Blood Money:
How the Federal Reserve Enables War
and Undermines Civil Liberties

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The subject of central banking has long been relegated to the purview of economic technocrats, its language shrouded in financial jargon, and its activities masked by pseudo-scientific concepts such as money velocity and monetary aggregates. As a result, the common concerned citizen rarely questions, or is even aware of, the central role that the US central bank, the Federal Reserve (Fed), plays in American society, much less any impact it may have on civil liberties. The everyday observer is more likely to be concerned with the ongoing US military engagements in the Middle East, enhanced TSA screenings or perhaps rising grocery prices than with changes in the discount rate, the Federal Funds Target Rate, or reserve requirements, all set by the Fed. For most people, concerns over obvious economic and political conditions obscure the underlying reasons; effects are recognized more readily than causes. What that citizen may not realize is that the Fed is a major influencing factor behind many of the more high profile aspects of American economic and public policy.

With the ever-escalating federal budget deficits of the last decade, none of the government’s activities can be accurately appraised outside the enabling influence of the Fed, particularly in the area of foreign policy and its corollary, civil liberties. According to the Office of Management and Budget, the national debt has increased 139% since 2000, and the monetary base – the portion of the money supply directly controlled by the Fed – has increased over 300% (St. Louis Fed). The connection between monetary expansion and war finance is well established, particularly in the economic literature of the Austrian school of thought. History demonstrates, even before the introduction of fiat paper money, that highly inflationary periods are nearly always linked in some way to war, and conversely, large scale warfare is with little exception coupled with a policy of monetary expansion.
An equally established school of thought clearly demonstrates that wars waged abroad invariably result in reductions, often severe, of civil and political liberties on the home front. Episodes peppered throughout American history – not least the experience of the last decade – make this causal connection obvious. A citizenry in the throes of nationalistic fervor or under the spell of an ill-defined fear is frequently more willing to trade liberty for security than under more peaceable circumstances.

A connection less often drawn is the one between central banking and civil liberties. This link is already implicitly asserted in the paragraphs above, but it is important to bring this thesis to the fore. The Fed is a direct and fundamental influence which undermines Americans’ civil liberties by enabling and financing an otherwise unaffordable foreign policy. If central banking and civil liberties lie across a canyon from each other, war is the bridge that spans the gap. This paper will defend this thesis by surveying first the relationship between central banking and war, and then the one between war and civil liberties, with the goal of demonstrating that the Fed not only creates economic havoc through inflation and the boom/bust cycle, but also plays a direct role in stripping the American people of any meaningful adherence to the Bill of Rights.

Costs of War

War is expensive, extremely expensive, in both blood and treasure. This observation should go without saying, but when today’s supposedly limited government budget hawks treat military spending like a sacred cow, it unfortunately bears repeating. In order to pay for war, the government must divert resources from the private economy, just as any government program requires. At any given time, the economy encompasses only so many resources. Whether the
government pays for war bills out of taxation, borrowings, or monetary expansion, the true cost is determined by how those resources would have otherwise been spent by private citizens. This is the concept of *opportunity cost*: The cost of any one use of a resource is the next best opportunity that must be foregone.

The opportunities lost to war can only be measured to a limited degree. Monetary expenses can be recorded, summed and analyzed. But while these expenditures are obvious enough to make the headlines, war entails many less obvious, even hidden, costs. These hidden costs are much more difficult to quantify, but are no less important in discerning the true cost of war. The idea of hidden or unseen costs is beautifully and famously expounded in the essay, *What is Seen and What is Not Seen*, by nineteenth century French economist, Frederic Bastiat. His central thesis is that economic acts produce immediate, visible effects as well as unseen future results. For Bastiat, the good economist sets himself apart by taking the unseen into account. He illustrates his point with a story known as “The Broken Window”.

In the story, Bastiat imagines a boy shattering a shopkeeper’s window pane. The bystanders, looking on the bright side, opine that at least the glazier will earn income repairing the window, thereby redeeming the boy’s destructive act by benefitting the community economically. This reaction entails what is seen, the obvious and immediate economic result. With an analysis that stops here, one might conclude that breaking windows is good for the economy.

What is missed by the bystanders is what the shopkeeper could have done with his money had he not been obliged to purchase a new window; an instance of opportunity cost. The shopkeeper may have purchased a new pair of shoes instead of a new window. Only in this case, by spending the same amount of money, he would have possessed new shoes *and* a window,
rather than just a window. So by going deeper into the unseen effects of the broken window, it becomes apparent that the community’s wealth has declined by the value of the broken window. Bastiat concludes that “Society loses the value of objects unnecessarily destroyed,” or more succinctly, "Destruction is not profitable."

Such a conclusion would seem to jive with common sense, but prominent economists, even Nobel laureates such as Paul Krugman, can be heard claiming that the Pearl Harbor attack and ensuing US participation in World War II “brought an end to the Great Depression” and that the 9/11/2001 terrorist attacks “could even do some economic good” (2001). Any theoretical framework that suggests that economic gain can result from wealth destruction demands reassessment. After all, if we can find solace in the economic gains of infrastructure destruction, why not follow the logic to its conclusion? Why wait for a natural disaster or foreign attack? We should destroy entire neighborhoods, implode whole downtown blocks of office buildings, and push millions of cars into the ocean, in order to reap the economic boon of rebuilding everything we’ve destroyed.

Of course, this exercise in *reductio ad absurdum* demonstrates the logical bankruptcy of such sophistry. The only reason commentators like Krugman get away with such remarks is because the devastation is relatively contained and the public desires to hear anything positive in the midst of tragedy. Applying Bastiat’s story to events such as World War II and 9/11 makes it clear that there is no profit in the destruction. Anyone who actually lost property in the devastation would easily recognize the truth of the situation. Any resources required for rebuilding must be diverted from the purposes for which they would have been used in the absence of such destruction.
Clearly, war – and all aggressive violence for that matter – is inherently destructive economically. Far more than shopkeepers’ windows are broken. Whole cities and villages are leveled, entire industries crippled, substantial swaths of the labor force killed and maimed. It is easy enough to recognize the economic losses suffered by the persons and nations at the brunt of any military attack. But the aggressor nation also suffers economically from waging war, though it is less obvious.

