The Troubling Suppression of Competition from Alternative Monies: The Cases of the Liberty Dollar and E-gold

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Proposals abound for reforming monetary policy by instituting a less-discretionary or nondiscretionary system ("rules") for a fiat-money-issuing central bank to follow. The Federal Reserve's Open Market Committee could be given a single mandate or more generally an explicit loss function to minimize (e.g., the Taylor Rule). The FOMC could be replaced by a computer that prescribes the monetary base as a function of observed macroeconomic variables (e.g., the McCallum Rule). The role of determining the fiat monetary base could be stripped from the FOMC and moved to a prediction market (as proposed by Scott Sumner or Kevin Dowd). Alternative proposals call for commodity money regimes. The dollar could be redefined in terms of gold or a broader commodity bundle, with redeemability for Federal Reserve liabilities being reinstated. Or all Federal Reserve liabilities could actually be redeemed and retired, en route to a fully privatized gold or commodity-bundle standard (White 2012). All of these approaches assume that there will continue to be a single monetary regime in the economy, so that the way to institute an alternative is to transform the dominant regime.

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A different approach to monetary reform is to think about ways that alternative monetary standards might arise in the marketplace to operate in parallel with the fiat dollar, perhaps gradually to displace it. This approach prompts us to look at the alternative monetary systems that are currently available, or could become available if allowed. We can try to evaluate the likelihood that members of the public would spontaneously adopt, wholly or partially, one or more alternative systems (White 1989). Of more immediate relevance—and the avenue taken here—is to consider how legal restrictions are currently blocking the process of monetary innovation, and examine the case for removing such obstacles.

In his monograph *Choice in Currency*, F. A. Hayek (1976: 17) proposed an end to any legal barriers that block the monetary use of foreign fiat currency or gold within any domestic economy: "But why should we not let people choose freely what money they want to use? By 'people' I mean the individuals who ought to have the right to decide whether they want to buy or sell for francs, pounds, dollars, D-marks, or ounces of gold." He believed a government's "claim to a monopoly, or their power to limit the kinds of money in which contracts may be concluded within their territory, or to determine the rates at which monies can be exchanged, to be wholly harmful." Thus, governments should "bind themselves mutually not to place any restrictions on the free use within their territories of one another's—or any other—currencies, including their purchase and sale at any price the parties decide upon, or on their use as accounting units in which to keep books."

Increasing the competition among central banks for market share, Hayek argued, would make each of them more serious about keeping the inflation rate close to zero. Hayek's antimonopoly message bears re-emphasizing in light of the new technologies for producing private monies, and the troubling recent government efforts to suppress them in the United States and elsewhere. Open competition would enable ordinary money-users to protect themselves against bad money. It might even elicit better behavior from central banks, much as competition in express package delivery has elicited better behavior from the U.S. Postal Service. For the sake of money-users, legal barriers should be removed not only against traditional gold- and silver-based monies and foreign fiat monies, but also against new types of commodity-based monies and the new noncommodity cyber-monies.

The potential alternative monies include: (1) foreign fiat monies in paper or account-balance form; (2) physical gold and silver coins, and banknotes redeemable into them, for which the Liberty Dollar project provided one model; (3) electronically transferable gold account balances, such as e-gold; and (4) private noncommodity cybermonies, for example Bitcoin and Litecoin. Research is needed on how the holding and use of foreign monies is discouraged by various tax and regulatory policies. As detailed below, the Liberty Dollar and e-gold have been shut down and their entrepreneurs prosecuted by federal authorities. Bitcoin faces hostility from the same authorities.[1]

The U.S. federal government has been acting as though it resents challenges to its near-monopoly of basic money within the United States and is seeking to legally impede competition. If that sounds unduly alarmist, read the indictments and the accompanying press releases.

Ordinary citizens are harmed by the restriction of monetary competition. If we care about the welfare of ordinary citizens in their role as money users, then the law should allow the market for monies to be openly competitive. It should not make money production a privileged monopoly. To the same end, provisions in the law that grant the federal government the authority to ban non-fraudulent money enterprises, or subject non-dollar-based money services to higher obstacles than dollar-based services, should be removed. Prosecution of honest money entrepreneurs should stop.

