, and upon the example of which he relied for his plans for re-

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*Law's works were collected and published in 1790. The name of the editor of this work is not given on the title-page, but M. de Senovert has generally had the credit of it. Eugène Daire, in his Économistes Financiers du XVIIIe Siècle, republished this work, and also several fugitive pieces by Law, which were not included in Senovert's collection. In Law's "Second Memorial on Banks," p. 548 of Daire's collection, Law says, "It will be easy to prove that, if the bank had been established by M. Chamillart, when I had the honor to propose it to this minister, this establishment would have sustained the Crown and the State." Page 563, he refers in a similar way to the papers which reached Desmarets.
generating France, were the Bank of Amsterdam and the Bank of England. The former was a bank of deposit. The merchant deposited a sum of money, and in return therefor received on the books of the bank a credit. The money, once in the vaults of the bank, was supposed to remain there permanently. Its place in the currency of the world was supplied by the bank credit, which had a *quasi* circulation at Amsterdam. If the merchant wished to make use of his credit or of any portion of it, he gave an order to have a transfer made upon the books of the bank. Coins of all sorts and of every condition were received on deposit, but credits were adjusted in terms of a fixed standard adopted by the bank. Bills of exchange could thus be drawn in terms which avoided the embarrassments arising from *augmentations* and *diminutions*, and from clipped and sweated coin. Confidence in the bank was complete, and bank credits were more available in Amsterdam than coin. Special deposits were permitted in cases where the merchant expected soon to require the specific use of coin; but it is supposed that the general equilibrium between coin and bank credits was preserved through the medium of brokers, who daily dealt in bank credits on the Dam, and who, whenever there was a special demand for coin, always stood ready to purchase credits. Thus, a credit at the bank could always be converted into coin, and fluctuations were avoided. The Bank of England was based upon a different plan. Like that of the Bank of Venice, its foundation was government credit. It was organized for the purpose of lending its capital to the government, and thus it became a sort of fiscal agent. No power was given the corporation to issue bills, but it was assumed that it was conveyed in the general powers of the act under which the bank was organized. Deposits were received, accounts with depositors were opened, and the bank very soon exercised the various powers and performed the several functions which it has
continued to do to the present time. It became, in short, a bank of discount and circulation, which received deposits from merchants and the capital of which was in the form of a government loan.

The constitution and management of these and of other prominent European banks had convinced Law that, if confidence could be restored in France and the people could be induced to treat with a bank, as the merchants in Amsterdam did with their bank, the entire coin of the realm could be drawn into its vaults; a large amount of paper currency could be floated, and would be preferred to coin as a circulating medium; the bank, like the Bank of England, could act as agent of the government, and, if it should receive all the taxes, the credit thereby gained would enable it to float still more paper. The source of prosperity in any country he attributed to the abundance of money. Credit was the equivalent of money. By means of the increase of the circulating medium, interest on the debt could be reduced, and perhaps the principal could be redeemed. Trade and manufactures would be stimulated, and from the more prosperous country a much larger revenue could be collected than could possibly be squeezed out of the unfortunate people as they were then situated. Such a bank would be more powerful than the Bank of Amsterdam, because it could make use of a portion of its deposits, reserving only a portion to redeem its bills. As the depository of all the coin in the realm and the receiver of all the taxes, it would also surpass the Bank of England in strength.

The possibility of founding such a bank was based, first, upon the establishment of confidence; and, second, upon a series of propositions which Law elaborated, and which have been epitomized by Forbonnais* substantially as follows:

1. That all materials suitable for coinage may be converted into money.

*Recherches et Considerations sur les Finances de France. Basle, 1758.
2. That the abundance of money is the condition on which depend labor, husbandry, and population.

3. That paper is more suitable than the metals for a circulating medium.

In developing this last proposition, Law dwelt upon the fact that, by augmentations and diminutions and by changes of standard of fineness, sovereigns had the power to make a metallic currency uncertain in value; and, further, that the value of gold and silver coin is affected by the market price of ingots. This price, he said, was governed by the quantity imported, and thus the value of the coin was in a measure dependent upon foreign powers. Paper having no intrinsic value was not affected by fluctuations of the market. The quantity could always be proportioned to the demand. Notes could be protected against fluctuations in value, arising from augmentations and diminutions, by expressing their denominations in coin of specified weight and standard. This would also act as a protection against runs upon the bank, as all temptation to convert the notes into coin in order to derive the benefit of an augmentation would thus be provided against. Such notes would also be used like bills of exchange for remittances, saving the cost and trouble of transporting coin, besides saving time in counting.

Law's first proposition for a bank was submitted at an extraordinary meeting of the council, held October 21, 1715, at which, in addition to the members of the council, several bankers, merchants, and representatives of cities in France were present.† The scheme then submitted was thus described in the report of the meeting:—

The idea of this bank is to cause all the revenues of the king to be brought to the bank; to give to the receivers and farmers of the taxes notes for ten crowns, one hundred crowns, and one thousand

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† The matter had been previously discussed at several meetings held at the residences of those who were interested. "18th [Oct.]. Yesterday there was a