Wars generally require increases in troop levels. Any number of military personnel greater than the minimum needed for strictly defensive purposes is a net loss to the labor force. Labor is a scarce resource like any other; a decrease in the supply of labor due to military recruitment leaves marginal production processes without the workers necessary to complete them. Society thus misses out on additional goods and increased competition, which reduces costs and increases quality.

Aside from any value received by the general population in the form of that nebulous “public” good, “defense,” wartime shifts in the economy benefit a narrow triumvirate of special interests; namely the military industrialists (more commonly known as “defense contractors”), the politicians, and the national security bureaucrats (which include military officers). They gain at the expense of everyone else in society who must bear the increased tax burden and the loss of purchasing power as well as the other economic dislocations resulting from inflation.

The wartime industrialists make huge profits on cost-plus contracts providing services and producing goods, many of which are made to destroy and be destroyed. Goods manufactured purely for destructive purposes. From 2003-2008, Haliburton saw its stock price increased 229%, General Dynamics by 134%, Raytheon by 117%, Lockheed Martin by 105%, and Northrop Grumman by 78% (Stiglitz 2008, 15). These profits were not earned on the free market by
pleasing voluntarily choosing customers. Rather they are earned through political wrangling, and are tainted by the coercive nature of taxation. Because of this, the Pentagon, and the firms it contracts with, are relatively unconcerned with keeping costs down, instead operating on what Columbia professor Seymour Melman called a “cost-maximization” model (Woods, 7). In his tribute to Melman, historian and economist Thomas E. Woods notes that, “Catering to the Pentagon…distorts a firm’s business sense and makes it less mindful of controlling costs than it would be if its customers resided exclusively in the private sector” (6).

So, military spending not only wastes taxpayer dollars, but also damages private companies, as well as the wider economy as a whole. An example of this damaging effect is the American machine-tool industry, which thrived during the 1940s and 1950s. Machine tools play a crucial role in the economy by increasing productivity, i.e. greater output using fewer resources. In the 1960s, the Defense Department became “the single largest customer for the machine-tool industry,” and “by 1967 the US for the first time imported more machine tools than it exported” (8). This illustrates an important principle: “the more an industry caters to the Pentagon, the less it makes decisions with the civilian economy in mind.” The more that the machine-tool industry came to rely on the Pentagon, the less value it was able to provide in the private sector. Woods cites a study which found that the growth of military research and development “has significantly retarded the growth of civilian R and D” (13).

This brings up again the crucial idea of opportunity cost; of the “unseen.” We will never know what discoveries and innovations have been foregone because civilian researchers simply don’t have the resources; military research has diverted them. Woods adds, “Even on those occasions when a legitimate advance in civilian well-being can be shown to have derived from military research, such research is not thereby vindicated. Here, too, opportunity cost ought to be
a central consideration. There is no non-arbitrary way to determine that funds diverted from civilian use to military research…yield greater social utility than the purposes to which people would have directed those funds themselves” (15). Ultimately, military spending bears responsibility for the full opportunity cost of “all the consumer and capital goods that never came into existence because the necessary resources were diverted to military production” (16).

Other costs of war are far more obvious and can be more tangibly expressed in money prices. According to a March 29, 2001 report from the Congressional Research Service, the total expenditures allocated by Congress for the wars in Iraq and Afghanistan since 9/11/2001 are $1.283 trillion. If the requested 2012 war spending is included, the total reaches $1.415. Even if troop levels in the two countries decrease as planned over the next decade, that total will grow to $1.8 trillion by 2021. However, this hardly begins to account for the entirety of the wars’ tangible costs.

In their 2008 book, The Three Trillion Dollar War, Nobel winning economist Joseph Stiglitz and Linda Bilmes attempt to quantify the full cost of the wars. Although their estimated $3 trillion price tag still falls short of World War II’s $5 trillion (in 2007 dollars), the amount spent per troop in Iraq is four times that of WWII (6). At that rate, and with every additional soldier in Afghanistan costing $1 million per year (Tiron), that record is unlikely to stand. A September 5, 2010, update from Stiglitz and Bilmes in the Washington Post brought the running tab near $4 trillion. The authors blame the wars for at least a quarter of the increase in the national debt from 2003-2008. “And that doesn't include future health care and disability payments for veterans, which will add another half-trillion dollars to the debt” (Stiglitz, 2010). Since the US government was already running a deficit before launching the wars in Afghanistan and Iraq, Stiglitz and Bilmes deem the entire cost to be funded through borrowing. They estimate
that the interest on that portion of the national debt will cost $1 trillion in interest payments over a 10-year period. Of course, if price inflation expectations push interest rates up, then that number could increase dramatically.

They point out that, “The costs of the war are real even if they have been deferred” by financing the war entirely through borrowing and monetary expansion. The reality of the wars’ costs however are heavily obscured by the Pentagon’s accounting system which is little more sophisticated than that of “a corner grocery store” and has flunked every financial audit since 1997. One result of this simplistic system is that it ignores the fact that the US military is “using up basic equipment and weaponry much more rapidly” than they can be replaced. In fact, the military is “churning through equipment at six to ten times the normal, peacetime rate.” As a consequence of this capital consumption, “It lowers the current cost of the war and allows some of the costs to be shifted into the general defense budget.”

Due to this obfuscation, as well as the position the wars hold within the broader Global War on Terror (GWOT), the wars’ costs can hardly be considered outside the context of the US national security spending as a whole. Unfortunately, the process of determining the total amount that the government spends on “defense” is not as easy as just looking at the Pentagon’s budget. Following similar analyses by economist Robert Higgs (2010), journalist Chris Hellman conducted a full scale investigation to discover the full expanse of the requested 2012 US national security budget (2011).

The headline Pentagon budget comes in at $676 billion, but that is merely the beginning of the story. Many national security-related functions are squirreled away, split up among various agencies. The Energy Department oversees the nuclear weapons program, and the Department of Homeland Security and the various intelligence agencies are budgeted separately.
After including Veterans Affairs, the State Department’s war- and terror-related activities, benefits for military and Defense Department retirees, and any interest paid on debt used to fund national security, the grand total tops $1.2 trillion, nearly one-third of the government’s entire budget. Taking just the headline Pentagon budget into account, the US still spent 43% of the world’s combined military budgets as of 2010, and nearly 6 times more than the second most profligate nation, China (List of Countries).