The Story of the Liberty Dollar

The Liberty Dollar was a project of an entrepreneur named Bernard von NotHaus and his nonprofit organization, NORFED (National Organization for the Repeal of the Federal Reserve and Internal Revenue Code). Von NotHaus had previously produced collectable silver medallions as proprietor of a business called the Royal Hawaiian Mint. In October 2008, NORFED launched its one-ounce silver Liberty piece, with a face value denominated in dollars. Whether it was a coin became a disputed legal question because a federal statute prohibits the unauthorized issue of coins. The face value was initially $10, well above the then going price for

[1]For detailed accounts of the Liberty Dollar, e-gold, and Bitcoin cases, see Dowd (forthcoming), a study that provides the proximate inspiration for the present article.

other one-ounce silver pieces, and was later raised to $20 on newly minted pieces in a preprogrammed response to the rising price of silver.[2] The organization also issued dollar-denominated paper certificates ($1, $5, $10) redeemable at the same par rates for silver kept in storage at a warehouse. The Liberty Dollar project later introduced gold and platinum pieces in higher denominations and copper pieces in a $1 denomination.

The intention to offer a new kind of *circulating currency*, superior to the Federal Reserve's fiat money, was clear from the project's original name ("American Liberty Currency"), its promotional brochures, and its website. In mid-2005 the website masthead proclaimed Liberty Dollars to be "America's Inflation-Proof Currency."[3] At that point the Liberty Dollar website quoted a U.S. Treasury spokeswoman as confirming the legality of the project: "'There's nothing illegal about this,' Dickens said after the Treasury Department's legal team reviewed the currency. 'As long as it doesn't say legal tender there's nothing wrong with it.'"[4] It also quoted a Secret Service spokesman as stating, "It's not counterfeit money."[5]

In September 2006, however, the U.S. Mint issued a press release with an ominous message. It first advised that Liberty Dollar "medallions" were "not genuine United States Mint bullion coins, and not legal tender." No conflict there, as the Liberty Dollar's promoters did not claim otherwise. Indeed their whole marketing pitch was that these were an *alternative* to official currency. But then the press release added: "NORFED's 'Liberty Dollar' medallions are specifically marketed to be used as current money in order to limit reliance on, and to compete with the circulating coinage of the United States. Consequently, prosecutors with the United States Department of Justice have concluded that "the use of NORFED's 'Liberty Dollar' medallions violates 18 U.S.C.

[2]For a discussion of the innovative idea of denominating a paper claim to a specified weight of silver in a specified quantity of dollars, but discontinuously appreciating the parity by a programmed rule responding to the market price of silver, see White (2000) and Dowd (forthcoming).

[3]http://web.archive.org/web/20050826190151/http://www.libertydollar.org.

[4]http://web.archive.org/web/20050718013643/http://www.libertydollar.org/html/articles/gillis.htm.

[5]http://web.archive.org/web/20051025094552/http://www.libertydollar.org/html/articles/nelson.htm.

§ 486, and is a crime" (U.S. Mint 2006).[6] Note the suggestion that "to compete with the circulating coinage of the United States" is a crime per se, a suggestion unwarranted by the language of the statute in question.

Here is the full text of the cited statute (18 USC § 486—"Uttering Coins of Gold, Silver or Other Metal") that the Liberty Dollar was accused of violating:

> Whoever, except as authorized by law, makes or utters or passes, or attempts to utter or pass, any coins of gold or silver or other metal, or alloys of metals, intended for use as current money, whether in the resemblance of coins of the United States or of foreign countries, or of original design, shall be fined under this title or imprisoned not more than five years, or both.[7]

The U.S. Mint also warned that the "medallions might look like real money" because they bear inscriptions: "'Liberty,' 'Dollars,' 'Trust in God' (similar to 'In God We Trust'), and 'USA' (similar to 'United States of America')" and "images that are similar to United States coins"—namely, the torch of liberty and the Liberty Head. The latter image appeared on "the obverses of United States gold coins from the mid-1800s to the early 1900s." The 2006 press release did not take note of clearly dissimilar markings, such as the 800 phone number, "LIBERTYDOLLAR.ORG," and "ONE OUNCE 999 FINE SILVER" inscriptions on the reverse, nor did it suggest that the cited similarities constituted counterfeiting or fraud.

In November 2007, the FBI executed a seizure warrant against the Evansville, Indiana, head office of the Liberty Dollar organization, following what was reportedly a two-year investigation.

[6]Two of the more absurd and irrelevant statements made in the 2006 press release and by federal prosecutors were (1) that the U.S. Constitution bans private coinage, and (2) that the U.S. government has some kind of exclusive property right in the word "dollar" or the dollar sign. Private coinage was allowed to circulate before the Civil War, and the word "dollar" or the dollar sign appears on every price tag, traveler's check, and ordinary check in America. Moreover, as of 2006, the dollar sign had never appeared on any official U.S. coin; its first appearance came in 2007 on the $1 coin.

[7]www.law.cornell.edu/uscode/text/18/486#FN-1REF. Here "to utter" means to place into circulation.

Von NotHaus told a local newspaper that the FBI took gold, silver, and platinum stored on the site, together with "the dies used to mint the Liberty Dollars"; carted away "nearly two tons" of copper $1 pieces featuring Ron Paul's image; seized the organization's computers and files; and froze its bank accounts (Lesnick 2007, Taylor 2007).

When federal indictments came down in May 2009, von NotHaus was predictably charged with violating 18 U.S.C. § 486. More surprisingly, he was charged with violating 18 U.S.C. § 485, an anti-counterfeiting statue that provides for fines or imprisonment of anyone who "falsely makes, forges, or counterfeits any coin . . . in resemblance or similitude of any coin of a denomination higher than 5 cents . . . coined or stamped at any mint or assay office of the United States . . . or in actual use and circulation as money within the United States."[8] The Liberty Dollar's resemblance to official coinage was partial at most. As the U.S. Mint press release had noted, a Liberty Head had not been used on official coinage since the early 1900s. The two heads were not the same. Perhaps most distinctive, besides the 800 number and URL, was the Liberty Dollar's inscription "one ounce 999 pure silver," whereas no official U.S. silver coins had been in circulation since 1968, and none had ever been inscribed with a bullion weight or a fineness rating.

In addition, von NotHaus was charged with two counts of fraud and with conspiring with others to commit the previous offenses. All these charges related to the silver pieces. The legality of the paper certificates was not challenged by the indictments.

After a brief jury trial, von NotHaus was convicted in March 2011 on the two main charges, plus the associated conspiracy charges (Lovett 2011).[9] He was cleared of fraud charges. More than two and a half years later, he still awaits sentencing. Following the conviction, the federal government has taken further actions to harass and intimidate users of Liberty Dollars. As summarized by a reporter for *Coin World*, officials of the U.S. Secret Service and U.S. Attorney's Office declared in August 2011 that "Liberty Dollars held by collectors may be subject to seizure as contraband by federal law enforcement," having been determined by the court to be counterfeits (Gilkes 2011).

[8]www.law.cornell.edu/uscode/text/18/485.

[9]Full disclosure: I was contacted by the defense and agreed to testify in the trial but was never summoned to appear.

In December 2012, the Secret Service compelled eBay to disallow listings of Liberty Dollars for sale.

The policy lesson is that to open up the Federal Reserve dollar to free currency competition Congress needs to legalize private production of precious-metal and base-metal coins for those who might want a metallic alternative to fiat money. The first and principal step would be to repeal or declare unconstitutional the statute (18 USC § 486) against making, uttering, or passing any unofficial coinage.[10]

The history of the statute indicates clearly that it is a relic of the Civil War, enacted to bolster the seigniorage potential of the greenback, which is no longer in circulation. The present U.S. Code's language is essentially that of an Act of Congress of June 8, 1864, entitled "An Act to Punish and Prevent the Counterfeiting of Coin of the United States." The 1864 statute specified a fine up to $3,000 for any unauthorized person who "shall hereafter make, . . . or shall utter or pass, or attempt to utter or pass, any coin of gold or silver, or other metals or alloys of metals, intended for the use and purpose of current money, whether in the resemblance" of U.S. or foreign coins "or of original design" (Sanger 1866: 120–21). The act thereby disallowed any private party to produce ("make or utter") new coins, or to use ("pass") existing private coins.