In addition to the wars currently being waged in the Middle East, a major contributing factor to the ballooning US military budget is its vast worldwide network of bases “so large and shadowy that no one -- not even at the Pentagon -- really knows its full size and scope” (Turse). Estimates conducted by Chalmers Johnson and Nick Turse pin the number of US military bases in foreign nations at well over 1,000. According to Johnson, “as of December 2007, the United States had 510,927 service personnel…deployed in 151 foreign countries” (2010, 121). During NFL broadcasts on FOX, sportscasters regularly extend greetings to “our men and women in uniform, watching in 175 countries around the world.”

Johnson writes, “Once upon a time, you could trace the spread of imperialism by counting up colonies. America’s version of the colony is the military base” (114). History is replete with stories of overextended empires collapsing under their own weight, and the US has no reason to escape as the first exception. Yet, military spending inexorably continues to grow, demonstrating what Johnson calls “military Keynesianism.” He warns against the misguided attempt to present national security spending as economically beneficial. “Military industries crowd out the civilian economy and lead to severe economic weaknesses. Devotion to military Keynesianism is, in fact, a form a slow economic suicide.” Johnson goes on to quote a 2007 study led by economist Dean Baker, who concluded that “most economic models show that
military spending diverts resources from productive uses…and ultimately slows economic growth and reduces employment” (143). Clearly, war and militarism entail huge economic costs, both seen and not seen. Costs of this magnitude present governments with the difficult problem of how to finance them. It is to this question that we now turn.

**Financing of War**

A government at war has three methods of financing the expense: taxation, borrowing, or inflation (defined here as an increase in the money supply). Increasing taxes is rarely popular and is likely a path only taken for wars that are more defensive in nature, which tend to be more popular. When it comes to wars of choice, such as the US war in Iraq, governing authorities are loath to turn to taxation. The advantages of funding war through taxation (at least for the taxpaying citizens) are the transparency and accountability that result from the direct financial burden. These very same characteristics are what motivate political leaders to shy away from using taxation to fund foreign interventions. They reduce rulers’ flexibility in exercising their unilateral will, and demand robust and ongoing justifications for war-making.

A government reluctant to increase taxes can still fund its wars through borrowing in the open market, competing with other investment opportunities for investors’ funds. Although this method is less direct than taxation, it will crowd out private investment, reduce growth in the capital stock, and shift resources towards current consumption instead. Another result of increased government borrowing is an increase in the interest rate above what it would have otherwise been, thereby increasing the government’s interest expense as well as rendering
marginal private investment projects unprofitable. Also, borrowing only averts taxation in the short run; eventually the borrowings must be paid back out of increases in tax receipts.

During times of war, these constraints almost always lead government officials down the third and most destructive path: monetary expansion. There are differing methods of implementation, and in cruder times, government treasuries would simply physically print up the money they needed to pay for the war. This would lead very quickly to a dramatic fall in the currency’s value. This was the path taken by the Continental Congress in the US War for Independence from Britain. According to historian H.A. Scott Trask, “taxation was never even considered” as an option to pay for the war. The paper bills, known as “ Continentals,” were first printed in 1775. Within a year, the inflationary effects were being felt throughout the colonies, prompting state legislatures to respond with price controls, which predictably resulted in “massive shortages.” By 1781, the Continental was trading between 1/100th and 1/1,000th of its face value, totally worthless, “not worth a Continental”.

Modern governments – and in particular the US – have taken a more sophisticated approach, combining borrowing and inflation. In this case, the central bank buys up government debt with funds created out of thin air. This way, the government can increase its borrowings while still maintaining low interest rates due to the increased money supply. Also by injecting the new money into the capital markets through the banking system, rather than paying directly for arms and soldiers with newly printed cash, the effects of inflation are more nuanced and less noticeable. That is, after all, the chief goal of inflation as a tool of war funding: its obscurity. Inflation is no less a tax than direct taxation or borrowings, but it is a stealth tax. The economic dislocations of inflation are often taking place behind the scenes, deep in the capital structure, in the realm of Bastiat’s “unseen.” Everyday citizens are unlikely to understand the consequences
of such monetary expansion, especially before general increases in prices become apparent. And when they do, government officials are often able to effectively blame businesses for the inflation. They are, after all, the immediate agent, if not the fundamental agent of change. Again, the seen obscuring the unseen.

**War and Inflation in American History**

There are many historical episodes in American history that illustrate this relationship between war and inflation, even before the Revolutionary War. In his *History of Money and Banking in the United States*, Murray N. Rothbard provides the details of many of these episodes, noting that “[w]ar has generally had grave and fateful consequences for the American monetary and financial system” (72). This theory is illustrated by the colonial government of Massachusetts, which had the dubious distinction of producing the first fiat paper currency seen in the Western world in 1690. Unsurprisingly, the endeavor necessitating such money-creation was state-led warfare.

According to Rothbard, “Massachusetts was accustomed to launching plunder expeditions against the prosperous French colony of Quebec” (51). Normally, the soldiers would simply be paid out of the loot resulting from a successful campaign. But this time, the French soundly beat back the attack and the aggressors returned to Massachusetts empty-handed. Desperate to mollify its disgruntled military, the Massachusetts government issued 7,000 pounds in paper notes to pay the soldiers, pledging to redeem them in gold or silver and make this a one-time occurrence. However, in 1691, the Massachusetts government printed another 40,000 pounds to pay off state debt. By this time, “the new paper pound had depreciated on the market
by 40 percent.” As for the government pledge to honor specie (precious metal) redemption, “all the bills continued unredeemed for 40 years” (52).

The failed campaign of 1690 and its aftermath did not deter the militaristic ambitions of the Massachusetts government for long. In 1711, another failed mission resulted in an issue of 500,000 pounds of fiat money, and in the period of 1744-1748, in the wake of still another losing effort against the French, paper notes in circulation increased by over seven times. The notes ended up worth only 10% of their original 1690 value.