Two types of private coins were in circulation at the time and served as substitutes for official currency. First, more than a dozen private mints had produced gold or silver coins during the California and other western gold and silver rushes (Kagin 1981). None were still in operation in 1864, the U.S. Mint having driven them out of business by opening branches in San Francisco and Denver. In both cities, the new U.S. Mint bought and used the equipment of a leading private mint. The Act banned the revival of any private mint to satisfy a preference for gold and silver over greenbacks, and banned the continued circulation of their existing products. Second, private merchants had begun supplying base-metal tokens for small change

[10]Rostcheck (2002) argues that any ban on private coinage is unconstitutional, on the grounds that Congress (in light of the 10th Amendment) has only the powers delegated to it by the Constitution, and the Constitution grants Congress only the powers to coin money, to "regulate the value thereof, and of foreign coin," and to punish counterfeiting. It does not delegate the power to ban private coins. But as he acknowledges, federal courts have long rejected unconstitutionality arguments based principally on the 10th Amendment.

as inflation, caused by the Union's copious printing of greenbacks, had banished official coins. Rising greenback-dollar prices had reduced the domestic purchasing power of legal-tender gold, silver, and even copper coins below their purchasing power on the world market, prompting residents of the Union to export, hoard, or melt them—the familiar effect known as Gresham's Law.

Private precious metal coins and tokens were convenient substitutes for greenbacks and fractional notes issued by the Treasury, so their continued circulation would have reduced the seigniorage revenue available to the Treasury from issuing greenbacks. Even if the use of an extraordinary revenue measure like banning private coinage was an understandable policy in a time of extraordinary revenue need like the Civil War, the federal government is in no such situation today. Government revenue is copiously supplied at lower deadweight cost by other means. Today the revenue motive provides no good reason to continue to ban private coins. The "general welfare" calls for a long-overdue restoration of the liberty of private firms or organizations to produce metal coins intended for use as money, and the liberty of ordinary people to use them as money.

As a second and supplemental step, the anticounterfeiting law (18 USC § 486) needs to be amended to clarify that pieces of *original design*, clearly marked to identify the producer as other than the U.S. Mint, are not to be considered counterfeit copies of official coins. Neither is it counterfeiting to make or use a private coin carrying one or more traditional design elements like the Statue of Liberty's torch, or the word "liberty" or "dollar," or the dollar sign ($), or any other element that is *not* a trademark of the U.S. Mint, when not part of an attempt to mimic the overall look of a current official coin in order to falsely pass an unofficial coin as an official coin.

Finally, to remedy an injustice, and to make it clear that the market is henceforth open to private mint entrepreneurs, the federal court system should vacate the conviction of Bernard von NotHaus, or the executive branch should pardon him.

The Story of E-Gold and Other Gold-Based Payment Systems

E-Gold Ltd. was a successful for-profit service offering transferable gold-denominated accounts. It worked in tandem with the sister service Gold and Silver Reserve Inc., hereafter G&SR, also known as OmniPay, which sold e-gold units to members of the public in exchange for official monies, and bought units back. Both firms were launched in 1996 by Dr. Douglas Jackson, a Florida oncologist. E-Gold also offered silver, platinum, and palladium accounts, but gold accounts ultimately held 97 percent of E-Gold's total account balances by market value (Jackson 2013a).

Like von NotHaus, Jackson viewed his product as a private currency immune to fiat money inflation. Jackson (2012: 10) told an interviewer that he liked to quote the following sentence from Vera Smith's *The Rationale of Central Banking* (1936), a classic work that reviewed historical debates over central banking versus free banking: "How to discover a banking system which will not be the cause of catastrophic disturbances, which is least likely itself to introduce oscillations, and most likely to make the correct adjustment . . . is the most acute unsettled economic problem of our day."

He then immediately commented: "A system and currency like e-gold, particularly after emergence and integration into the financial mainstream as a reserve asset used as a medium of settlement, can definitively solve this problem." Unlike the Liberty Dollar, which began as a hand-to-hand currency and introduced electronic transfers only later, e-gold was designed exclusively for Internet transactions from the start. E-Gold kept its account balances in grams of fine gold, and backed them 100 percent with gold bars warehoused in London.

Brian Grow et al. (2006) described E-Gold's service model this way in *Business Week*:

> Opening an account at www.e-gold.com takes only a few clicks of a mouse. Customers can use a false name if they like because no one checks. With a credit card or wire transfer, a user buys units of e-gold. Those units can then be transferred with a few more clicks to anyone else with an e-gold account. For the recipient, cashing out—changing e-gold back to regular money—is just as convenient and often just as anonymous.
>
> E-gold appeals to "gold bugs": people who invest in the precious metal and believe money ought to be anchored to it.

Jackson (2006: 76; 2013c) has always disputed suggestions that the system was anonymous, or that G&SR had no identity controls on persons buying or selling e-gold units, although in court he agreed that the controls were insufficient to block criminal abuse of the system.

E-Gold's customer base at first grew slowly, then more rapidly in 2000 and 2001 (Dibbel 2001). One symptom of success was the launching of competing "digital gold currency" payment systems, similarly providing in-house transfers from one account holder to another, such as e-Dinar (launched in 2000 through a partnership with E-gold); e-Bullion (2001); GoldMoney.com (2001); 3P Pay (2001), acquired by Crowne Gold in 2002; Pecunix (2002); and i-golder (2005).

Douglas Jackson told *Business Week* that "E-Gold has about 1.2 million funded accounts through which transactions worth $1.5 billion were conducted in 2005" (Grow 2006). He told a congressional hearing: "Since its inception, E-Gold has settled over 67 million individual transactions and is today processing 50,000–70,000 account-to-account transfers per day, valued at over $2.0 billion USD annually" (Jackson 2006: 75). Kim Zettner (2009) of *Wired* reported: "At E-Gold's peak, the currency would be backed by 3.8 metric tons of gold, valued at more than $85 million. E-Gold was now second only to PayPal in the online payment industry."

In his congressional testimony, Jackson (2006: 75) enumerated the benefits of the e-gold system as convenience and low cost for remittances and payments, finality (nonreversibility), and a store of value free from political risk:

> E-gold is a payment system that, unlike any other, allows people from any region or economic background to operate globally: a migrant worker can send value back home easily and a merchant can accept payment from someone in a third-world country who may be without access to a charge card or bank account. E-gold alone is free of chargeback risk, yet the fees for receiving payment in e-gold are a tiny fraction of those charged by any other systems. Thanks to e-gold, for the first time in history, normal people of modest means worldwide have the option of using a medium of exchange and store of value that is designed from the ground up to be immune to debasement.

The upward trajectory of e-gold ended in December 2005 when FBI and Secret Service agents raided three locations in Florida: the offices of G&SR (E-gold Ltd. itself was registered in the

Caribbean nation of St. Kitts and Nevis), Jackson's home, and the firm's computer servers in Orlando. According to Zettner (2009), federal investigators learned of E-Gold when they discovered that a ring of credit card scammers were using E-Gold accounts to transmit ill-gotten funds. The Department of Justice then targeted E-Gold itself:

> Its goal was to force the service to comply with [post-9/11] regulations governing money-transmitting services like Western Union and Travelex. Federal regulations required those businesses to register with the Treasury Department's Financial Crimes Enforcement Network (FinCEN), to be licensed in states that required it, to diligently authenticate the identity of customers and to file suspicious activity reports on shady-looking customers. But E-Gold wasn't doing this.
>
> Jackson believed E-Gold was exempt from regulation because it was a payment system not a money transmitter.

That is, E-Gold was transferring ownership of gold among its customers, not transmitting *money* in the manner of Western Union.[11] At the same time, Zettner (2009) noted, "Jackson insisted E-Gold wasn't a bank, either." Because E-Gold did not make loans, it indeed did not meet the joint criteria for being considered a bank (both taking deposits and making loans) and thereby being subject to bank licensure and "know your customer" bank regulations.

Was Jackson right to think, relying on the advice of his legal counsel, that then-existing statues and regulations did not apply to his service? That is a question for experts in the field of money-service business law, but some federal officials appear to have thought that he may have been right. Grow et al. (2006) reported:

> Federal officials reluctantly confirm this loophole: E-gold and other digital currencies don't neatly fit the definition of financial institutions covered by existing self-monitoring rules

[11]In response to a question from Rep. Ron Paul at a congressional hearing in July 2011, no less an authority than Federal Reserve chair Ben Bernanke insisted that gold is not money today (Fontevecchia 2011).

> established under the Bank Secrecy Act and USA Patriot Act. "It's not like it's regulated by someone else; it's not regulated," says Mark Rasch, . . . former head of the Justice Dept.'s computer crime unit. The Treasury Dept.'s Financial Crimes Enforcement Network (FinCEN) is studying ways to close the regulatory gap. Meanwhile, U.S. officials say E-Gold and similar companies should voluntarily do more to deter crime.

The phrases "don't neatly fit the definition of financial institutions covered" and "should voluntarily do more" as used here imply that E-Gold and other digital gold payment providers were not clearly compelled to do more by existing law.