We have already noted the inflationary experience during the War for Independence, which then influenced the Constitutional prohibition against state paper money, and the implicit rejection to all fiat paper. However, this lesson was quickly forgotten in the War of 1812, which was largely funded by notes issued by southern state banks. The money was almost entirely spent in the northeast, where the fighting was concentrated, causing economic dislocations and price increases in the region, with wholesale prices increasing 35% from 1811-1815. When the banks there sought to redeem the paper notes, the issuing banks faced the prospect of insolvency. In what Rothbard calls “one of the most flagrant violations of property rights in American history, the [issuing] banks were permitted to waive their contractual obligations to pay in specie while they themselves could expand their loans and operations and force their own debtors to repay their loans as usual” (74).

According to Rothbard, “the Civil War exerted an even more fateful impact on the American monetary and banking system than had the War of 1812,” effectively ending “the separation of the federal government from banking” (122). Federal spending rose from $66 million in 1861 to $1.3 billion in 1865, with much of this gap funded by the issuance of paper “Greenbacks.” Congress issued $300 million in Greenbacks in 1862 and another $150 million in
1863. “Over the entire war, the money supply rose from $45.4 million to $1.773 billion, an increase of 137.9 percent, or 27.69 percent per annum” (130). Wholesale prices doubled over the course of the war, and by the summer of 1864 the value of the Greenback had fallen 60%. In the wake of runaway currency depreciation, the government turned heavily to taxation and borrowing in the latter half of the war.

American involvement in the twentieth century’s worldwide conflagrations can hardly be imagined without the aid of the Federal Reserve’s monetary manipulation. It should be seen as no coincidence that the same president who signed the Federal Reserve Act of 1913, less than four years later had involved the US in a protracted European war. Woodrow Wilson’s grand fantasies of making the world “safe for democracy” could hardly have been pursued without the Fed’s willingness to purchase government war bonds at subsidized interest rates. This is evidenced by the fact that both the money supply and consumer prices doubled from 1915-1920 (Friedman and Schwartz, 198). Although income tax rates skyrocketed during the war, they only accounted for 21 percent of war funding. “The remainder was funded by Fed-backed borrowing (56 percent) and outright money creation (23 percent)” (Paul, 66). It was in this environment that Ludwig von Mises wrote in 1919 that “one can say without exaggeration that inflation is an indispensable means of militarism. Without it, the repercussions of war on welfare become obvious much more quickly and penetratingly; war weariness would set in much earlier” (163).

This phenomenon is no better illustrated than by the current US wars in the Middle East. Not only have taxes not increased during this period, but rates were cut just after the invasion of Iraq in 2003. The vast costs of these wars, as well as all the other expansions of the national security state since 9/11/2001, have been funded entirely through monetary expansion and borrowing, which is facilitated to a significant degree by the Fed through its interest rate
manipulations. If the federal government had to depend solely on private investors to buy its vast bond issuances, interest rates would inevitably rise as the government bonds crowded out ever more private investments. But since the Fed is able to purchase Treasury debt with funds created out of thin air, it is able to keep interest rates, and therefore the government’s cost of debt, far lower than they would otherwise be. However, this arrangement can only be maintained by ever-more money creation by the Fed. At some point, either when the Fed reverts to a tighter monetary policy, or when price inflation becomes more widespread, interest rates will rise, leading to ever-higher government deficits. The populace has only belatedly begun showing concern over the ballooning government budget deficits and the skyrocketing national debt. Unfortunately, few seem to be making the connection between the debt and US militarism.

While the historical and political connection between war and inflation is obvious enough, the question remains: is inflation a consequence or war, or is war a consequence of inflation? In some ways, the answer is: both. Some may argue that certain wars are necessary enough to justify inflationary measures that should be avoided in peacetime. For them, victory demands that if the more obvious financial tools of taxation and borrowing prove insufficient, then the government must turn to the printing press. In this case, inflation would be but an unfortunate corollary to a necessary war. However, the far more common occurrence demonstrates that monetary expansion is a tool that enables governments to wage wars it otherwise wouldn’t, extend wars it would otherwise end, and disguise the resulting costs. A government with a money printing press is a government looking for a fight, and a government less accountable to its citizens.
War and Civil Liberties

Now that we have seen the way that inflation uniquely enables governments to fund the mammoth costs of war, let us turn to the second link in the chain: the way in which war abroad undermines civil liberties at home. American history is replete with examples of this phenomenon from the earliest days of the republic. Politicians have always sought to expand their power by taking advantage of fear; when the populace perceives danger to their security, they will far more readily accept incursions into their personal liberties that they wouldn’t think of tolerating in calmer times.

In his book War and Liberty, law professor Geoffrey R. Stone provides accounts of several periods of conflict in America and how civil liberties fared during those times. The nation had scarcely finished electing its second president when it faced its first major attempt to curtail the freedoms hard won in the Revolutionary War. In the mid 1790s, the US found itself caught in the middle of the ongoing feuds and wars between Britain and revolutionary France. Following a treaty between the US and Britain, signed in 1794, France began seizing American ships. The patriotic fervor that then swept the US resulted in legislation that threatens American liberties to this day.

In the wake of the 1796 presidential election – in which John Adams narrowly defeated Thomas Jefferson – a bitter rivalry developed between America’s two major political parties, the Federalists and the Republicans. The Federalists, represented chiefly by Adams and Alexander Hamilton, took a generally conservative outlook, favoring a strong central government and a strong projection of military power. On the other side, the Republicans, led by Jefferson and James Madison, were skeptical of involvement in European conflicts, and favored an extremely
limited laissez-faire central government. Many Federalists feared that the influx of European immigrants during the 1790s would “contaminate the purity…of the American character,” particular if it came to war with France (5).

Over the protests of the Republicans, the majority Federalists passed a pair of acts in 1798 limiting the rights of resident aliens. First was the Alien Enemies Act, which has sadly remained a permanent part of American wartime policy. The legislation “provided that, in the case of a declared war, citizens or subjects of an enemy nation residing in the United States could be incarcerated or deported at the direction of the president” (6). Unsatisfied with the extent of the Alien Enemies Act, the Federalists also passed the Alien Friends Act, which “empowered the president to detain and deport any noncitizen he deemed dangerous to the United States” without any formal charges, hearing, or chance for a defense of any sort for the detainee. The Republicans argued unsuccessfully that this “detestable” act vested an inordinate level of arbitrary power in the person of the president. Although the Alien Friends Act expired in 1801 when Jefferson took office, it has been unofficially resurrected during the current US War on Terrorism in the form of indefinite detention of any individual whom the president unilaterally deems to be an “enemy combatant.” This highlights the important role that prior precedent plays on the slippery slope of liberty restrictions.