Both before and after the raid, Jackson voluntarily cooperated with federal authorities by sharing information on suspicious account activity. He provided information that led to the identification and arrest of major credit-card scamming ringleaders. At his own initiative he blocked suspected criminals from cashing out their accounts. His defense attorneys provided evidence (*U.S. v. E-Gold* 2008: 68, 70, 74–75) that Jackson had met with IRS officials responsible for enforcement of the Bank Secrecy Act, and was waiting for a ruling from them on whether the firm needed to be licensed, when the raid took place.

The Justice Department nonetheless indicted Douglas Jackson (along with Reid A. Jackson and Barry K. Downey, identified as E-Gold's co-owners) in April 2007 on four charges (*DGC Magazine* 2008): "One count of conspiracy to launder monetary instruments, one count of conspiracy to operate an unlicensed money transmitting business, one count of operating an unlicensed money transmitting business under federal law, and one count of money transmission without a license under D.C. law."

They key statute in the money transmitting indictment was 18 USC § 1960 ("Prohibition of Unlicensed Money Transmitting Business"), which bans ownership or operation of an "unlicensed money transmitting business." The statute includes the following definition: "The term 'money transmitting' includes transferring funds on behalf of the public by any and all means including but not limited to transfers within this country or to locations abroad by wire, check, draft, facsimile, or courier." It is not clear from this language whether gold-denominated account balances count as "funds." The statute refers to the definition of money transmitting in another statute, 31 USC § 5330 ("Registration of Money Transmitting Businesses"), which offers a related but slightly different definition: "The term 'money transmitting service' includes accepting currency or funds denominated in the currency of any country and transmitting the currency or funds, or the value of the currency or funds, by any means through a financial agency or institution."[12] By this second definition, strictly interpreted, E-Gold would *not* seem to have been a "money transmitting service," because it did not transmit currency or funds "denominated in the currency of any country," nor "the value of the currency or funds" it had accepted, but rather transferred ownership of claims to purchased gold.

Making the argument that neither E-Gold nor G&SR fit the statutory definition of a money transmitting business under 18 USC § 1960 or 31 USC § 5330, specifically because they did not transmit claims to cash or currency, or that at best the statutes are unconstitutionally vague, the firms' attorneys filed a motion to dismiss the indictment's three counts related to money transmitting. In a memorandum opinion (*U.S. v. E-Gold* 2008) D.C. District Court Judge Rosemary M. Collyer denied the motion, ruling that under the statutory definitions "a business can clearly engage in money transmitting without limiting its transactions to cash or currency" because in the language of 18 USC §1960, "'Money transmitting' includes transferring funds on behalf of the public by any and all means." She implied, but did not argue explicitly, that claims to gold held on account are "funds" in the statute's sense of the term. The judge had previously quoted, and here seemed to accept without question, the indictment's description of the e-gold system as one in which "the account holder can then use the e-gold to buy a good or pay for a service, or to transfer *funds* to someone else" [emphasis mine]. Therefore, she ruled: "Defendants' alleged conduct, including, inter alia, transferring funds on behalf of the public by wire, qualifies them as a 'money transmitting business' under Section 1960."[13]

[12]www.law.cornell.edu/uscode/text/18/1960;www.law.cornell.edu/uscode/text/31/5330.

[13]Curiously, Judge Collyer quoted the language of a Financial Crimes Enforcement Network (FinCEN) regulation referring to "funds" but neglected to notice that it refers specifically to "funds denominated in currency." Gold ounces are not "denominated in currency" in the standard meaning of the phrase.

Assuming that gold holdings are "funds," the statement that the defendants engaged in *transferring funds on behalf of the public by wire* can only refer to the combined efforts of the two firms, G&SR and E-Gold, not either firm separately. In-house balance transfers among account holders, which E-Gold provided, are not *wire* transfers. G&SR wired money only to customers who sold e-gold holdings to it. Paying a customer who sells the firm gold is not, as such, transferring funds on behalf of the public. The combination of G&SR and E-Gold did provide a functionally similar service to money transmitting through the three-step combination of G&SR selling e-gold units to customer A for addition to A's account, E-Gold transferring the units on A's order to account-holder B, and then G&SR buying the E-Gold units from customer B.