Unfortunately, the two Alien Acts were not the only blows that civil liberties suffered in 1798. The Sedition Act, passed by the Federalists over the bitter opposition of the Republicans, outlawed any speech or publication that expressed a view “against the government of the United States, or either house of the Congress of the United States, or the President of the United States…” (8). Notably absent from the act’s protections was the position of Vice President, held at the time by opposition leader Thomas Jefferson. In fact, the act was employed solely against
President Adams’s political enemies; all fourteen indictments issued by the Adams administration were against partisans of the Republican Party. According to Stone, “The Federalist strategy was aimed directly at the presidential election of 1800” (12). Unfortunately, little has changed since that time. The Federalists were simply employing “a time-honored strategy for consolidating power,” namely “to inflate the public’s fears, inflame its patriotism, and then condemn political opponents as ‘disloyal’” (18). The Sedition Act expired with the Alien Friends Act in 1801, and lay officially dormant for over a century until Woodrow Wilson’s push for US entry in to World War I.

If John Adams and the Federalists laid the groundwork for later abuses of foreigners residing in the US during wartime, then Abraham Lincoln set the precedent for unilateral executive branch authority. Within a week of taking office, Lincoln issued an executive order suspending the writ of habeas corpus in response to secessionist agitation in Maryland, even disregarding a ruling by Chief Justice Roger B. Taney that the order was unconstitutional. The “Great Writ,” dating back to the Magna Carta, “is a judicial mandate directing a government official to present to the court an individual held in custody so the court can determine whether the detention is lawful. The writ is essential to the separation of powers, for it empowers an independent branch of the government – the judiciary – to decide whether the executive has detained an individual unlawfully” (24). The writ is an explicitly protected right in Article I, Section 9, Clause 2 of US Constitution.

Later, in the summer of 1863, Lincoln expanded his habeas suspension order to encompass the entire nation, following violent anti-draft riots. Anywhere between 13,000 and 38,000 civilians were imprisoned by the military during the war, and upwards of 300 opposition newspapers were shut down by military authorities. “Some individuals…were arrested merely
for expressing their political beliefs” (Stone, 38). Although sometimes expressing displeasure at some abuses of detention, “Lincoln did not act decisively to prohibit such arrests” (31). Like so many presidents before and after him, Lincoln was willing to sacrifice peacetime principles for wartime expediency.

The majority of America’s founding fathers and early leaders were extremely skeptical of getting involved in the twisted intrigues of European political alliances and warfare. In his farewell address, George Washington decried “those overgrown military establishments, which under any form of government are inauspicious to liberty, and which are to be regarded as particularly hostile to republican liberty” (1796). John Quincy Adams later echoed this sentiment, when he declared that, “[America] goes not abroad, in search of monsters to destroy,” but instead “has abstained from interference in the concerns of others, even when conflict has been for principles to which she clings, as to the last vital drop that visits the heart” (1821). This consensus remained largely intact until Woodrow Wilson’s visions of worldwide democratic grandeur embroiled the US in a brutal and stalemated European war and set the example that would guide a century of global US military involvement.

In a case of bitter irony to be repeated with FDR and WWII, Wilson was reelected in 1916 under the campaign slogan that he had “kept America out of war” (Stone, 42). But within a year, Wilson was seeking a declaration of war from Congress. Why the change of direction? While the ostensible justification was the sinking of several US vessels by German submarines, the US had been quietly supporting the British war effort for some time through loans and armament shipments. According to the important revisionist historian Henry Elmer Barnes, the reasons for US involvement in the World War I were “many and complex” (Riggenbach, 106). “Wilson was very pro-British in his cultural sympathies…. He did not desire to have the United
States enter the war if England seemed likely to win without our aid, but as soon as this appeared doubtful he was convinced that we should enter as early as he could persuade Congress and the country to follow him.” In pursuit of this persuasion, Wilson launched an official government propaganda campaign under the leadership of a public relations expert, George Creel. As director of the Committee on Public Information (CPI), Creel “produced a flood of pamphlets, news releases, speeches, newspaper editorials, political cartoons, and even motion pictures, all intended to engender a hatred for the enemy (Germany and Austria) and encourage suspicion of any “disloyal” citizens (Stone, 49).

But Wilson was not satisfied simply with persuasion. Barnes also noted among Wilson’s motivations a megalomaniacal lust for power and a “conception that unless he was at the Peace Conference he could not act decisively in bringing about a peace of justice and permanence” (Riggenbach, 106). Indeed, Stone notes that “Wilson was a man with little tolerance for criticism,” even declaring that “if there should be disloyalty, it will be dealt with with a firm hand of stern repression” (42). This promised repression first took form in the Espionage Act of 1917, passed by Congress less than three weeks after granting the president’s request for a declaration of war. The legislation as presented by the administration, outlawed any publication that the president deemed “useful to the enemy” or causing “disaffection in the military” (46). Although the final version approved by Congress was tempered to some degree, the Wilson administration pursued prosecutions under the act zealously, with Attorney General Thomas Gregory declaring, “May God have mercy on [war dissenters], for they need expect none from…an avenging government” (49). At Gregory’s urging, concerned citizens formed private organizations that attacked, harassed, wiretapped, reported, and even killed fellow citizens they suspected of disloyalty.
In its eagerness to stamp out dissent, the Wilson administration prosecuted more than 2,000 dissenters during the war “for allegedly disloyal, seditious, or incendiary speech” (54). Victims were sentenced to prison terms of up to 20 years for the offense of promoting Christian pacifism, or making statements such as, “the government is for the profiteers” (55). In one case, film maker Robert Goldstein was sentenced to 10 years for producing a movie about the Revolutionary War that portrayed the British in a negative light, an unacceptable affront to America’s key ally in the war effort according to the Wilson Administration. According to Stone, “it became impossible to question the war or the draft without running the risk of being accused of unlawfully obstructing the war effort” (56). Despite this unfortunate reality, the Wilson Justice Department was not satisfied with what it saw as “loopholes” in the Espionage Act. Congress caved to the administration’s pressure, passing the even more draconian Sedition Act of 1918, which criminalized any “abusive language” about the government or the military. The Supreme Court upheld both acts in response to challenges brought by citizens convicted under the laws for distributing pamphlets critical of the draft.

In 1923, President Coolidge released from prison all remaining victims of the Wilson Administration, and a decade later, President Roosevelt granted amnesty to all convicts of the Espionage and Sedition Acts. The indignation spawned by the Wilson Administration’s extreme persecution of political speech formed the foundation and inspiration of the modern civil liberties movement. This dark period demonstrated Americans’ willingness to, in the words of John Dewey, “grovel in the sacrifice of their liberties” in a time of war (Stone, 63). While Congress repealed the Sedition Act in 1920, the Espionage Act remains on the books to this day, along with the Alien Enemies Act. As demonstrated time and again in American history, episodes of rapid growth in government power usually recede, but never all the way back to its original level.
In his indispensable study, *Crisis and Leviathan*, economist Robert Higgs dubs this phenomenon the “Ratchet Effect.” Governments invariably take advantage of various crises (most particularly war, but also economic crises, as evidenced by the Great Depression and the 2007-8 financial crisis) to expand their influence and power. These advances necessarily involve some measure of intrusion into citizens’ civil liberties. The trade-off between government power and individual liberty is zero-sum; an increase in one necessarily entails a decrease in the other. When the crisis – or at least the fervor surrounding it – finally subsides, the government will normally walk back some of its growth, but never all. Post-war budgets, although generally smaller than wartime, never shrink all the way back to pre-war levels. Some wartime limits on free speech or travel may be repealed, and the courts may strike down others, but invariably, some remain – even if left unenforced for decades, such as the Alien Enemies Act or the Espionage Act. These remnants of past government abuse lay dormant, lurking in forgotten memory, but quietly forming the foundation for future government power-grabs. Provided with an already advanced starting point, each new crisis invites unprecedented levels of government encroachment into liberties previously deemed sacred.

This phenomenon was exhibited in the run up to US entry into World War II. In anticipation of US entry into another European conflict, the ghost of the Alien Friends Act rose from the grave in the form of the Alien Registration Act of 1940, which “required all resident aliens to register with the Immigration and Naturalization Service (INS). This was the first time the United States had ever made such an ‘inventory’ of noncitizens” (Stone, 64). In the wake of the attack on Pearl Harbor, the government immediately classified all 900,000 Italian, German, and Japanese nationals as “enemy aliens” under the Alien Enemies Act of 1798. As enemy aliens, these individuals were subject to restrictions on travel, and forbidden to possess radios,
cameras, or weapons. Eventually, these restrictions were lifted for Italians, and lightly enforced for Germans. But the 40,000 Japanese subject to the act would not fare so easily.

In February of 1942, President Roosevelt issued Executive Order No. 9066 which authorized the military to transfer anyone of Japanese descent to ten “resettlement communities” in isolated areas throughout the country. Stone describes the outcome of FDR’s order:

Over the next eight months, almost 120,000 persons of Japanese descent were ordered to leave their homes in California, Washington, Oregon, and Arizona. Two-thirds of these individuals were *American citizens*, representing almost 90 percent of all Japanese-Americans. No charges were brought against these individuals. There were no hearings. They did not know where they were going, how long they would be detained, what conditions they would face, or what fate would await them. They were ordered to bring only what they could carry. Many families lost everything (66).

The president’s order was opposed by many in the administration, including the Department of Justice, the FBI, and Naval intelligence, which saw no credible military necessity for the detentions. Why then did FDR pursue such a severe policy? According to members of his cabinet, Roosevelt often ignored the legality of actions he deemed necessary. Attorney General Robert Jackson remarked that, “Because he thought that his motives were always good for the things that he wanted to do, he found difficulty in thinking that there could be legal limitations on them.” Jackson’s successor, Francis Biddle, who had unfailingly opposed the Japanese detention policy, astutely commented later that “the Constitution has never greatly bothered any wartime President” (74). Another major factor in motivating the internment order was driven by domestic political considerations. Patriotic xenophobia was at a fever pitch on the West coast.
following the Pearl Harbor attack. Roosevelt and the Democrats faced an important election in 1942, and depended heavily on the West coast vote. FDR then delayed the release of the detainees until December of 1944, notably after he had secured a fourth term as president.

By the time of the Vietnam War, the experiences of the two world wars had brought about a shift in American political culture that valued more highly freedom of political speech and protection against arbitrary internment. Because of this shift, presidents Lyndon Johnson and Richard Nixon did not have the public support necessary to implement overt legislation against war critics in the mold of Adams or Wilson or Roosevelt. Instead, they were limited to taking more indirect legal measures against dissenters, charging them with more mundane crimes such as trespassing, flag desecration, or draft-card burning. Unsatisfied with the effectiveness of such efforts to silence the growing opposition, they turned to “massive programs of surveillance, infiltration, and harassment in order to disrupt and incapacitate the antiwar movement” (Stone, 111). This was nearly all done covertly.

The FBI led the way, directed by J. Edgar Hoover and his secret counterintelligence program (COINTELPRO) which he had first developed in the 1950s to monitor suspected Communist sympathizers. The FBI began focusing its COINTELPRO methods on war critics in 1968, eventually mobilizing 2,000 agents, 1,700 domestic intelligence informants, and 1,400 “confidential” sources (117).

In its campaign to destabilize the antiwar movement, the FBI sent anonymous letters to employers, landlords, parent, and schools accusing antiwar protesters of drug abuse, homosexuality, and treason. It distributed bogus campus newspapers defaming peace activists, sent fraudulent letters to supporters of antiwar political candidates to sabotage their campaigns, spread false rumors that antiwar leaders were embezzling funds or cooperating with the FBI,
incited local police departments to harass antiwar activists for minor offenses, and disrupted
peaceful demonstrations (113).