Of course, functional similarity does not imply that either G&SR or E-Gold or both together fit the technical legal definition of a "money transmitting business" as then defined by the law. If they did not fit the legal definition, a would-be prosecutor should have no legal case. A practice that is a substitute for prohibited practices is not itself prohibited. A maker of small cigars cannot be prosecuted for not following rules and regulations on cigarettes written in a way that does not cover small cigars. As Jackson found out, however, contrary to the hopes of his firms' attorneys, relying on a favorable interpretation of the statutory language was not an effective defense. Once federal anti-money-laundering authorities decided that G&SR and E-Gold did not scrutinize customers to the authorities' satisfaction, namely at the level of licensed money transmitters, even if the firms' owners never intended to have criminals use their services, the authorities had the discretion to issue a set of indictments that a federal judge was unlikely to dismiss.

After his motion to dismiss the charges was denied, threatened with lengthy jail time and heavy fines, Douglas Jackson and his co-defendants agreed to a plea bargain.[14] Jackson was sentenced (Zettner 2009) to 36 months of "supervised release," including "six months of house arrest and electronic monitoring, and 300 hours

[14]According to the Department of Justice (2008) press release announcing the guilty pleas, "Douglas Jackson faces a maximum prison sentence of 20 years and a fine of $500,000 on the conspiracy to engage in money laundering charge, and a sentence of five years and a fine of $250,000 on the operation of an unlicensed money transmitting business charge."

of community service." He was also forced to turn over "about $1.2 million to the government." His firms were assessed $300,000 in fines. The feds did not seize the warehoused gold (which was in London), but even the most innocent account holders were left without access to their gold. "Also as part of the plea agreement," noted the Department of Justice (2008), "the businesses will create a comprehensive money laundering detection program that will require verified customer identification, suspicious activity reporting and regular supervision by the Internal Revenue Services' (IRS) Bank Secrecy Act Division, to which the Financial Crimes Enforcement Network delegated authority according to federal regulations." E-Gold and G&SR were closed down until they could come into compliance. They have never reopened.

The transcript of the sentencing hearing (*U.S. v. E-Gold* 2008: 14) provides troubling evidence to support the view that E-Gold was being prosecuted, or at least a heavier sentence was being requested, in part because of Douglas Jackson's free-market "philosophy," his daring to challenge *in words* the wisdom of the established government-regulated money and banking system. Judge Rosemary M. Collyer posed the following question to prosecution about the sentencing memo the federal government had submitted to the court:

> You say E-Gold was found [*sic*] at least in part based upon a philosophy that opposed government regulation of financial institutions and the banking industry. E-Gold's founders and principals blindly followed that philosophy to the point of ignoring for over a decade laws designed to protect citizens from precisely the types of criminals that require anonymity. What do you mean when you say that it was founded on a philosophy that opposed government regulation?

Jonathan W. Haray, assistant U.S. attorney, responded:

> Your Honor, the government bases that largely on public statements made by Dr. Jackson, who has provided public statements, some that are available or have been available on E-Gold's own website. . . . I'm referencing some interviews that were done with *Business Week Magazine* or *Business Week* online where Dr. Jackson was very candid I think about his view of his vision for the company which was to create a

> system of, sort of a version of a financial institution that didn't have government regulation. And that he derided the U.S. banking system because of the involvement of U.S. banking regulations and laws.

Another member of the prosecution team, Laurel L. Rimon of the U.S. Department of Justice (*U.S. v. E-Gold* 2008: 95), seemed to acknowledge that the applicability of existing legal restrictions to e-gold was unclear, but that the federal government intended to make an example of E-Gold to send a message:

> E-gold is the most prominent digital currency out there. It has the attention of the entire world. That world is a bit of a wild west right now. *People are looking for what the rules are and what are the consequences.* Criminal activity runs rampant. It's important that this case be seen as making a clear statement that if you are a person who knowingly facilitates and conducts funds transfers with dirty money, you're going to pay the price [Emphasis added].

Judge Collyer (*U.S. v. E-Gold* 2008: 112) spoke to the ubiquity of government control over money and payments:

> I have no doubt that Dr. Jackson has respect for law. He wanted to set up a currency system that avoided government oversight. That's clear what he wanted to do. He thought he could do that. Turns out he couldn't.

In her sentencing memorandum (*U.S. v. Douglas Lee Jackson* 2008: 3), Judge Collyer acknowledged that E-Gold "conceptually, is not illegal" provided it acquires a money transmitter license and operates under its customer identification and transaction reporting requirements.