The FBI wasn’t the only government agency prying into the private lives of peaceful
citizens. In 1967, the CIA started covertly monitoring a wide-ranging collection of antiwar
organizations and individuals, eventually gathering information on more than 300,000 people.
Army intelligence ran a similar operation, assigning 1,500 agents to collect data on practically
every American group seeking political change. They ultimately built files on more than 100,000
war opponents, including Senator Adlai Stevenson, Martin Luther King Jr., the American Civil
Liberties Union, and the American Friends Service Committee. The NSA joined the effort in
1969, intercepting phone calls of political activists. Under the Nixon Administration, the IRS
conducted targeted audits of those on the White House’s “enemies list.”

The FBI’s COINTELPRO activities were finally exposed in the spring of 1971, and the
program was officially shut down later that summer. In 1978, Congress passed the Foreign
Intelligence Surveillance Act (FISA), which aimed at providing a remedy for Cold War and
Vietnam era abuses. The act required US intelligence services to obtain a warrant from a
specially-designated FISA court before wiretapping anyone legally residing on American soil.
Unfortunately, this legislation did not put the issue to rest for long, as will be discussed below.

While periods of crisis (real and imagined) in American history have invariably been
accompanied by surges in government power, the exact form that surge takes can vary uniquely
from situation to situation. This is often a reflection of the prevalent political tides of the period,
which ebb and flow over time. However, this phenomenon is often counter-balanced by the ever-
advancing precedents set during previous eras of crisis. This paradigm is important to keep in
mind when assessing the growth of government powers since 9/11/2001.
In some ways, the response of George W. Bush to the terrorist attacks of 9/11 was a markedly positive improvement from his predecessors. In contrast to Wilson’s anti-German rhetoric and FDR’s brazen internment of Japanese, Bush instead cautioned the American public against hostile reactions to Muslims in general. In addition, it is hardly imaginable that anyone could or would be directly prosecuted by the federal government for antiwar speech. Both of these differences clearly reflect shifts in American political values over the last century.

However, this is about as far as the good news goes. It wasn’t long before Bush was revamping the disloyalty message employed since at least John Adams: “You’re either with us or with the terrorists.” The theme was picked up by the rest of his administration, with Attorney General John Ashcroft stating, “To those who scare peace-loving people with phantoms of lost liberty, my message is this: Your tactics only aid terrorists” (Stone, 129). Compare these quotes to others from American history, such as John Adams claiming that those opposing a military buildup “would sink the glory of our country and prostrate her liberties at the feet of France” (5), or Woodrow Wilson declaring that “there are citizens of the United States…who have poured the poison of disloyalty into the very arteries of our national life” (43).

Unfortunately, political demonization wasn’t the only challenge the American citizenry faced to their liberties from the Bush Administration. While public sentiment is markedly more suspicious of overt government attempts to restrict civil liberties today than in past wartime periods, the executive branch, following the lead of Lincoln, LBJ, and Nixon, has taken unprecedented steps to secretly and unilaterally enact measures that would be politically less viable if pursued through normal legislative channels. In the wake of the 9/11 attacks, the Bush Administration began implementing a regime of secret arrests and detentions of anyone the president deemed an “enemy combatant.”
One of the most egregious examples was the case of Jose Padilla, an American-born citizen who was arrested in Chicago in May, 2002 on the suspicion that he was part of a “dirty bomb” plot. However, the tip had come from a source who had been tortured into “confessing” the information, and the evidence never proved strong enough to formally charge Padilla in connection with any bomb plot. Instead, he was imprisoned for three and a half years without being charged with any crime. During this time, he was not allowed any contact with the outside world, and was subjected to “harsh interrogation techniques”, known in simpler times as torture. In a November, 2006 brief, arguing a motion to dismiss, Padilla’s attorneys outlined the treatment he endured at the hands of the government: He was kept in solitary confinement in a tiny windowless cell, unable to tell what time of day or night it was. He was made to endure severe sleep deprivation, extremely cold temperatures, threats of execution, noxious gasses, physically abusive interrogations, and hours spent bound in painful stress positions (Motion).

The government eventually indicted Padilla with the crime of “criminal conspiracy”, a charge that was completely unrelated to the alleged dirty bomb plot. Even this path was pursued “only because the U.S. Supreme Court was set to rule on the legality of their treatment of Padilla, and indicting Padilla enabled the administration to argue that his case was now ‘moot’” (Greenwald 2006).

Although Padilla’s story is one of the most disturbing examples of executive power under the Bush Administration, other developments in the GWOT are equally troubling. An Executive Order issued by President Bush on November 13, 2001, authorized that terror suspects would be tried by military tribunal rather than in federal court, which has been the longstanding norm. In fact, the plotters of the 1993 World Trade Center bombing were indicted, tried, and convicted in federal court in New York, as was attempted “shoe bomber” Richard Reid. Under the military
trials established by Bush, the government is allowed to present: a) secret evidence, unknown to the defendant, b) coerced confessions, and c) hearsay evidence, all drastic departures from legal standards dating back at least to Roman times (Stone, 139). In 2006, the Supreme Court nullified the second two “features”, but Congress responded with legislation allowing both (138). According to Constitutional lawyer Glenn Greenwald, the Military Commissions Act of 2006 essentially legalized the type of treatment suffered by Jose Padilla (2006).

One of the most important and uniquely troubling aspects of the Padilla case – beyond the shocking fact that no one in the government has in any way been held accountable for such treatment of an American citizen – is the secrecy surrounding it. Stone puts Padilla’s experience in the context of past abuses by the American government:

The Alien Friends Act of 1798 did not authorize the detention of citizens and did not authorize secret incarceration; Lincoln’s suspensions of habeas corpus granted detained trials before military tribunals and did not involve secret detentions; and even the World War II internment was a public act that did not hold anyone incommunicado (135).

Had it not been for the fact that the government “slipped up” by assigning him a lawyer, “Jose Padilla would simply have disappeared from the face of the earth.” Stone adds, chillingly, “To this day, we have no way of knowing how many other American citizens, if any, remain in custody.”

Unfortunately, the secrecy doesn’t stop with indefinite detention. Section 215 of the USA PATRIOT Act, pushed through Congress just weeks after 9/11/2001, authorizes government officials to secretly obtain records (financial, medical, etc.) about any American citizen without providing any probable cause, and even criminalizes notifying the subject of the investigation.
Within months of 9/11, President Bush secretly authorized the National Security Agency (NSA) to conduct electronic surveillance of American citizens on American soil without probable cause and without a warrant as required by the FISA of 1978. This program operated in secret for nearly five years before being exposed by the New York Times in 2006. Apart from the damage inflicted on civil liberties by such secret programs, the secrecy itself may pose the gravest threat of all to American freedom. After all, how can the public stop programs of which it is unaware?

In past wars, any restrictions of liberty at home were at least – on the surface – understood by both the perpetrators and the victims as temporary measures justified only by relatively short term periods of emergency. But with the Bush Administration’s declaration of a Global War on Terror, the crisis that serves as the excuse is measured in generations rather than months or years. Stone writes, “A war of indefinite duration…seriously increases the risk that ‘emergency’ restrictions will become a permanent feature of American life” (129). In such a setting, the potential permanence of any new government powers demands a level of skepticism and scrutiny far greater than that demanded in the past. Unfortunately, more than two centuries of ratcheting government power seem to have largely desensitized the American populace to the gravity of the situation.

Many American voters, eager for a departure from eight years of the Bush presidency, cheered the election of Barack Obama, who ran on a campaign of “change.” Sadly, voters have not seen the change they voted for, at least not in the area of the War on Terror and its effects on civil liberties. Far from a change in direction, President Obama has maintained or extended nearly every Bush-era program in the area of national security. After pledging to close the military prison at Guantanamo Bay (where hundreds of suspects have been held without charge for nearly a decade) and give detainees civilian criminal trials in federal court, Obama instead
issued an executive order on March 7, 2011 that created “a formal system of indefinite detention” (Finn). What started out as a rogue program under Bush is being formally ensconced in legal precedent by Obama. In a new development all his own, Obama has also asserted the right to summarily assassinate US citizens living abroad who he suspects of involvement in terrorism (Greenwald 2010). It appears to matter little who occupies the Oval Office; civil liberties have always been and will always be under threat as long as the US continues to pursue its militaristic bent.

Conclusion

Thus far, we have observed the immense costs of war, both seen and unseen. We have examined the tendency of the US government to habitually turn to inflationary methods in order to fund these costs. We have also seen how war and the culture it spawns has repeatedly facilitated the growth of government power and resulted in the loss of political and civil liberties. This essay asserts that this chain of events entails a causal connection; that through the mediums of war and militarism, the Federal Reserve bears direct and significant responsibility for the destruction of civil liberties that Americans have experienced throughout their history and particularly since 9/11/2001. But why should this necessarily be so? Could it not just be an accidental coincidence of history that inflation, wars, and losses of liberty tend to crop up together? After all, correlation does not prove causation. Some may deny any direct relationship between economic policy and political freedoms.

Milton Friedman called such a view “delusional.” In his popular book, Capitalism and Freedom, he finds “an intimate connection between economics and politics” (8). Friedman
outlines two key ways in which economic arrangements can promote a free society. First of all, he found that economic freedom is an end unto itself, as a subset of freedom in general. Secondly, economic freedom is also indispensable in the attainment of political freedom. The reason that economic freedom is able to accomplish this is because it “separates economic power from political power” (9). A planned economy, in contrast, requires the consolidation of economic and political power. Should it then really surprise us that centralized government control over the money supply is accompanied by an oppressively powerful political structure?

If the Fed was not able to make war seem so financially painless in the short run, if the costs of war were more directly felt by the American populace, then perhaps the civil liberties losses which invariably accompany wartime could be avoided. It is inconceivable that the American people would tolerate the dramatic violations of their civil liberties as they have outside of the fevered patriotism of wartime. It is equally inconceivable that such wartime episodes would occur so often or last so long as they have outside of the Fed’s assistance. Economist Thomas DiLorenzo points out that without the Fed to monetize the costs,

There would not be as many wars, and the ones that do occur would likely be shorter, if they were paid for through direct taxation. Taxpayers feeling the sting of gigantic wartime tax increases would be much more inclined to pressure their governmental representatives to limit their military adventures to national defensive purposes, as opposed to imperialistic ventures based on more dubious motives. Americans may agree with the goal of ‘spreading democracy around the globe’ as long as they believe it won’t cost them much (or anything). Present them with an explicit tax bill for it, however, and many of them will reverse their opinion (2008 39).
We have seen time and again in American history the pattern of monetary expansion enabling warfare, which in turn justifies government restrictions of personal liberties. While this pattern is evident from the US’s very founding, its consequences have been even more heavily felt since the inception of the Federal Reserve in 1913. According to Representative Ron Paul, “It is no coincidence that the century of total war coincided with the century of central banking. When governments had to fund their own wars without a paper money machine to rely upon, they economized on resources. They found diplomatic solutions to prevent war, and after they started a war they ended it as soon as possible” (63). Indeed, economist Joseph Schumpeter opined that even if a fiat paper currency were demanded by sound economics (which it is not), it should still be opposed on the grounds of personal liberties and peace (1954, 405). A government unfettered by short-term financial concerns is far less likely to be restrained by the weaker chains of public opinion.

For most travelers enduring the humiliation of “enhanced” TSA pat-downs at the airport, the Fed is likely the last place they would direct their anger. For the victims of illegal wiretaps or indefinite detention, the Fed is probably the furthest culprit from their minds. If Jose Padilla were to sue government officials for his treatment, Fed Chairman Ben Bernanke is unlikely to be among the defendants. While many may have a hard time seeing the Fed in any context outside of arcane technical monetary policy issues, we must come to recognize the Fed for what it is: the very lifeblood of the leviathan state. The Fed’s monopoly on currency and the issuance of money and credit are indispensable to an activist government. In particular, the Fed is an essential prop for the warfare state and its deleterious effect on civil liberties. The Fed must be held responsible for a significant portion of every destructive or invasive government policy that has ever afflicted the American people (not to mention the millions of foreign victims of US warfare). If the
American people care to restore their lost civil liberties, they must strike at the root of the problem; they must end the Fed.
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