Douglas Jackson tried for several years to bring E-Gold Ltd. and Gold & Silver Reserve into compliance with federal and state restrictions on money transmitters. He discovered a Catch-22 that nobody at his sentencing seems to have anticipated: He could not get a license as a money transmitter in Florida or elsewhere because he was now a convicted felon. In a recent interview, Jackson (2012: 6) told an interviewer that he was winding up E-Gold and G&SR, and had incorporated a new firm to try to license what he called "the intellectual property underlying the e-gold system" to "a financial institution or agency, whether new or established, that is fully acceptable to regulators and licensable in the various jurisdictions." As of November 2013 no successor firm had yet appeared, but I am told that eventual success is expected. In December 2010 Jackson (2010) announced on E-Gold's blog the approval of a plan for the release of frozen account balances, requiring the account holder to complete "an agreed upon customer identification process." Due to a variety of obstacles, the actual claims process was not launched until June 2013 and is presently ongoing (Jackson 2013b).

The regulatory closure of E-Gold and G&SR, the convictions of Douglas Jackson and associates, and the far-reaching powers of federal officials to which these events testify, has had a chilling effect on the "digital gold currency" industry. Crowne Gold, based in Nevada, closed its operations in 2008. In July 2011, the Treasury's FinCEN issued revised regulations that require digital currency firms doing business with U.S. citizens, even if domiciled outside the United States, to register as "Money Services Businesses," which means incurring sizable upfront costs and ongoing reporting obligations to remain in compliance. GoldMoney.com, domiciled on the English Channel island of Jersey, closed its balance-transfer service in December 2011 due to what it called the "global increase of compliance requirements for payment service providers" (Expat-World 2011).[15] The digital gold payment service iGolder, registered in Belize, closed its operations in August 2013. Its website (www.igolder.com) now announces: "During the past months, we have been recommending Bitcoin more than our own payment system. . . . Since iGolder has a central point of failure (our server may be raided by thugs wearing some kind of uniform), we feel it is safer for us to cease operations."

Only a few online payment firms appear to remain in business that allow transfers of gold units between account holders (as E-Gold did): E-dinar, based in Dubai; Pecunix, based in Panama; Perfect Money, also based in Panama; and c-gold, based in the Seychelles. Each requires strict identity verification to open an account.

[15]GoldMoney continues to provide online purchase and physical storage of precious metals.

The policy lesson of the E-Gold story is that anti-money-laundering laws and money transmitting licensure requirements in the United States—and the discretion given to their federal enforcers—are serious entry barriers to any domestic gold-based online payment system, apparently to the point of being completely prohibitive. To be frank, the laws are tools of state surveillance. They are prior restraints of citizens' liberty, applied *before* any crime has been detected. They are accordingly, as Paul Rosenberg (2012) argues, objectionable on human rights grounds.

From a pragmatic or consequentialist perspective, a billion dollars in compliance costs is not worth it if it yields less than that in the value of crime reduction. We would need a fair and comprehensive cost-benefit study of these laws and their application to new online gold payment services before we conclude that the laws are worth having in their present form. Such an analysis would need to take into account both the static loss of preferred payment options and valued financial privacy for law-abiding customers, and the Kirzner (1985) dynamic cost of suppressed payment system innovation. International payments via E-Gold-type services are easy, instantaneous, and final, and account-to-account transfer payment fees have been well below those of payments via Western Union, credit cards, or bank wire.

The compliance expenses of "know your customer" rules and associated transaction reporting requirements inevitably increase the price of payment services to consumers. In other areas of life where the costs and benefits of crime prevention are internalized, as by the owners of supermarkets and shopping malls, we do not generally see a policy of requiring IDs before allowing access.

Conclusion

The legal barriers to open currency competition in the United States are not only (1) the legal tender laws to the extent that they render it doubtful that a U.S. court would compel specific performance of a nondollar contract, (2) capital gains taxes and state sales taxes on precious metals, and (3) the statute(s) banning private coinage. Clearing away the legal barriers to a parallel monetary standard, as the case of e-gold shows, must also include (4) elimination of any aspects of anti-money-laundering laws, bank secrecy laws, or money-transmitting licensing requirements, or their application by federal enforcement agencies, that discriminate against payment systems that use nondollar units. This last barrier is becoming ever more salient as FinCEN moves to restrict Bitcoin and Bitcoin exchanges (Lee 2013, Ferrara 2013).

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